

# Be prepared for the muddle through

## Economy

The economic and financial world is in a state of turmoil. The economic news is bad. But we know this. As Charles de Kock senior portfolio manager, Coronation Fund Managers said at the recent Conversations presentation – we at least know there is some serious trouble coming our way and we have to take evasive action.

De Kock says there are three potential ways to get out of the mess and reduce the debt – the hedonist route where we spend more to get growth going – carry on spending. Here debt is seen as a symptom with the real problem being no spending by corporates and no confidence. Growth is seen as the only way out. In practice this is not proving a successful route as investors are not prepared to fund spending.

Option two to get out of the mess is the 'calvinist route' – take all the pain now and use drastic spending cuts to reduce debt. Like going on a diet, de Kock said, feel terrible while you are doing it but afterwards you will feel better.

Logically this sounds a feasible option – but economies are not rational and in practice this option has led to such low growth that growth and revenues have just shrunk too much. (Japan for example.)

The third and likely route is the muddle through – where politicians allow some pain but ultimately protect votes. This is chipping away at the problem rather than one big action. This route means is that we are likely to see a default – Greece. What does this mean for an investor?

De Kock said we are likely to see lower interest rates for longer and this does have implications for those in cash funds – for a few years real cash returns may even be negative. And eventually inflation will be a concern. In South Africa in particular the SA Reserve Bank may, in pursuit of the dual mandate of inflation targeting and growth, keep rates longer for lower. Stagflation is a possibility (low growth and high inflation). "Investors are going to have to accept sluggish returns." Tax hikes, in some form or another, are also likely.