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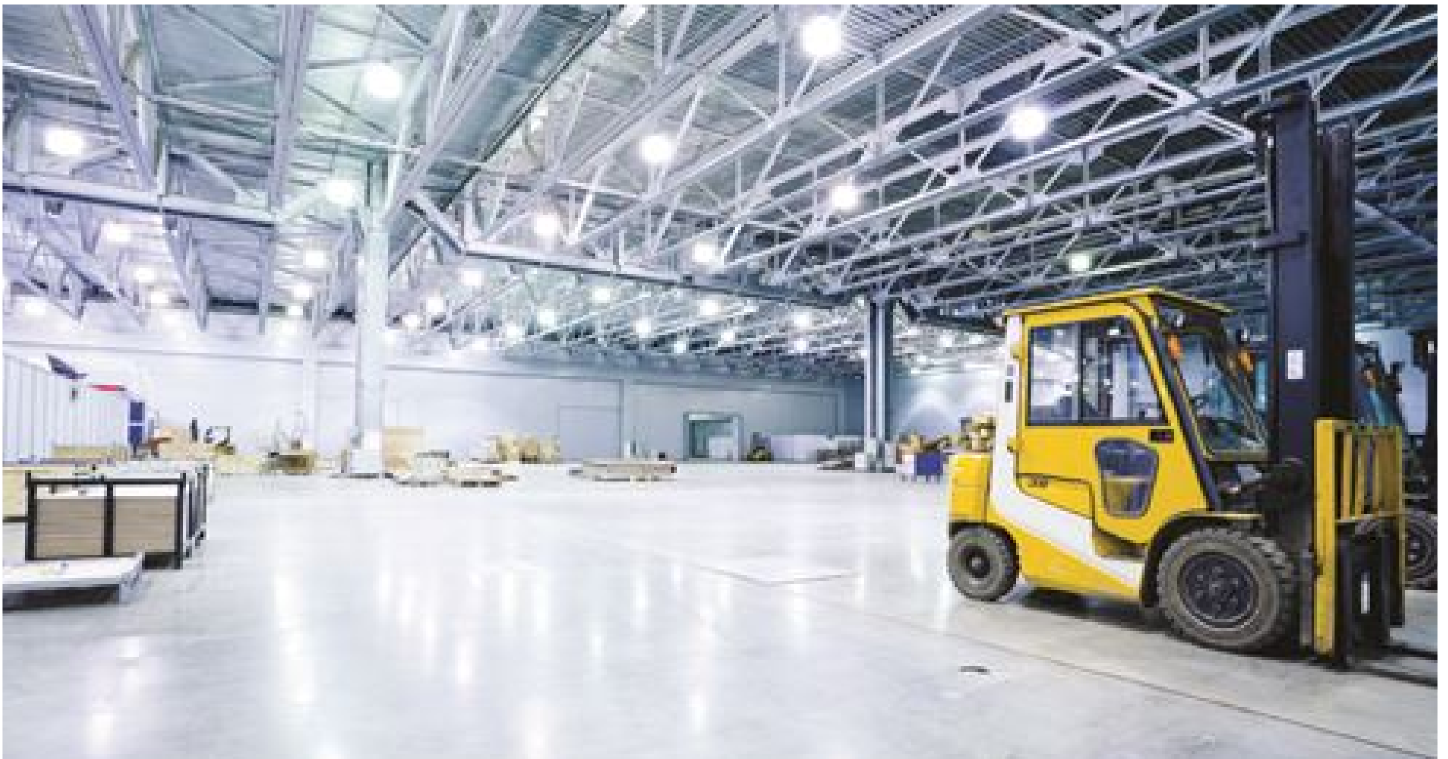
Equity investors face a 30-year slump in the rate of return

By **Niels Clemen Jensen** / 15 Oct, 2018 at 07:27



Last month I argued why bonds won't deliver respectable returns for many years to come. Today I will argue that equities won't do much better than bonds.

We will obviously go through the ups and downs of economic cycles, so don't have a go at me if equities suddenly deliver spectacular returns.

My point is that if you invest in equities today, close your eyes only to reopen them 30 years from now, I predict that average annual inflation-adjusted global equity returns will be no more than zero to 3%.

Here is what you need to know:

ΔGDP = ΔWorkforce + ΔProductivity.

In other words, only two factors drive GDP growth – workforce growth and productivity growth. We already know that the workforce will decline in most countries for many years to come, therefore we desperately need productivity to grow if we want the economy to grow, but how do we do that?

Why productivity is falling

There are many reasons why productivity growth is so pedestrian. To begin with, ageing of society causes productivity growth to slow, as older workers are less productive than their younger peers.

Secondly, servicing the growing populace of elderly ties up ever more capital – capital that could otherwise be used to enhance productivity. Thirdly, excessive indebtedness in all economic sectors has led to more and more capital being used to service existing debt.

Finally, the rising cost of producing the energy we need to spin the wheels every day is another reason. I note that the US energy sector ties up more than 30 times more capital for every barrel of oil produced than it did at the peak of the second oil crisis in 1980. The low-hanging fruit has simply been picked, and it is becoming ever more capital-demanding to increase the production of oil and gas.

In other words, capital is increasingly being used unproductively or, as we economists like to say, capital is being misallocated.

One of the clearest signs of problems on the horizon is the fact that debt grows so much faster than GDP these days. All the way back in the 1950s and 1960s, debt grew in line with GDP. Today, in many countries, GDP grows only by 20-30 cents for every dollar of added debt, ie most capital is deployed unproductively.

Some investors believe that debt is only so high today because significant amounts of capital have already been invested in the new ground-breaking digital technologies, and that this will eventually pay off.

Nothing could be further from the truth

This is the first of a two part series on productivity. Check back on Monday 26 November for the second instalment

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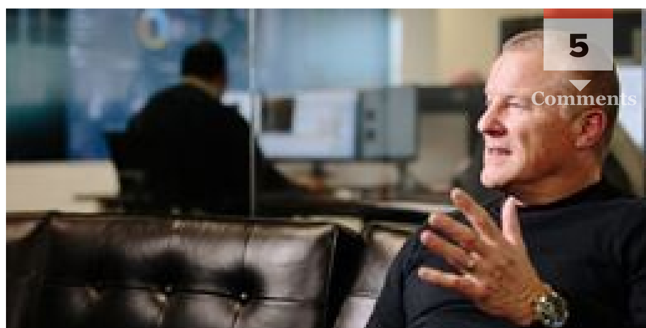

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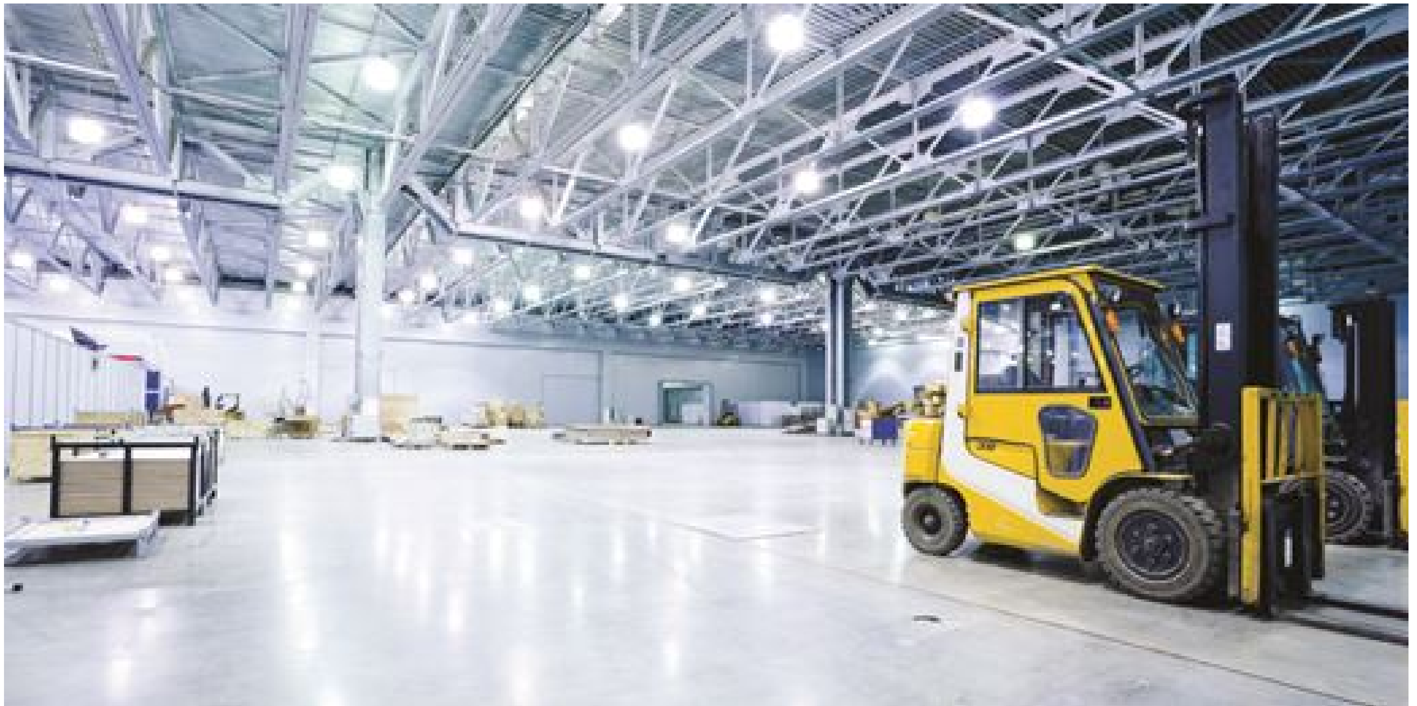

Unless we fix our productivity crisis the average annual inflation-adjusted global equity returns will be no more than zero to 3%.

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