*(Contribution for UpDate no.6, 2015)*

PERSONAL FINANCE

# EXPERTS' VIEWS IMPLY MORE HARD TIMES FOR SAVERS

Each year around October time I attend an annual gathering, usually in London, of a Think Tank of top fund managers who are responsible for the allocation of billions of dollars of investors' money. The object is to glean as much as I can from experts in different areas of the business in order to get an overall picture and understand the differing views that give us some idea of where we are and where we might be going.

This year the event included experts from the likes of Schroder and BlackRock as well as the host company Momentum, some elements of whose round-up I am including here. 'Why should this be of interest to me?' I can hear some people say as this might seem a long way from the realities of living or working in Indonesia or any other location away from the world's financial hubs. The reason is there are implications for anyone who has any kind of investment, savings or pension scheme or who has a mortgage or has to consider what currency to hold for the best. It can also have an impact on what financial decisions should be taken in the future. Before we consider this impact let me review some of the salient messages that emerged, most of which explain why we are seeing our cash languishing in banks and investment gains, if any, barely covering product and management charges.

***Debt has risen, not fallen, since the 2008 financial crisis***

Total debt, excluding the financial sector has increased by 36 percentage points to 265% of GDP in developed economies since 2007. It has increased even more rapidly in emerging economies where debt has risen by 50 percentage points to 167% of GDP. In China, debt has risen from 149% of GDP to 240% since 2008, but with a difference as the debt has been in the household and corporate sectors, whilst it is the government sector that has taken on debt in the developed world. Of course, governments have encouraged debt to stimulate growth and sustain employment numbers, which in turn keeps people happy and the same governments in power. But when

debt gets out of hand the result is tight credit, reduced spending, debt defaults and wealth destruction.

We are seeing a new phase of the post-2008 crisis world. First we had the property and banking collapse in the Anglo-Saxon world, then the Euro crisis and now the emerging markets are falling due to the collapse in commodity prices and the slowdown in China. Emerging countries now account for 40% of global GDP so when China and the rest of the emerging world slow it has a very significant impact on global growth.

***So what is happening in China?***

Forty years ago what happened in China had no meaningful impact on the rest of the world. But in the past 40 years China's economy has expanded by thirty times. I recall visiting China in wintertime in the early eighties when it could only be described as a fairly primitive rural economy that seemed way behind Indonesia in development. Hot water in my hotel was available for only 10 minutes early in the morning and overcoats were necessary in the unheated restaurant. I quickly adapted to using chopsticks as there was no cutlery! But on a more recent visit it had become an economic powerhouse. I saw no more horses and carts as I rode the Maglev in Shanghai at 400 kph.

But China's rapid development has come at a cost, and clearly there has been misallocation of capital. The Maglev is impressive but are there not other priorities? It is ironic that China was keen to bid for a bullet train project between Jakarta and Bandung and I think it a wise decision of President Jokowi to scrap the idea in favour of more pressing, albeit less prestigious projects. I recall that when I stepped off the Maglev which stopped well short of the city centre I had to carry my bags down a flight of steps and wait for a taxi in the rain. A thought perhaps for the developers of the MRT; unless there is a sound infrastructure of transport and pedestrian access around it there will not a great incentive for people to abandon their cars and motorcycles.

But I digress. Recent attempts by China to sustain the boom such as the recent stock market manipulation and currency adjustment backfired. There are likely to be more problems ahead as the country tries to adjust to the realities of excessive debt, over-capacity and an ageing workforce. At the same time one should not write off the country's ability to keep growing; its latest measure

(announced since the conference) to allow families to have two children as opposed to one well help to stem the deteriorating demographics.

Speakers did not consider we were seeing a rerun of the 1997 Asian crisis as foreign currency reserves are much stronger now but the slowdown is producing a reversal of the capital flows seen over the past decade and in turn is putting pressure on currencies across the developing world (as we have seen with the Rupiah).

***An increase in Fed interest rates – Sword of Damocles?***

Fears of the first US Dollar interest rate for several years has spooked stock markets and currencies for the past 18 months. Every time the US economy has shown a hint of strengthening and the markets have sensed a rise is imminent the US Dollar has risen and markets have had the jitters, only to recover again when the likelihood subsides. It was interesting to see that speakers had differing views on when the 'dreaded' increase would be announced. Some thought it could still be this year, others thought not till next year with even a possibility that it would not occur then. For the Fed it is a dilemma; higher interest rates are necessary to ensure a return to more 'normal' market conditions, yet a premature increase could cause the US to fall back into recession, taking much of the world with it.

At the time of writing employment figures in the US were looking positive so those predicting a December rate rise were in the ascendency again.

***So where does all this leave confused investors?***

Firstly perhaps with the realisation that it will be a long time before cash in the bank will pay a meaningful return. Those seeking higher interest rates by putting money into weak currencies have seen the consequences over the past year. US Dollar bonds issued by the US Treasury are perceived to be the safest of havens but don't expect a return in real terms from them. Their main benefit is the capital protection. We have had a rough ride in the stock markets in recent months and this is likely to prove another underperforming year with many countries ending negative, but history still tells us that this is where the long term money should be so we must hang in, expect a bumpy ride and not be too ambitious with our expectations. Regular savings plans are still one of

the best ways of turning volatity to your advantage; every time the markets fall your regular contributions are getting a ‘discount’ but you must stick with the plan for the long term.

Property is normally a sound long term investment also but try not to buy when everyone else is buying and don’t sell when everyone else is running for the doors! If you have a mortgage at the moment be prepared for interest rate rises to follow any that emerge from the US. Usually when interest rates rise property values fall.

Above all perhaps, be aware that governments will be less able to support pensions in the future and with the likelihood that investment returns will be limited for some time it may be wise to spend less and save harder for the future. Be like a squirrel and prepare for a long winter. If the sun still shines, it’s a bonus!

***Colin Bloodworth, Chartered Member of the CISI,*** *has spent over 20 years in Indonesia. If you have any questions on this article or related topics you can contact him at 021 2598 5087 or colin.bloodworth@ppi-advisory.com*