

Taking advantage of bad times

Economies go through cycles of wealth generation followed by contraction – and even destruction. Yet recessions keep catching us unawares. **SIKONATHI MANTSHANTSHA** investigates the means to survive.

Those people and businesses that made judicious use of the good times provided by the longest economic growth cycle SA has ever seen (2003 – 2008) will be in a better position to take advantage of the current economic environment and to generate wealth for themselves, says Professor Eltie Links, who teaches International Management Studies and Doing Business in Africa at the University of Stellenbosch Business School.

Saving during the good times is the buffer that ultimately makes it possible to secure future wealth by enabling you to invest profitably while asset prices are under pressure, says Links. “When times were good, you should have done the necessary things like saving and taking good care of your finances in order to last through recessions.”

Links says people should always remember that good times never last. “Bad times also never last, but you’ll find the bad ones last longer if you didn’t make the necessary provision during the good times.”

Now that the global economy has been in recession for over a year with no immedi-

ate end in sight, most businesses and consumers will no doubt be found wanting on ways to survive.

Even blue chip multimillion-dollar companies have succumbed to the subprime-induced recession. Does certain death await struggling smaller businesses too? Or are there wealth-creating opportunities amid the bloodbath of the stock and property markets?

Potentially, recessions can be a good thing over the long term, as they help the economy to restructure itself and become more competitive, says Stellenbosch University’s Bureau for Economic Research economist Hugo Pienaar. Companies become more streamlined and productive after realising that they need to cut out unnecessary costs to survive. This includes job layoffs or reduced salaries and paying off debt – thus strengthening the balance sheet.

“Although never seen as a good thing, recessions do flush out uncompetitive

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companies and help consumers to cut back on debt. If you can emerge from a recession with a more streamlined and productive company, then it was a good thing!”

Pienaar says a major negative effect of recession is the drying up of liquidity in global markets. Money disappears, and companies that rely on credit to survive often fail, as has occurred recently with some of the developed world’s largest companies.

But where does the money suddenly go then? “Money doesn’t go anywhere. It is just that banks suddenly become reluctant to lend,” says Pienaar. Banks reduce or withhold credit supply, both to consumers and other businesses, as a direct response to the rising bad debts resulting from years of easy money.



“In the local economy consumers are still suffering from the interest rate increases of two years ago and bad debt is high and rising,” he says.

However, Pienaar sees a silver lining around the credit liquidity cloud as the situation starts to normalise in the European and US markets. “Unprecedented government support there has helped avert a disaster of the magnitude of the



Make provision:
Prof Eltie Links



Competitive economy:
Hugo Pienaar



Investment mode:
Monale Ratsoma

Great Depression.” He says the economic situation would have been a lot worse had the British and US governments not intervened. They responded by injecting billions of capital into some financial and industrial institutions that were in danger of collapsing. “Policymakers have learnt from the mistakes committed during the Great Depression,” says Pienaar.

That, however, is not immediately going to benefit the SA economy, as positive growth can only be expected next year. That’s according to Thebe Securities econo-

mist, Monale Ratsoma. He says the private sector, like the government, has to move to investment mode for growth to take place. But for that to happen, confidence needs to return to the economy.

When asked whether government has to do more to aid that confidence, Ratsoma counters: “What more can the government do?” With the successive interest rate reductions since December 2008 to pre-June 2006 levels – coupled with the government’s infrastructure investment programme – much has already been done to stimulate confidence in the SA economy.

Ratsoma says the recession, which was led by a sharp fall in consumer spending and commodity prices in SA, has provided the country with a chance to restructure its economy to move away from relying on consumer-led expenditure. Instead the country can focus on manufacturing and exports. “That is the ideal way to go. However, the reality is that it’s not going to happen,”

he says. South Africa’s rigid labour dispensation prevents the country from competing effectively with the likes of China on manufacturing. “Manufacturing is never going to thrive in an environment where organised labour is as powerful as it is in SA.”

Both Ratsoma and Pienaar agree that the recession has provided many investing opportunities, with asset prices currently priced significantly lower than before the recession. But to take advantage of those, people need cash, and cash is scarce.

As Ratsoma observed, the global recession has largely bottomed out and the economy is likely to have stabilised at the lower levels. That signals the beginning of the next economic cycle – growth. Both Pienaar and Ratsoma agree that asset prices currently offer great value, and as Links says, investments around the current property and equity levels will see the investor through the next recessionary cycle.

The best way to do that is to pay off debt faster and then to take advantage of the discounted asset prices like property and shares, advises Links. “Don’t see this as an opportunity to accumulate more debt.” Asset prices are significantly discounted – by over 30% and sometimes by 50% for equities – on what they were two years ago. ^a

Drowning in a sea of opportunity?

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