2050 INVESTORS

THE ROARING 2020S

Hosted by Kokou Agbo-Bloua
Societe Generale's Head of Economics, Cross-Asset & Quant Research

EPISODE 1 - Featuring Charles De Boissezon, Societe Generale Cross Asset Research's Global head of Equity Strategy

In the first episode of the '2050 Investors', Kokou starts his investigation with this question: are we entering a new Roaring 2020s? As we are emerging from a historic shock linked to the pandemic, with trillions being poured into the global economy, it seems like we are on the verge of an economic boom, But, how sustainable is all this spending? Are we going to see a green infrastructure and cultural revolution?

SOCIETE GENERALE

2050 INVESTORS – EPISODE 1 SCRIPT

(Opening credits for all episodes)

Welcome to 2050 Investors, the podcast that deciphers economic and market mega-trends to meet tomorrow's challenges.

I'm Kokou Agbo-Bloua, I head up Economics, Cross-Asset and Quant Research at Societe Generale.

In each episode of 2050 Investors, I'll investigate a key mega-trend that relates to the Economy, the Planet, Markets and You.

(Beginning of episode 1)

As I am speaking, first week of June, the OECD has just raised its GDP growth forecasts for the UK – where I am based.

Really, it seems like we are on the verge of an economic boom. As we are in the 2020s, and as we are emerging from a global pandemic, I really do have to ask: Are we about to enter the Roaring Twenty 20s? Are we going to see a green infrastructure and cultural revolution?

The Roaring Twenty 20s. I love this catch phrase. I love its historical connotations and implications for current economic and market dynamics. It really is a fascinating, fun and complex topic actually.

So, are we entering a new Roaring Twenty 20s? To be blunt, yes, it sure does looks like it… The empirical evidence clearly suggests that we are in the midst of a new growth cycle.

A growth cycle triggered by over 25 trillion dollars of combined fiscal and monetary stimulus. And yes, you heard me correctly, 25 trillion dollars, that's a lot of money.

If you search headlines online, you'll see a lot of content on the 1 trillion European Green Deal. Titles like: "Europe's climate goal: Revolution" or "Europe's green moment: How to meet the climate challenge" are all everywhere.

And of course, there is also the 2 trillion dollars Biden infrastructure plan.

Or even just look at the strong equity market recovery that is being driven by high earnings growth that seems to be defying the laws of gravity. You also have to see the S&P that's hitting new all-time highs multiple times in the last six months. Even the credit market is on fire.

And even after all the borrowing last year, no one is fearing a massive wave of corporate bankruptcy anymore. Companies having repaired their balance sheets. And believe me, this is a good thing! One could even call this the first successful mass vaccination of corporate zombies thanks to government support.

This all shows that we are experiencing a robust economic V shape recovery. Confidence is improving in the vaccination campaigns. There is definitely light at the end of the tunnel.

Now, all of this is great, but … (and yes there is always a but with these things) … while there is always light at the end of the tunnel, it's probably best to make sure that it is not an oncoming train. Because indeed, we've had our fair share of trains over the years. Everyone remembers the eurozone debt crisis, the subprime crisis, the dotcom crash….

In other words, I think the big question, really, is all about sizing up this new decade. This actually is what a lot of my current discussion with clients and colleagues are about!

For instance, just last week, I was having a chat with my boss who really challenged me on whether or not the Roaring Twenty 20s will take us back to unbridled consumerism, mass pollution and social inequality. Definitely something worth investigating.

Now take the European Green Deal or the massive Biden plan, the big question is how sustainable all of this spending is? – be it both on the consumerism side and the infrastructure side.

And most importantly, what are the implications for portfolio managers?

So, the roaring twenty 20s, are they on or not? In our collective psyche, the Roaring 20s refers to recovering from war, pandemic, to the beginnings of mass consumerism, travelling, dancing, basic animal spirit, polluting cars, you name it. It's all there.

So how similar is this to our current recovery?

Let's start our investigation and travel back in time a little. About 6 months.

That's when I first saw the phrase "The Roaring Twenty 20s". It was back in mid-January. I remember it well. I was coming back from a squash game at 7am in the morning. A game which I lost, unfortunately. So not a good way to start one's day really.

Anyway, I started my morning routine of sorting my inbox into a matrix of degree of urgency versus importance. And I actually stopped on an email chain that was probably not urgent and not important but was really interesting. It included a snapshot of the front page of The Economist with the "Roaring 20s".

It's brilliant and made so much sense.

The parallels just jumped at me. The last pandemic was about 100 years ago. It took the world economy by surprise and had a large human, psychological and emotional toll. Social distancing, the need to wear masks, it was all there. But no vaccine though.

Now, fast forward back to that unfortunate squash game. Joe Biden had just been inaugurated as the 46th president of the United States and congress went Democrat, albeit by a small margin. This paved the way for 2 trillion dollars infrastructure spending plan. As you probably know, a plan that has a strong focus on climate change and energy transition. Build Back Better.

As a direct consequence, Cyclicals, Mining, construction stocks, and commodities, started to ROAR upwards. A big change after having been neglected for over a decade by investors. This is the REFLATION trade, and it has clearly been the key theme of the year so far. I mean, can you hear the sound of a market melt up?

So, back to the question and to see what the parallels are between the 1920s and 2020s. Let's, courtesy of Google, do a quick web search on the 1920s.

I'll spare you my sources, but Wikipedia is definitely somewhere in there. Anyhow, the 1920s in the United States was called "roaring" simply because of the exuberant popular culture at the time... Jazz, Hillbilly music, the Charleston dance.

It was also a period of economic growth and widespread prosperity driven by recovery from the First World War, which led to a boom in construction and an incredible growth of consumer goods thanks to mass production.

It was also a period where women fought for their emancipation. A period of social and racial inequality with the infamous Tulsa Oklahoma massacre in 1921. All of which is not really ESG in today's standard. But that said, the energy and particularly the optimism that followed a devastating first World War and a brutal Spanish Flu pandemic appear to rhyme with our current context.

Optimism is a good thing. But a little dose of pessimism can be too… take me for instance, I just looked out the window and it's raining. Again. I can assure you however that when it comes to the weather in the UK "a pessimist is an optimist with experience".

But more seriously, let's now travel back to the future (and yes pun intended).

While history does not repeat itself, in this instance, it does clearly rhyme. At first glance this makes sense as 2020 was a disastrous year. I'm sure we can all agree on that!

The world economy was put into hibernation in order to save lives and livelihoods. Governments did the equivalent of the famous "Whatever it takes" of former ECB president Mario Draghi to save lives by spending trillions.

So, to recap WTI crude oil is up 42% year to date. Gasoline is up 55%. Mass consumerism is back fast and furious. Companies are making more money than they did in 2019. The Q1 GDP growth rate in the US was 6.1%. 41% of the population is vaccinated in the US. In the UK, 40 million people have received at least one dose of the vaccine. And in Europe, they are starting to vaccinate their 12- to 18-year-olds. If this is not the Roaring Twenty 20%, I don't know what is.

But, historically speaking, after the Roaring Twenties came FDR's New Deal, with the 1929 crash in between of course. In our case, and as we just discussed, we are seeing huge uptakes in consumerism and massive infrastructure commitments from both sides of the pond.

A key question I repeatedly see when reading the press is: Is this growth sustainable? Are the infrastructure commitments for a sustainable economy themselves financially sustainable?

First of all, this rebound in economic activity makes sense. This is because during the lockdown companies had to cut costs and liquidate their inventories to raise cash and survive thanks to government financial support. Supply chains globally were disrupted.

It is therefore not a surprise that as the economy is reopening thanks to successful vaccines, we find ourselves in a restocking cycle where demand is outpacing supply. And this is driving prices of goods. It is also creating what's called cost push inflation.

In addition, you have to consider the fact that cumulative excess savings, A.K.A money sitting in household bank accounts, has now reached a staggering 2.4 trillion dollars. That's money that was not spent on services, on holidays, on luxury good items, or cars. This also includes the 1400-dollar stimulus checks. To put this into perspective, it is close to 10% of US GDP. This is HUGE.

In Europe this number is about 5 to 6% of GDP or close to a trillion dollars. And this is also huge!

And of course, some of this money has found its way into the equity markets. The number of new online trading accounts has skyrocketed. This has led to pockets of irrational exuberance in some shares like the GameStop episode that was all over the news a few months ago.

What's important though is that some of this money will go into revenge spending. Tickets for travels this summer are already fully booked.

This reminds me of FDR's inaugural speech in 1933 when he said, "The only thing we have to fear is fear itself". "The only thing we have to fear is fear itself" because fear can paralyze risk taking. It can paralyze entrepreneurship and the economy.

The antidote to fear is confidence and the other side of confidence is trust. Trust in a successful vaccine rollout and efficacy. Confidence is a crucial driver of growth or as economists would say, it drives the marginal propensity to spend.

So, is THIS SUSTAINABLE?

Well, let's look at it this way. Business cycles can follow a clock. If you take a credit clock for instance: you have a debt crisis at 9 o'clock, or where we were in 2009.

Then you move to 12 o'clock. This is the deleveraging phase. A sort of creative destruction or Darwinism. This is where excess capacity is liquidated. Where companies default and where corporate balance sheets with too much debt are repaired.

You then move to 3 o'clock which is the co-recovery phase. These are the happy days. Healthy growth.

Then comes 6pm.The releveraging phase. This is where you see excessive risk taking and releveraging to generate more profits by taking bigger and even bigger risks. To quote Einstein, *there are two things that are infinite.* One, the size of the universe. And two, human stupidity. And he was not even certain about the size of the universe.

This is where the seeds for the next crisis are sown, it is inevitable. Excessive risk-taking ends up in a debt crisis and the cycle restarts.

If you think about it, it's similar to the four seasons in nature. The debt crisis is winter at 9 o'clock, followed by Spring at noon, that's the rebirth, and then summer at 3pm and autumn at 6pm.

Today we are roughly at 2 o'clock in the business cycle with current commitments by US and European governments to spend trillions of dollars over the next decade.

The sustainability of this investment cycle will simply depend on the return on investment of these green projects versus their cost of capital. And today, that cost of capital is very low. That's because interest rates for government debt are at record lows thanks to Central banks.

This really is an opportunity for a green revolution. A revolution both in our mindset and the fabric of our industry. But beware… Winter is coming, and it is up to us to break the cycle.

Central banks and governments have been trying to distort the cycle and to prevent winter i.e.. A debt crisis. What happens when an unstoppable force meets an immovable object, well time stops? We cannot distort the economic clock forever.

So… Ok. We have trillions on the table. But what does that mean? What are the implications for portfolio managers?

This is one of the most common questions I get in client meetings. Because indeed, we all know that "There is no such thing as a free lunch". Even though "The best things in life are free", no free lunch I'm afraid guys.

We could be entering yet another boom-and-bust cycle. Let's not forget that the 1920s ended with the October 1929 stock market crash after years of irrational exuberance.

This then led to the Great Depression. We've all read the struggles of migrant farmworkers in The Grapes of Wrath by John Steinbeck. So, fool me once, shame on you. Fool me twice shame on me. Fool me 10 times, hum… then that's insanity which Einstein, yes Einstein again, once defined as "*Doing the same thing over and over again but expecting different results*".

And yes. You may have realized; Einstein is one of my favourite sources for quotes... But back to our trillions of recovery spending. How or rather, who is going to pay for it all?

We know what happens to governments who lose control of their public finances. You get a sovereign debt crisis. This was the eurozone debt crisis, with Greece, and then concerns about Spain and Italy.

What is unique this time around though, is that everyone is increasing their debt with the help of central banks. There is no discrimination against the weakest link because actual human lives are at stake.

To better understand this, I've decided to look into the Biden infrastructure plan a little closer. And when I say I, I mean calling my colleague Charles de Boissezon, Societe Generale's Global Head of Equity Strategy, who recently has been in the news talking about Green America.

[Interview starts]

Kokou: Hi Charles, how are you?

Charles: Hi Kokou, how are you?

Kokou: Good! How's Paris? I hope it's not raining as much as it is in London right now…

Charles: Well, you know Kokou it's not raining and on top of this bars have just reopened so I'm feeling great!

Kokou: Brilliant! Charles, I have a few questions for you. First, can you tell us about the Biden plan and what's so special about it?

Charles: Well, is it big? Yes. Is it bold? Yes. But these are not my words, Kokou, but those of Biden in Pittsburgh in March when he laid out his spending plan for America. I believe this plan will be looked at in the future the way you and I look at the Roosevelt's New Deal or Kennedy's New Frontier back in school. It is that special.

And why? Because government plans you know, especially in the US, typically the focus is on the economy, and now there's a new player in town: the planet. And the idea with the Biden plan is, for the first time ever, to take climate impact into consideration for investments. Systematically. It is a sea change.

Kokou: Yes, it's a very good point, particularly the planet as the new game in town. What are the implications for key sectors over the next decades? You think it's an evolution or a revolution?

Charles: You know Kokou, when I hear people reducing green transition to wind power, electric vehicles, I say: think again. Repairing 10 000 bridges, 20 000 miles of highways and roads, spurring the construction of 1,5 million sustainable homes: Biden's green ambitions go beyond just the clean energy companies. And they go big.

In fact, I see five pillars to his plan for investors to look at: Renewables & Biofuels and Transportation, yes. But also: Electric Utilities, Construction & Engineering and, finally, Rural broadband and 5G.

Now for some of these, it's an evolution, like Construction or Electric utilities. For others, it's a revolution, like Transportation or Biofuels.

For now, we're looking at 1,7 trillion dollars spending, but for me, at least as important is the fact that investors demand that companies act for good to fight climate change. I mean, see what's happened recently at some global oil majors with courts and shareholders making unprecedented moves. This is a revolution.

[Interview ends]

Kokou: In a nutshell. This is a big deal. A revolution we all need to follow. So, to wrap up, are we entering the Roaring Twenty 20s? Yes, we are!

Is it sustainable? Yes, if we don't screw it up! And what are the long-term impacts?

Well, it is not about just saving the economy, but it is about saving the planet and ourselves at the same time. Think about this: the planet is maybe just like a biological organism with a high fever. Fighting a virus. Human population. We have the opportunity to be an asset for the planet and not a liability. Because the irony is that a virus by destroying its host, eventually destroys itself. Ask Covid-19.

So, this not just about the planet, it is about ourselves and the next generation.

There are key differences and key similarities with the Roaring 20s, but I hope that instead of repeating history, we have the opportunity in the 2020s to make history. To make a better a history.

(Credits)

Thank you for listening to this episode of 2050 Investors and thank you to [Charles de Boissezon] for sharing some useful insights with us.

I hope this episode has helped you get a glimpse of the future of finance! You can find the show on your regular streaming apps. Please subscribe, leave some stars on Apple Podcasts, leave comments anywhere you like and spread the word!

See you at the next episode!

(Disclaimer)

Whilst the following podcast discusses the financial markets, it does not recommend any particular investment decision. If you are unsure of the merits of any investment decision, please seek professional advice.

Credits. Presenter & Writer: Kokou Agbo-Bloua. Editor: Julien Moity, Vincent Nickelsen. Production Designer: Emmanuel Minelle, Radio K7 Creative. Executive Producer: Fanny Giniès. Sound Director: Antoine Larcher. Music: Rone. Graphic Design: Cedric Cazaly.