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There is a pattern to all this drama

Michael Nairne, Serious Money

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Jobless men swarm boxcars for the "On to Ottawa" protest shortly after the stock market crash of 1929 and the beginning of the Great Depression. Economic downturns are cyclical, so investors must be patient to wait for things to recover.

It takes a brave soul to read a newspaper today with a steady hand. The world seems to lurch from crisis to crisis. One day it's the possibility of a financial contagion sweeping through Europe. The next, it's the spectacle of political gridlock in the United States that could lead to a debt default. Story after story recounts languishing growth in most of the developed world along with sputtering employment gains.

This torrent of bad news should be no surprise. Leading economists Carmen Reinhart and Ken Rogoff foretold the state of the developed world's economies back in 2008. Their sweeping research into the

financial crises of the past few centuries found that, instead of being an extraordinary occurrence, crises are a recurring event.

They also follow a pattern. The stage is set by a debt cycle when borrowing, often real estate-related, skyrockets. The onset of the crisis is marked by collapsing asset values as real estate prices plunge and bankruptcies soar. As asset writedowns proliferate, a banking crisis ensues. Lending and liquidity dry up, investment and consumption collapse, and a deep recession ensues.

That is only the start of the drama. As government revenues evaporate and spending jumps, deficits mount at an alarming rate. Typically, government debt soars by 86% in real terms in the three years following a crisis. Hence, sovereign debt crises frequently fall on the heels of banking crises.

Real estate prices continue to erode far after the recession is over. It takes, on average, six years for real house prices to hit a low. For a severe downturn, price declines can reach 50%. By this standard, real U.S. house prices, which have dropped about 35% from their 2006 peak, could face another year or so of decline.

Deleveraging typically goes on for seven years after the crisis. This would put us less than half-way through this painful journey. Meanwhile, the debt overhang cuts about 1% per annum from real GDP growth and unemployment rates run on average 5% higher for a full decade after the crisis.

The harsh reality is that many developed countries are only part way through a laborious retrenchment that will stretch on for years. Investors can therefore expect a steady diet of dismal news for some time to come.

Fortunately, there are several actions you can take to ameliorate this unhappy situation.

First, ensure your portfolio has a proper allocation to emerging markets. These countries are now the growth engine for the globe. This is where all the good news is; we just don't get exposed to it. Consumption by emerging-market consumers now exceeds that of the famed American consumer. Goldman Sachs estimates the BRICs will contribute twice as much to global growth through to 2020 as the United States, Germany and Japan combined.

Second, understand that lacklustre economic growth in the developed nations doesn't necessarily equate to dismal equity returns. Several academic studies have found that stock returns are more dependent on valuations than economic growth rates. Stocks are much cheaper today than a decade ago.

Third, be glad you are a Canadian and that you can stabilize your portfolio with rock-solid, AAA federal government bonds. Just don't overdo it — government bond yields net of inflation are minuscule.

Fourth, ensure your portfolio is crafted to meet your risk tolerance. The run-up in stock prices since the low of 2009 means many portfolios today are overexposed to market downdrafts.

Investors can take some comfort in the fact that the painful aftermath of the global financial crisis will gradually recede. St. Augustine said, "Patience is the companion of wisdom." Investors with a healthy dose of both will do just fine.

-Michael Nairne, CFP, RFP, CFA, is the president of Tacita Capital Inc., a private family office and investment counselling firm in Toronto.