GETAnalysis
RESEARCH

July 9, 2013

Current Asset Markets & Economies – The Inversion of Fundamentals

WRITTEN BY: ASHOK DHILLON

Ashok Dhillon has 40 years of front-line business experience in Canada and International markets. He incorporated his first construction company in 1974, and since then has founded and led companies in construction and international power development.

Over the last 20 years Mr. Dhillon, has led and worked with top Canadian talent in the legal, engineering and accounting firms, such as Fasken Martineau, Russell & DuMullen, Stikeman Elliott; Hatch, Moneco Agra, New Brunswick Power, SNC Lavalin; and Ernst & Young, Arthur Anderson, and Grant Thornton. And in London, worked with Perkins Couie and Morgan Grenfell. Mr. Dhillon's companies have partnered and worked with Pan Canadian Oil & Gas, WestCoast Energy, TransCanada Pipelines, and international companies such as AES, Enron Power, Hyundai Heavy Industries.

Mr. Dhillon has worked and negotiated with highest levels of Governments in Canada and India. He has pursued and won mandates to develop power plants in Canada, and foreign jurisdictions such as Hungary, Iran, Pakistan and India with uncompromising ethical standards. His extensive experience in securing and negotiating multi-hundred million and billion dollar mandates in power project development, gives him in-depth knowledge and intuitive insights into macro and micro, national and international, geo-political and economic realities and trends.

Mr. Dhillon has been invited to speak on international business at various forums, including as an expert witness for the Standing Senate Committee, Government of Canada, on "The Rise of Russia, China and India".

In our Universe, all things are subject to constant change, but within the overall constant change, there are the basic immutable laws of fundamental structure that do not change. And if they do change, then the fundamental reality has changed and we do not have a Universe as we know it.

Similarly, our global geo-political economic realities are subject to change, and that change is taking place constantly. In some respects, those realities changed dramatically at the end of 2008. Dramatically but not fundamentally. The basic immutable, fundamental laws of geo-politics and economics still apply. Since 2008, everyone has been expecting the most extreme changes of geo-politics and economics, at some point to revert back to a recognizable semblance of the predictable old order. So far that has not happened, instead greater distortion, particularly in economic reality has been engineered and sustained indefinitely.

On the political front, changes that have taken place due to the 2008 crash have been dramatic, in some instances, particularly in Europe, but are still of a recognizable nature. For instance, governments changing from 'right of centre' to the 'left of centre', or vice-a-versa, as in Greece, France, Italy, Spain, etc., but there was no change in the fundamental structure or nature of global politics due to the crash of 2008. The changes in the Middle East (*the 'Arab Spring'*) in some of the countries, were not directly due to the financial crash, as in Europe, although it could have contributed in some measure, but were a long overdue reaction to brutal suppression of citizen rights, and economic exploitation of peoples in an entire region of the World, that had vast resource (*oil and natural gas*) wealth, the benefits of which had been long denied the citizenry. Even there, the changes that have taken place are recognizable, from autocratic dictatorships to some form of greater autonomy - as troubled, unstable, but emerging democracies.

On the Economic front it has not been that simple. In the aftermath of the 2008 financial crash, the governments of most major economies had to respond to the threat of a total global collapse of the financial system, through the injection of massive liquidity (*cash*) that numbered in the hundreds of billions, and soon surpassed the trillions mark. That government sponsored intervention was required and necessary, and had some precedent in economic theory and practice of the past (*Keynesian*), although not of similar intensity, global scale or duration.

What had not been anticipated was the escalating continuation and scale of government stimulus intervention, going on to 5 years now, necessitated by the persistent plunge in global economic output. The near collapse of the global financial system and the resulting nosedive of the economies, precipitated by the free-market, deregulated, small government, banking crowd of the West, particularly in the United States, ironically triggered the most massive global government intervention required in history. This unprecedented direct financial (*cash*) intervention in terms of amount and length, in the global economies, has created an anomaly that turned the normal relationship between stocks and other assets markets, and national economies inside out. Unfortunately the consequences of such prolonged distortion of fundamental 'free market' laws are creating an unrecognizable economic landscape that is unprecedented, unpredictable and ultimately unsustainable. And for 5 years it has proven to be so.

The rational for keeping the stimulus going was

WRITTEN BY: ASHOK DHILLON

obviously the precipice upon which the U.S. and the global economies continued to teeter on, well after 2008. But perversely, now the need for continued stimulus through direct infusion of liquidity and record low interest rates, is not only to boost economic activity, but has been usurped by the need to keep asset markets inflating and prevent them from tanking, an anomaly created by easy money and ultra cheap credit (*particularly in the West and Japan*) resulting in the extraordinary stimulus creating anemic economic growth numbers at best, as in the U.S., relatively no growth in Europe, and declining growth in emerging economies, including China. But that same unprecedented and prolonged stimulus has propelled the asset markets to soar to record heights, and addicted the market players to extraordinary and fast returns, so much so, that the Central Bankers now, are forced to consider and manage market expectations and their sustainability, as much as, if not more of, fundamental economic activity.

Perversely, it would seem from their reactions lately, that the markets hope for weak economic data to show, so that stimulus is not withdrawn. When economic data shows improvements, markets have reacted negatively in fear of the stimulus tapering and the near zero interest rates rising, the very return to normalcy that all others have been hoping for and Central Bankers have planned, and till recently, directed their extraordinary policies towards.

Fundamentally asset markets are supposed to reflect the underlying strength of the national economies. Today, that fundamental economic law has been broken ushering in an upside down World, and an irrational logic where the financial policies are being directed by the need to keep institutional investors happy and markets inflating, with the secondary hope that somehow the economies will catch up and a balance will be restored. It is an irrational and futile hope, in our view, and destined to insure more years of volatility, uncertainty, and sharp regressions, creating an unpredictable reality that prevents and threatens the underpinnings of any possibility of sound sustainable recovery. The program seems to have been hijacked by the same players that triggered the crash in the first place, in pursuit of the extraordinary, fast and easy money that they are again addicted to today.

The ongoing, and now the 'assets market' sustaining stimulus, prevents the necessary adjustments from taking place and distorts all economic fundamentals, giving out questionable signals of recovery that threaten to disappear with just the talk of stimulus withdrawal.

In the U.S., stimulus tapering is on the horizon, albeit tremulously, with the reassurance that excess liquidity will be maintained and interest rates will remain low indefinitely, again maintained more to reassure markets than from economic fundamentals requirement. In Europe, the talk continues to focus on additional bailouts of their many weak economies, as they still teeter on the precipice. China is forced to re-infuse liquidity into shadow banking, in face of a panic inducing intra-bank rate rise, and the possible resultant banking system collapse. And other major emerging countries such as India, Brazil and Russia are regressing.

What kind of global recovery is that? Forget about sustainable, 5 years and trillions of dollars in the making!

We think one of the most fragile, irrational and unsustainable ones. Our predictions regarding the improbability of sustainable global economic recovery, since the start of 'Quantitative Easing – III (*QE3*)' have been absolutely correct so far, and we see no reason to change our prognostications.