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The Ninety-Nine Percent

Between the recent market correction (since recovered) and a contentious Presidential primary season, many are expressing feelings ranging from cynicism to downright pessimism about the future. As investment managers, we balance that understandable view with the positive dynamics driving long-term opportunities in global markets. Whether considering U.S. technological innovation or evaluating economic trends that indicate increasing global prosperity – especially for consumers in emerging economies – we remain long-term investment optimists.

As realists, however, we know that the long term will be comprised of a series of short-term cycles, both up and down. Likewise, we acknowledge that the positives of global growth bring challenges as well. It can be difficult, for rich and poor countries alike, to manage the spoils of broadening prosperity.

It is Tough at the Top

Let's start with the perspective of America's relative prosperity compared to the world. If one earns over \$35,000 per year, they are in the coveted top 1% of income earners *globally*. Though there are too many Americans facing economic struggles, the reality is that the majority of Americans are one percenters in a global context, with 7 billion others trying to catch up.

Moving to a comparison of selected developed versus emerging economies, (as Table 1 illustrates) the U.S., Germany and Japan comprise just 7% of global inhabitants but generate around 35% of GDP. Strikingly, their GDP per capita is more than ten times that of India and China. Even though relatively little growth is forecast to come from the developed world due to economic maturity and low population growth, there is substantial wealth creation when these economies "limp by" with 2% economic growth.

China and India have populations of around 1.3 billion each, but India is projected to grow faster from a smaller base of GDP per capita – \$1,770 per year versus \$7,500 in China. Collectively, the expected doubling of GDP per capita over the next ten years in these countries may add \$17 trillion or more to today's global GDP of \$75 trillion. That expansion of global GDP is before counting the potential contributions to growth from the other four billion global inhabitants *not* represented by the countries listed below.

Table 1 ¹	<u>U.S., Germany & Japan</u>	<u>China & India</u>
Population	0.53 billion	2.7 billion
% of World Pop.	7%	36%
GDP	\$25.9 trillion	\$12.4 trillion
% of Global GDP	35%	17%
GDP Per Capita	\$49,000	\$4,700
Proj. GDP Growth	1-2%	5-8%

Castes of Thousands

As mentioned in earlier newsletters, virtually all countries are combating corruption and bureaucracy as major headwinds. Recent world events also demonstrate how social media and rising expectations among youth can quickly lead to massive organized protests.

1) Sources: United Nations Population Division, World Bank, U.S. Bureau of Economic Analysis.

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In India, there are special cultural issues to be dealt with in regards, for example, to the 3,000 or so castes that can countervail democracy. In July 2015, a 23 year old from the Patidar caste formed a political movement after becoming incensed that his sister's caste was not "low enough" to qualify her for a certain scholarship. In just 60 days, with the help of social media, he arranged a protest in Ahmedabad with 500,000 in attendance². In February of this year, a related protest by another caste led to riots, 28 deaths and the destruction of a canal serving water to 28 million people³. These protests in India, which make U.S. political kerfuffles seem minor, have become somewhat routine and demonstrate how difficult it can be to adjust when lifestyles change from agrarian to city-like, and when young people become educated and facile with social media.

Let's Play Slapjack

In China's case, a primary government aim has been to crack down on corruption. China's Central Commission for Discipline Inspection recently announced that it punished almost 300,000 communist officials last year—82,000 of whom received "heavy punishment." These numbers sound high but comprise less than 1% of the 88 million communist party members⁴. Beyond whatever political consequences there may be, the impact on consumption of opulent luxury goods and gambling—two categories that tend to draw the attention of authorities—has been dramatic. In Macau, the only place where gambling is legal, gaming revenue dropped 40% recently.

We point out these stories and trends not because we think they will ruin the positive Asian landscape. Keeping contentment among hundreds of millions of low-wage workers in developing countries is daunting for policymakers there, but the "troubling news" is often a reflection of the *opportunities* being created and the ever-rising expectations of their citizens. In the last 15 years, both India and China have vastly improved their citizens' standard of living as evidenced by the United

Nations Human Development Indicators Index and there is room for continued improvement. India and China raised their development scores from 0.4 to 0.6 and 0.5 to 0.7, respectively, since 1990, but remain well below developed countries like the U.S., Germany and Japan which score about 0.9 on this scale⁵.

Looking at the U.S., our corporations are positioned to benefit from an expanding consumer-class abroad and we remain a global powerhouse of technological innovation. Yet, Americans are not immune to feelings of economic discontent. The ripple effect of innovation and broader global prosperity, which we view as a net positive, does impact efforts to preserve the relative wealth our country enjoys, including the standards of living for those with lower-skill, middle-class jobs.

Though future performance can never be guaranteed, it is our belief that high-quality companies with strong balance sheets are best positioned for the current environment. They have the flexibility to navigate the inevitable struggles and weather the downturns—and, at times, take advantage of them—while capitalizing on positive long-term trends. With this long view, the broadening prosperity globally remains impressive and creates enormous opportunity for both the global 1 percenters (i.e. Americans) and the other 99 percent alike.

Andrew C. Burns

ABurns@HamiltonPoint.com

Richard S. Woods, CFA, CPWA®

RWoods@HamiltonPoint.com

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2) "Curfew in Ahmedabad as Caste Protests Turn Violent." *Al Jazeera*. 26 Aug. 2015.

3) "Backward ho!" *The Economist*. 27 Feb. 2016.

4) Pandey, Avaneesh. "China Punished Nearly 300,000 Officials For Corruption in 2015." *International Business Times*. 7 Mar. 2016.

5) United Nations Human Development Report 2015: Work for Human Development.

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