



Investment Insight

Friday, 14 July 2017

Here's to the future. While we always advocate taking a long term view when investing in risk assets, few of us have a 50 year time horizon, so this week's **Inside Track** is most likely of more interest to the next generation.

In a recent commentary, Kaushik Basu, former Chief Economist of the World Bank outlines his views as to how he sees things playing out in 50 years' time. As you will see his expectations are pretty optimistic; however, it is also worth noting that he is unlikely to be around to face the critics should his views not play out!

Hong Kong Phoney. Towards the end of last month the share prices of a considerable number of small cap Hong Kong firms, crashed, losing over \$6 billion in value. As confidence in the sector disappeared some stocks fell over 90%.

In a report issued almost two months ago, David Webb, a former director of the Hong Kong stock exchange, was convinced the writing was on the wall and it was just a matter of time before what happened, happened. In his report Webb claimed that the shares were owned by the same group of people and as Reuters noted, "Webb's report mapped out a complex web of cross-shareholdings between companies...".

This resulted in a domino effect when the selling began. As this week's **Pic of the Week** illustrates, the complex map of share ownership in these highly illiquid smaller companies is startling.

Quoted...

"A bank is a place that will lend you money if you can prove that you don't need it." – **Bob Hope**

The Inside Track

Kaushik Basu, former Chief Economist of the World Bank, is Professor of Economics at Cornell University and Non-resident Senior Fellow at the Brookings Institution. The following are extracts from his recent commentary.

The world is experiencing a slow-motion economic crisis – one that, most experts agree, will continue for the foreseeable future. The global economy has grown in fits and starts since the economic crisis of 2008 – one of the longest recorded staginations of the modern era. In virtually all middle- and high-income countries, wages (as a share of GDP) have been steadily declining for nearly 40 years. But what about the next 50?

Today, the situation certainly looks bleak. Economic stagnation and widening inequality have contributed to a surge in xenophobia and nationalism in the advanced countries, exemplified by the United Kingdom's vote to exit the European Union and the election of US President Donald Trump – and now his decision to withdraw from the Paris climate agreement. Meanwhile, large parts of the developing world – notably, the Middle East and North Africa – have been embroiled in conflict, with some teetering on the edge of state failure. But while such turbulence is likely to continue for the near future, there is little consensus on what lies beyond that. To be sure, long-run forecasting is usually a fool's errand. In 1930, in similarly troubled times, none other than John Maynard Keynes tried his hand at it, with the famous essay "Economic Possibilities for our Grandchildren." He got his forecast wrong.

Nonetheless, Keynes's attempt surely sets a respectable precedent for economic future gazing. So here I go: in 50 years, I predict that the world economy is likely (though not guaranteed) to be thriving, with global GDP growing by as much as 20% per year, and income and consumption doubling every four years or so. At first, this scenario probably seems farfetched. After all, the global economy currently is growing at a rate of just 3% annually (a bit worse, in the last few years). But it wouldn't be the first time global economic growth accelerated to previously unimaginable levels.

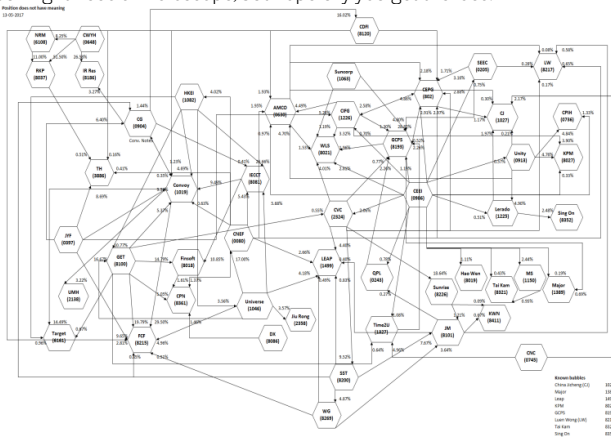
From 1500 to 1820, according to data collected by the late Angus Maddison, the world's annual growth rate was just 0.32%, with large sections of the world experiencing no growth at all. In China, annual per capita income stood at \$600 throughout this period. For someone living at that time, today's disappointing 3% growth rate would have been inconceivable. How could they anticipate the Industrial Revolution, which lifted average annual global growth to 2.25% from 1820 to 2003? Today, it is the Digital Revolution that promises to lift growth to new heights. Indeed, we are in the midst of dramatic technological breakthroughs, with advances in digital technology connecting all corners of the world. As a result, workers are not just becoming more productive; they are gaining greater access to employment. Individuals in developing countries, for example, are now able to work for multinational companies. The upshot is that more workers are participating in the labor market. The economic effects of this trend have not been all positive. In the United States, for example, the average real (inflation-adjusted) wage has barely risen, even as unemployment has fallen to 4.3%. By enabling lower-wage workers abroad – and, increasingly, machines – to do more jobs, technology has reinforced this "maximum wage ceiling."

The key to breaking through this ceiling is to change the kinds of work in which people are engaged. Through improved education and training, as well as more effective redistribution, we can facilitate more creative work – from art to scientific research – which machines will not be able to do in the foreseeable future. Though such work may seem wasteful, owing to the number of people and amount of time it takes to secure one major achievement or breakthrough, one such achievement or breakthrough is all it takes to create enough value to boost everybody's standard of living. And, indeed, as the creative sector grows, growth will pick up substantially. This outcome is likely, but it is not certain.

Consumption patterns will also need to change. If, as overall consumption doubles every four years, we also double the number of cars on the road or miles that jets fly, we will quickly exceed the planet's limits. This is all the more true given that rising life expectancies will not only compound population growth, but also increase the share of elderly people. The right incentives will be needed to ensure that a large share of our wealth is directed at improving health and achieving environmental sustainability. If we do not manage such policy shifts in the coming years, the world economy will probably swing to the other extreme over the next 50 years. In such a scenario, 2067 would be marked by even greater inequality, conflict, and chaos, with voters continuing to choose leaders who take advantage of their fears and grievances. What I believe can be ruled out is a middle ground, with the world looking roughly like it has over the last 30-40 years.

Pic of the Week

You might need a microscope, but hopefully you get the idea.



Week ahead: Key events

- 17/07 China GDP & Industrial Production
- 17/07 US Manufacturing
- 18/07 China Property Prices & Eurozone CPI
- 19/07 US Housing Starts
- 20/07 UK Retail Sales & US Initial Jobless Claims
- 21/07 Japan Department Store Sales

Market View

	Last 7 days	Last 12 mths	YTD	5Y Ann.
Global equities	+1.3%	+14.7%	+9.1%	+10.6%
US equities	+1.6%	+13.1%	+9.3%	+12.5%
European equities	+1.5%	+13.9%	+6.4%	+8.0%
EM equities	+3.8%	+20.2%	+20.7%	+2.4%
Irish equities	+0.8%	+18.1%	+5.9%	+16.7%
Commodities	+0.2%	-8.9%	-6.3%	-10.2%
Hedge funds	+0.4%	+5.4%	+3.0%	+1.9%

Economic indicators	Bond yields	Inflation	GDP YoY
Ireland	+0.9%	-0.4%	+7.2%
Germany	+0.6%	+1.6%	+1.7%
USA	+2.3%	+1.9%	+2.1%
China	+3.6%	+1.5%	+6.9%

Currencies	Current	YTD Δ
EUR:USD	1.14	+8.4%
EUR:GBP	0.88	+3.2%
EUR:CNY	7.73	+5.4%
GBP:USD	1.29	+4.9%
Bitcoin	2,312.71	+142.9%

Commodities	Current	YTD Δ
Gold	1,216.06	+5.5%
Copper	5,853.50	+6.0%
Oil	48.32	-17.9%
Wheat	516.50	+15.4%

Central Bank rates	Current
Eurozone	0.00%
USA	1.25%
UK	0.25%

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