VIEWPOINT

Healing, but some parts still hurt

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This year started with such promise. Heralded as the year the recovery would finally start to gain traction, expectations were high. The mood, however, soured quite quickly, as geopolitically the world started behaving badly.

Peace talks in the Middle East collapsed, leading to a war in Gaza; Russia invaded the Ukraine, seemingly oblivious to protestations; planes were shot out of the sky – and amazingly one plane disappeared completely. Then suddenly, a new and brutal threat arose in the Middle East in the form of ISIS, which saw the allied effort switching from last year supporting the rebels against President Assad, to this year fighting against the rebels on the same side as Assad!

We warned investors at the beginning of the year that emerging markets would continue to struggle economically, as Janet Yellen continued to withdraw stimulus from the US economy at $10bn a month. We also said that equities, although expensive, remained the place to be.

2014 has, however, also delivered a fair amount of surprises, so let's look at the world and see who's hot and who's not.

US building muscle again

The US recovery looks sustainable, despite a weaker world. Their exports are obviously hurting from a slowdown in China and the Eurozone, but that will at least partially be offset by a lower oil price and 'lower for longer' interest rates.

The lower oil price has been a welcome surprise. Essentially the oil price is a temperature gauge of the global economy, so a slower world led to a decline in demand. Furthermore, with the US now producing most of their oil and gas needs, together with increased output from previously war-torn Middle Eastern states, global supply now exceeds demand. US energy neutrality, conceivably within the next three to five years, is indeed a game changer. It will narrow their deficit, decrease their debt and make them more competitive.

In addition, their employment levels are back above the 2007/'08 peak (albeit after more than $3.5 trillion of printing!) Slower global growth will see interest rates 'lower for longer'.

Europe is still a challenge

Despite much excitement at the beginning of the year about the fact that Europe was either flat-lining or growing slightly, the IMF now sees a 40% chance of a triple-dip recession across the Eurozone, and a 30% chance of deflation. Germany – the locomotive relied upon to pull Europe out of the mess they're in – is slowing fast. The conflict in the Middle East, Russian sanctions, an emerging market slowdown – all on top of a slow and hardly recovering Europe is hurting.

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Essentially, the Eurozone needs quantitative easing and the Germans are saying no. In fact, the hardworking, prudent Germans have come to believe they are supporting the rest of Europe, and Ms. Merkel would do well to listen to calls for 'Deutschland first', otherwise she may well find herself voted out.

The Eurozone still needs attention, and the Germans are increasingly reluctant to help

Meanwhile, all is not well around the Mediterranean. Greece's debt to GDP is 176% and rising, whilst their stock market is down 40% since March. French debt is around €2 trillion, Italy is higher at €2.1 trillion, with debt to GDP at 136% and zero percent growth. So the Eurozone still needs attention, and the Germans are increasingly reluctant to help.

Britain, on the other hand, is booming. Having had their growth forecasts raised repeatedly over the past 18 months from 1.5% for 2014 to the current 3.4%, their recovery seems intact. Inflation is at 5-year lows, which is important, as it means they too should keep interest rates 'lower for longer'. Their biggest threat remains the London housing market, with central London up 80% since 2009. They recently sold a garage for R10 million, an unfurnished flat for £140 million (R2.5 billion), and 10 central London boroughs are now apparently worth more than the combined value of Scotland, Wales and Northern Ireland!

No hard landing in China

Turning to China, they have a slightly slowing economy, with expectations of approximately 7.1% GDP growth next year. Whilst rumours of problems in their property market and banking systems persist and remain a cause for concern, the absolute number of 7.1% should not be too much of a worry in itself. China's economy is enormous – and not that far off the size of the US economy – so still to be growing at 7.1% is impressive and should be seen as such. The US is scheduled to grow at 3.1% in 2015 and they're thrilled with that!

China, too, has demographic issues, with a fertility rate of 1.6 per woman. They need 2.1 to maintain their population. The UN predicts that their population will start declining by 2030. To combat this, they recently loosened their one-child policy, but of the 11 million couples who were eligible to have another child, only 3% took it up, as the costs of getting a child from birth to Beijing College are way beyond the average Chinese couple.

They're also consciously transforming their economy from being the workshop of the world, to a more consumption-driven economy. Their labour costs have risen quite significantly, and they are by no means the cheapest anymore.

Attractive Africa

Meanwhile, Africa's emergence as a preferred investment destination received endorsement from EY's 2014 Africa attractiveness survey, where only North America was seen as more attractive than Africa as an investment destination, in a survey of more than 500 clients. Africa is also a lot more stable than it used to be, with the number of countries in Africa with elected governments rising from around 12% in the 1980s to over 75% today.

Rising Chinese wages also means that low-skilled African workers can compete in terms of price with Chinese workers. So not only are the Chinese setting up more factories in Africa, but they're hiring the locals as well. Africa's population is set to double by 2050, and in order for this to be the demographics bonus that it should be, skills training and jobs will be crucial.

Of course Ebola – or more accurately Ebola hysteria – has the potential to derail the African Renaissance and upset Africa's improving image. For the countries involved (Guinea, Sierra Leone and Liberia) economic paralysis is setting in as they struggle to find anyone prepared to do business with them, let alone visit them. Isolation, leading to economic collapse if it happens, will greatly affect their ability to maintain sufficient health services, and indeed to contain further spreading of the virus.

However, panic and ignorance have stoked irrational levels of fear, with South Africa now seeing numerous cancellations by foreign tourists, most notably Chinese and Americans. This is utterly bizarre, given that West Africa is far closer to Europe (with far more regular flights) than it is to Johannesburg. Sadly though, unlike SARS which had Asian origins, this one is African, and we're going to have to get through it. Anyway, heart disease is what most people in the developed world will die of – not Ebola!

SA should tread lightly on the ratings road

It is amazing though that with Oscar, Dewani, Ebola and our new visa regulations, we have any tourists at all. The weaker rand and a pragmatic approach to visas will go a long way towards supporting one of our few job-creating industries.

SA is now perilously close to junk status

Another week, another downgrade. SA is now perilously close to junk status, which would see global pension funds, mutual funds and insurance companies unable to buy our debt. The time for action is now. For far too long we have tolerated poor leadership, trying to keep everyone happy, thereby avoiding all difficult decisions. We cannot continue like that; it's becoming too expensive. We have to get the economy growing and start creating jobs, and if the current leadership of this country is unable or unwilling to do it, then we need somebody who can. SA does not need a change of government; we simply need to put the right people in the right jobs. There are so many areas within government that work effectively – SARS, the Department of Finance, South African Reserve Bank and the Public Protector – to mention but a few, and now the municipalities under Minister Gordhan should start improving as well. Our challenge is to take the areas that are not performing, remove incompetent incumbents and replace them with experts. SA is doing OK, but we could be doing so much better and quite quickly with proper leadership – and that is what is so frustrating about being South African.

Parliament becoming more vigilant

Another week and another riot in parliament. Emigration is back on the agenda, and many are saying that this now really is the beginning of the end! My view is slightly different. We have of the freest press in the world and the SA media has clearly had enough of incompetence and wrong decisions being made. They have become vociferous in condemning bad behaviour. This, coupled with the highly effective and somewhat outspoken 'alliance' the DA and the EFF seem to have struck in parliament, I really believe, is grinding both the President and the ANC down.

For too long we have essentially had a two-party parliament. Now you have an entirely different dynamic, and I think government is realising that wrong decisions will not only no longer be tolerated, but will be very publicly punished. Appointing friends to key posts, purely on the basis of political alignment leads to enormous, expensive mistakes. This destroys our reputation, deters investment, costs jobs, and tax payers are tired of funding it.

There are more than enough great people within the ANC, but due to not being politically aligned, they're not even considered for key positions. The combination of a 'no more nonsense press' and an increasingly vigilant opposition in parliament means that real pressure is finally being brought to bear on poor leadership. This will hopefully lead to government – in order to avoid attack – choosing the path of least resistance, and making the right decisions.

Nic Borain, the political analyst, summed it up best recently when he said: "We argue that the cacophony of negative political news about South Africa leaves financial markers vulnerable to mispricing the political risk. Deep below the storm forces are at work that are likely to lead to an upside surprise and catch markets wrong-footed." The chances of a positive political surprise are more likely than a negative surprise.

So, going forward, watch the three-pronged attack: this new alignment is true democracy in action. If there is anything murky going on in and around the nuclear deal, it will be very difficult to hide without it being exposed. Whilst putting experts in charge of key posts won't solve all our problems, there's a lot that we could fix quite quickly and that will make for a calmer, happier parliament and country.

From a global market perspective, the bears are watching, but they're not growing. Expect the Europeans to 'do what it takes' in the form of quantitative easing to get their economies growing again. In addition, the combination of global growth accelerating into 2015, a significantly lower oil price, and lower for longer interest rates all should lead to a happier 2015, and that's something to look foward to.

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