

# The A to Z of investment in 2010



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**By Jeremy Gardiner, director, Investec Asset Management**

## **Africa:**

Increasingly being seen as the next India. By 2040 Africa's workforce should exceed China's and India's<sup>1</sup>. Will apparently produce more oil than North America next year and should produce roughly 20% of global oil by 2020, up from less than 10% today.

## **Brazil:**

Not all countries have to be austere. Brazil, almost insensitively in a world where people are cutting back on food because of austerity measures, recently introduced tax-deductible boob jobs. Maybe it's good for tourism – apparently evidence of these tax deductions is abundant on Brazil's beaches.

## **China:**

Now the world's largest exporter, they consume more cars than the Americans; they have the world's largest foreign exchange reserves at \$2.4trillion and they are nearly the world's largest economy<sup>2</sup>. They have the world's largest army and they are significantly increasing naval and air forces. Need we say more?

## **Dollar (US):**

Influenced by a cocktail of negative factors. US Government finances are shot and the world has had it with the dollar. Almost two-thirds of China's reserves sit in dollars and they want out.

## **Euro:**

Will it collapse or won't it? Basically, it's up to Germany, who are enjoying the euro as it is weaker than the Deutsche Mark would have been, thereby bolstering their exports. It's different for the PIIGS; they would love a weaker currency as it would save their economies, but if they went back to their old currencies and devalued, their debt – which is denominated in euros – would double overnight.

## **Football World Cup:**

A huge success, rebranded South Africa by showing the world our first world infrastructure and showing that you can come here for a two-week holiday and not get attacked. Expect a significant influx of tourists starting next year, with a lot more US and Asian visitors than before. If you think that a 30-second TV ad during a primetime sports event like the World Cup costs approximately \$250 000, we had every newspaper, magazine, TV and radio pumping out positive stuff on us for an entire month. You can't put a price on that!

## **Greece:**

In Greece it appears paying tax was almost voluntary. Only fifteen people admit to earning over €1 million, while according to tax returns the wealthiest suburb in Athens has 324 swimming pools, even though an aerial photo revealed 16 974! Greece loses R232bn per annum because of tax evasion<sup>3</sup>. They retire too early and their pensions are too generous. They have been saved for the moment with another loan, but it will take public debt from 120% to 150% of GDP. Giving Greece another loan is tantamount to giving an alcoholic another drink – they may feel better over the short term but it's going to take a lot more to fix the problems over the long term.

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## Home loans:

Home lending in the US is at a quarter of 2003 levels, effectively back at 1993 levels. Roughly a quarter of all mortgages in the US are under water, i.e. you owe more on the house than it's worth – in Florida, that number is approximately 45%.

## Ireland:

Going to need all the help they can get. Ireland joined the Eurozone with German interest rate levels at roughly 2%. People borrowed every cent they could, fuelling a massive property bubble. On top of that, Ireland pegged corporate tax at 12.5%, resulting in a massive influx of corporates. Unfortunately, all good things eventually come to an end – commercial property fell 65% and house prices halved. The youth is leaving as are all the Polish and other immigrants, further exacerbating the housing surplus.

## JSE:

While US stock markets went sideways for the last ten years, the South African stock market has returned around 15% per annum over the same period. Who would have thought?

## Korea – North versus South

Appears to be more about sabre rattling from North Korea in order to gain leverage for future negotiations with the West. So don't expect a significant escalation in hostilities, although with the Jong Il family one can never be sure.

## Live longer:

There are currently 1600 centenarians in Britain alone, four times as many as thirty years ago. The reasons include medical advances, improved nutrition and better housing. There will be approximately six women to every man over the age of a hundred<sup>4</sup> – great if you're a man (as long as you're not dead!). The bottom line is: plan your financial affairs accordingly; this game could go into extra time.

## Merkel

As expected, the Germans have led a hard-working and prudent existence, while the Mediterranean countries have been enjoying a siesta. As a result, Angela Merkel is annoyed and wants Greece to start selling islands! The future of the Eurozone effectively lies in her hands.

## Nationalisation:

By all means, debate nationalisation, but at some stage the debate must end, as talk of nationalisation does not warm the hearts of foreign investors. Mining is a huge job provider and now ranks below tourism and car production in South Africa. We are slipping fast and we need to be more cognisant of global opinion. Botswana now beats SA on all measures relevant to mining.

## Obama:

The Americans have 10% unemployment, lagging growth and a burst housing bubble and they are grumpy with President Obama because he hasn't fixed America. This was evidenced in the mid-term elections, with Republicans making significant strides against the Democrats. They were naïve if they thought he could fix America in two years. President Palin is not impossible and would fare far worse.

## PIIGS:

Portugal, Italy, Ireland, Greece and Spain – all had it too good for too long. They are going to have to cut wages, raise taxes, expect less from government, work harder and retire later. It's not going to be pleasant. Expect widespread riots across Europe as a result.

## QE2:

Quantitative Easing – a politically correct term for printing money. Weakens the currency concerned, i.e. the dollar, and strengthens everyone else. Expect QE3, possibly QE4 plus European QE. In other words, it's not over yet.

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## **Rand:**

Driven by a cocktail of positive factors, including a shift out of the developed world into emerging markets, plus the fact that the rand offers a relatively high yield in a world of low interest rates. Also, it is a commodity currency and finally, from a government finances perspective, we are in better shape than most. So looks like 'stronger for longer'.

## **South Africa:**

Economically, in great shape. We are growing while others are slowing. Our debt to GDP is below 35% (versus 80% in the UK and 100% in the US); our budget deficit is 5.2% (versus 11% in the UK); we have no subprime; inflation is near the bottom of the 3% to 6% range and interest rates could drop another 50 basis points. Give credit where credit is due – government finances have been remarkably well managed for the past sixteen years.

## **TARP:**

Originally expected to cost \$700bn, the Troubled Asset Relief Program will cost less than a tenth of that at approximately \$25bn<sup>5</sup>, because the auto and insurance company rescues were far cheaper than expected. The taxpayer will in fact make \$6.8billion profit from the rescue of Citigroup alone.

## **US economy:**

Starting to benefit from dollar weakness, thereby making their exports more competitive. Americans are also entrepreneurial by nature, so don't write them off. They will be back, but probably not as the world's only superpower.

## **Volatility:**

Expect more and get used to it. The world is not fixed and while certain parts of the world will prosper, others will continue to threaten collapse.

## **What should you be doing?**

Interest rates will stay lower for longer, so cash returns will remain poor. Bonds will at least offer a yield but are not without risk. So by default, investors will wind up overweight in equities. Watch out for bubbles and make sure you're diversified. It's going to be tricky going forward.

## **Xchange controls:**

At R4 million per person per annum, exchange controls are essentially a thing of the past. Given the fact that the rand and South African markets have outperformed so magnificently over the past ten years, South Africans are jaundiced towards offshore investment. Don't be – use this opportunity to diversify.

## **Yuan:**

Artificially managed, kept low to keep the Chinese export dream alive. Impossible to compete against and they ignore American requests to allow the yuan to strengthen.

## **Zimbabwe:**

Economically stabilising and even recovering, despite the political stalemate.

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<sup>1</sup> UN World Population Prospect: McKinsey Global Initiative

<sup>2</sup> Financial Times

<sup>3</sup> RMB MorganStanley

<sup>4</sup> Office for National Statistics (UK)

<sup>5</sup> Congressional Budget Office

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