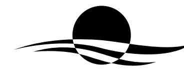
Growth STRATEGIES

Trend Analysis That Builds Business Decisions



LA JOLLA INSTITUTE
Steve PonTell

Dr. Roger Selbert, Editor & Publisher
E-mail: roger@rogerselbert.com

3200 S. Barrington Ave. #4 • Los Angeles, CA 90066
Telephone: (310) 721-6322

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1 – GLOBAL ECONOMIC SENTIMENT

Indicators of consumer and investment sentiment are used by international corporate and portfolio managers as ways to measure when to put money to work. When sentiment is negative, investors tend not to invest for fear of logging quick losses to capital. And right now, investor sentiment is negative.

According to the annual Global Economic Conditions Survey, which polls financial officers in small and mid-sized firms in the US and around the world, there are no signs that the global economy is coming out of the doldrums. According to these global accountants, we are faced with strong negative trends in the world economy that are likely to persist well into 2013.

What's weighing sentiment down? In the US, it's lackluster housing and job markets. In the UK and Europe, it's the ongoing problems with bank liquidity and sovereign debt. Even China appears to be retrenching. Much of the apparent global recovery in early 2012 has dissipated. The mood has soured in the US, and investor confidence is even worse than consumer confidence.

To be sure, economic fundamentals have deteriorated in the core economies, particularly the US and Europe. But it is this retreating optimism that is responsible for most of the drop in business confidence in the second quarter, according to the survey of accountants from around the world.

On the other hand, those companies and investors that are putting money to work now have a longer term view of particular markets. Perhaps they see some of the more positive trends we highlight in the following items.

2 – INVESTMENT OPPORTUNITIES

Calamos Investments, a global investment management firm, recently released its Global Economic Review and Outlook. Here is a synopsis:

GLOBAL OUTLOOK

- **Political volatility stokes market volatility.** Intense political confrontations in the US, Europe and China will contribute to volatility throughout the global financial markets.
- **Emerging markets continue to grow, albeit more slowly.** Emerging markets should continue to contribute to global GDP growth, even if at a slower pace than recent years.
- **US stays on a slow-growth track.** Economic data continues to affirm that the US will avoid a double-dip recession. Although employment data remains bleak, consumers are doing the right things to support the economy – deleveraging and spending.
- **The Eurozone remains a source of volatility.** The Eurozone crisis is being recognized as more than a liquidity issue. While this is encouraging, far more needs to be done and the road ahead is long, difficult and unclear.
- **Ultimately, the pace of growth should correlate with fiscal restraint and expanding**

economic freedoms. Expect uneven growth from country to country as some nations adapt more readily than others to evolving sovereign relationships. Sound fiscal policies and expanding economic freedoms, such as fair trade and reasonable regulations, can help countries capitalize on the opportunities of globalization.

INVESTMENT OPPORTUNITIES

- **Equities are highly compelling.** Equities remain the most attractive asset class in the current environment, particularly growth equities. Investors remain overly pessimistic about the prospects for growth companies, and we believe many equities are notably undervalued.
- **Mid-grade corporate bonds remain attractive.** Even though inflation is low today, history has shown that it can rise rapidly and unexpectedly, a particularly detrimental scenario for holders of longer-term government bonds. Meanwhile, given a slower-growth environment, lower quality corporate bonds may not be providing appropriate compensation for risk. However, we continue to find attractive risk/reward among select mid-grade corporate credits.
- **Global businesses provide access to secular growth.** Broadly speaking, global companies with geographically diversified revenues and healthy balance sheets may be best positioned to grow on the back of secular trends, especially those related to emerging markets. Moreover, these companies have the flexibility to go where capital is treated best.

3 – CITIES AND THE RISE OF THE CONSUMER CLASS

Cities have long been the world's economic dynamos, but today the speed and scale of their expansion are unprecedented. Through a combination of consumption and investment in physical capital, growing cities could inject up to $30 trillion a year into the world economy by 2025. Understanding cities and their shifting demographics is critical to reaching urban consumers and to preparing for the challenges that will arise from increasing demand for natural resources (such as water and energy) and for capital to invest in new housing, office buildings, and port capacity.

So concludes a new report from the McKinsey Global Institute, Urban world: Cities and the rise of the consuming class.

McKinsey finds that the 600 cities making the largest contribution to a higher global GDP will generate nearly 65% of world economic growth by 2025. However, the most dramatic story within the City 600 involves just over 440 cities in emerging economies; by 2025, the Emerging 440 will account for close to half of overall growth. One billion people will enter the global consuming class by 2025. They will have incomes high enough to classify them as significant consumers of goods and services, and around 600 million of them will live in the Emerging 440.

The world's center of economic gravity has changed over past centuries. But since the mid-1980s, the pace of that shift – from the United States and Europe toward Asia – has been increasing dramatically. This trend is expected to continue.

4 – THE DECADE OF THE CIVETS

The past decade was all about the BRICs, the massive economies of Brazil, Russia, India and China, which kicked off at the beginning of the new century, boomed and are now slowing like

the rest of the developed world. Taking their place is a new group of fast-rising economies promising businesses outsized returns.

The next decade could belong to the CIVETS – Colombia, Indonesia, Vietnam, Egypt, Turkey and South Africa – whose rising middle class, young populations and rapid growth rates make the BRICs look dull in comparison.

So writes Deborah Stokes on web site [Business without Borders].

The BRICs are yesterday's news, she reports. Hardly emerging economies anymore – China is the world's second largest economy and Brazil will take seventh place this year – it was inevitable that their pace of growth would slow down.

Now more connected by trade to the developed economies, the BRICs are feeling the same slow-down effects as the developed economies. And in the case of China and Brazil, they are also wrestling with the strains of their rapid ascensions. Real estate bubbles, currency control issues and hyper-wage inflation are sending global companies elsewhere for growth.

Brazil is forecast to grow a mere 3% this year. China, while still targeting a strong GDP growth rate of 7-8% in 2012, is well off its double-digit rates of the past decade. Russia, meanwhile, which can't kick its dependency on oil exports and endured the retrograde re-election of Vladimir Putin, may grind out 3.2% growth this year. India is also slowing, with a GDP target of 6.9% growth in 2012, a sharp decline from its 2010 pace of 9.6%.

The CIVETS, meanwhile, are at the lift-off point. The six countries in the group are posting growth rates higher than 5% – with the exception of Egypt and South Africa – and are trending upwards. Lacking the size and heft of the BRICs, these upstarts nevertheless offer a more dynamic population base, with the average age being 27, soaring domestic consumption and more diverse opportunities for businesses seeking international expansion.

5 – AFRICA EMERGENT

One of the unfortunate consequences of the well-advertised "bad news" out of Africa concerning some very real conflicts and the lingering authoritarian tendencies on the part of a few regimes is that most of the continent's "good news" tends to get eclipsed. But Africa is home to six of the world's fastest-growing economies over the past decade and as a whole, Africa is expected to grow faster this year than any other region or country, apart from China and India. Having rebounded quickly from the recent global contraction, Africa is on track to see a total gross domestic product of $2.6 trillion by the end of this decade. Far from being a fluke, these positive indicators are the result of significant forces which have been at work transforming Africa's economic prospects and, ultimately, its social and political landscape.

So writes J. Peter Pham on web site [Diplomatic Courier]. He outlines these forces:

First, Africa is not only one of the most populous regions on the planet but one of the youngest; the size of the African workforce is growing more rapidly than its counterparts elsewhere. These demographic trends, when coupled with robust economic growth, will lead to the emergence of a solid consumer base, especially in countries that invest in a skilled workforce. Overall, the African Development Bank estimates that around 150 million Africans joined the ranks of the middle class since 1990 and another 40 million will join them by 2015.

Second, Africa's population is rapidly urbanizing, thus adding further impetus to positive economic

growth. Around 40% of Africans currently live in urban areas, but given current rates of urbanization – the fastest-growing in the world – that number will be slightly more than half by 2030 and well over 60% by 2050. Already, Africa has 49 cities with a population over 1 million; there is a clear and mutually reinforcing relationship between urbanization and economic growth.

Third, Africa has embraced recent technological innovations with alacrity, using them to "leapfrog" traditional stages of development. Nowhere is this more evident than in mobile telephony. The number of subscribers has mushroomed from almost none in the mid-1990s to 15 million in 2000 to 88 million in 2005 to over 500 million in 2010; by 2015, it is estimated that there will be nearly 800 million.

Fourth, Africa's financial services sector has grown rapidly in response to its changing economic landscape as rapid urbanization, rising incomes and technological advances bring more people – many of whom were formerly locked out of the formal financial system – into contact with banks and other similar institutions. The expansion of the financial sector not only creates new jobs and other economic opportunities, but it helps establish formal identities for millions of market participants and it provides greater security than the current cash-based transactions.

Fifth, demand for Africa's natural resources, the initial key driver for the economic boom in many countries, remains a powerful force. Demand for its primary commodities is boosting prices and, in turn, motivating new investment in exploration and extraction. Moreover, African agriculture's importance is also growing as demand for food by the developing world's rising and increasingly affluent populations surges even as local resources diminish.

Of course, economic potential is not the same thing as results and the history of Africa is strewn with the wreckage of once promising countries whose bad leadership and even worse policy choices reduced to little better than basket cases. On the other hand, political stability, commitment to reform, and policies liberalizing trade and markets can magnify the impact of the forces already reshaping the continent's economic, political, and social terrain. A 2010 study by the McKinsey Global Institute estimated that GDP growth accelerated three times as fast in African countries that adopted policy reforms, privatized state-owned enterprises, allowed more business competition, opened trade, lowered taxes, and strengthened regulatory and legal systems than in non-reforming countries.

If these trends continue, Africa will emerge in the coming years as a significant force in the global economy – a place where engagement is no longer driven primarily by aid and humanitarian sentiments, but rather where economic opportunities and the potential therein for mutual benefit form the basis not only for a new social contract between African governments, businesses, and civil society, but for true partnerships between Africa and its international partners.

The July Consumer Demand Index (our monthly survey of American household purchasing plans) was not encouraging. In fact, the signs of optimism among US consumers we saw in June have vanished. Our expectations are that US consumers will continue to be hesitant and just muddle through, with high energy prices, a weak labor market and political uncertainty taking their toll.

For more info go to www.consumerdemand.com