

Economic Views for Investors

by Roger Nightingale

The economics numbers are getting less bad

After declining precipitously in the second half of 2008, the world economy – its industrial component in particular – seemed to stabilise in the spring of 2009. By then, inventories had been reduced to satisfactory levels. Output was no longer required, therefore, to run significantly below sales.

White noise?

But was there anything else going on? Was the resilience wholly cyclical, or was it partly secular? Close to the event, of course, it's difficult to tell: the two phenomena are all but indistinguishable. In the States in the thirties and in Japan in the nineties, there were many instances of the one being interpreted as the other.

A cyclical recovery? Or a secular one?

Governments and investors both hope the new stability is indicative of longer term recovery. But it would be wise to be cautious. It's not until the next cyclical downturn, due early in 2012, that we'll know for sure how things have been going. In the meantime, worryingly, the auguries are far from favourable. There are a number of considerations that threaten to blunt near-term resilience and, if they persist, to emphasise longer-term debility.

It's unlikely to be robust

Employment is a particular anxiety. In Europe and Asia, the extent of job cuts hitherto has been negligible. GDP may have fallen by 4%, but the number of workers has been reduced by less than ½%. Why the disparity? Probably because employers had hoped that activity would rebound fast enough to obviate the need for redundancies. It hasn't. Accordingly, in the next year or so, though there might be something of a cyclical upturn, the likelihood is that unemployment will soar.

Employment is going to be too weak

How will that affect consumer spending and personal sentiment? Adversely. And the problem will be intensified if pay settlements continue to moderate. In Japan, in the last twelve months, salaries have declined by 1½%. In the UK and US, net of bonuses, they have trended sideways. Six months hence, negatives may have become universal. Young workers, those who've never known recession, those who've never known the indignity of being jobless, will be traumatised and their spending will implode.

And real interest rates too high

Real interest rates are another worry. In the last twelve months, inflation has fallen faster than the nominal cost of credit. The authorities misjudged the situation hopelessly: central bankers being too cautious and commercial bankers too greedy. The result now is that borrowing costs are penally expensive. Consumers and industrialists are encouraged to defer their spending and raise their saving.

Public spending will be reined in

It's bad enough now. But it'll get worse as the months go by. Currently, many countries are engaging in mindless public spending. But the recklessness won't last forever. As taxpayers make their views known, the process will be halted. Then, civil servants and local authority workers will start losing their jobs.

And housing will turn softer

Housing may see another dip. It's likely that mortgage lenders will find that much of what they've done in the last twelve months has unravelled. The borrower turned out not to be safe because he lost his job. The 75% mortgage turned out not to be secure because the house price fell more than 25%!

Are politicians to get their just deserts? Sadly, No

The political repercussions will be considerable. Even if they'd behaved honourably, incumbent governments would be blamed for the economy's failings. The fact that they haven't will just make the retribution worse. In elections that lie ahead, the installed rascals will be uninstalled – and the alternates given a chance.

Will stock markets carry on rising? Probably, Yes

The securities markets, meanwhile, will probably rise. They've been cheap for a long time already, but investors have been too frightened by the prospect of depression, bankruptcy, pestilence and famine to take a stand. That may now be changing. Corporate results have been satisfactory and net purchases have begun. Indices have been volatile, but trending upwards.

Pensioners might have to man the barricades!

Good news for the poor pensioner. Let's hope the news-flow stays favourable. Let's hope the loathsome public sector pensions (those of MPs most particularly) are re-jigged – lightening the burden on the productive part of the economy, lowering the rewards for the unproductive part. If, additionally, the retirement age were to be raised (to 68 for the former, to 70 for the latter), justice would have been done. And there'd be dignity in superannuation for the good guys.

Contact us... Visit our website www.sippolutions.com for further information on our SIPP products and services. Alternatively, contact Roger Nightingale on 01858 419300 or email nightingale@sippolutions.com or visit www.rogernightingale.com.

Disclaimer

This document is the opinion of Roger Nightingale and does not represent the opinions of Pointon York SIPP Solutions and is for your private information only. We are not soliciting any action based upon it and whilst information contained herein is based on sources we believe to be reliable, its accuracy is not guaranteed and may be incomplete. Any opinions expressed are Roger Nightingale's current opinions as of the date appearing on this material only and are subject to change without notice and might not be followed up on a specific ad-hoc document. This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of clients of Pointon York SIPP Solutions. Investment professional use only. Not for public distribution.