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Global Risks Rise – As Recovery Reassurances Numb

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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”.

As a slowly rising tide can trap the unwary on the beach, or the steadily heating water can boil the frog, the global public is losing the fear and the focus and is being converted to the greed camp by the relentless rise of the stock markets and the constant drumbeat of ‘recovery is underway’.

And yet, in the last five years the global geo-political-economic risks have never been higher, and are in fact rising.

Too prolonged a warning is the bane of any prognosticator. If one cries ‘wolf’ for too long, predictably the effect starts to fade, and if carried on longer, one could engender irritation and abuse. None of that has happened yet, but we can feel the fatigue of the public with being vigilant against the growing global economic threats, both financial and geo-political, and the desperate need for normalization. Therefore, at this time we feel impelled to, metaphorically, smack our readers with the ‘kyosaku’ (*a switch that is used in Zen meditation to wake a practitioner that is losing focus while meditating to find enlightenment*) in the form of this targeted Geo-political Economic Report, touching upon the looming threats.

In spite of all expert opinion over the recent past 5 years, the Global economic condition is not improving. Yes, there are economic indicators that are showing improvements in the developed economies. But considering the depth to which these economies had sunk after the 2008 crash, the cumulative recovery and the associated positive indicators, combined, still show a weak, unstable and struggling global economy, that can barely manage growth. And that

Global Risks Rise – As Recovery Reassurances Numb

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tortured performance was only made possible with the expenditure of unprecedented trillions of dollars spent since the crash, and with the benefit of the combined focus of the biggest and best economic minds employed by governments.

Yet, with all the financial and technical help from the biggest Governments and Central Banks the economies are still faltering. 'So' *(to borrow Janet Yellen's favorite lead-in word to most questions*), the wolves are still at the door - and hiding in the ever changing but perennially anemic statistical numbers.

Since the post crash highs, reached in 2010, the global economic output has declined steadily and very significant financial stimulus, and historically record low interest rates (*the Chart below, source: IMF*).

The following chart speaks for itself. The divergence in the two realities is stark and ultimately unsustainable, regardless of the constant 'guidance' of the Fed and the other Central Banks. The Global economic growth that was to materialize - didn't - for all the fundamental economic reasons we have spoken to previously in our 'Geo-Political Economic Reports'. Instead, the Federal Reserve chose the path of boosting of the asset markets to create the 'wealth effect', through aggressive financial stimulus and ultra easy monetary policy as the path to greater and broader economic recovery, with a hoped-for filter down effect. That filter down effect didn't materialize either (*5 years and counting*) but, in the mission to boost the asset markets they certainly succeeded spectacularly, as the markets have soared worldwide to record setting highs, imperviously detached from the underlying global economic reality (*the Chart below, source: Bloomberg*). The power of the Fed and the other major Central Banks has been instrumental in the asset markets defying basic laws of

Global Risks Rise – As Recovery Reassurances Numb

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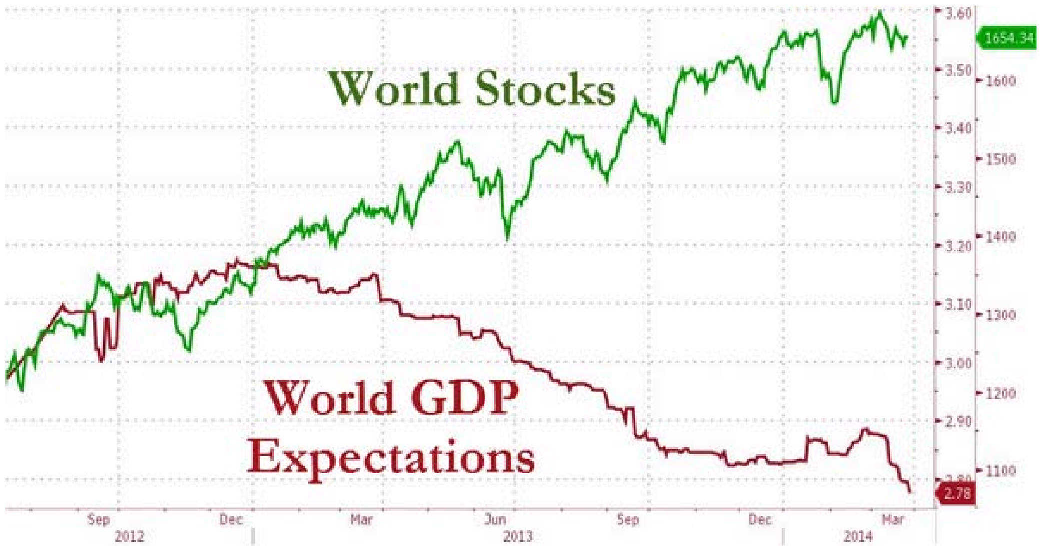
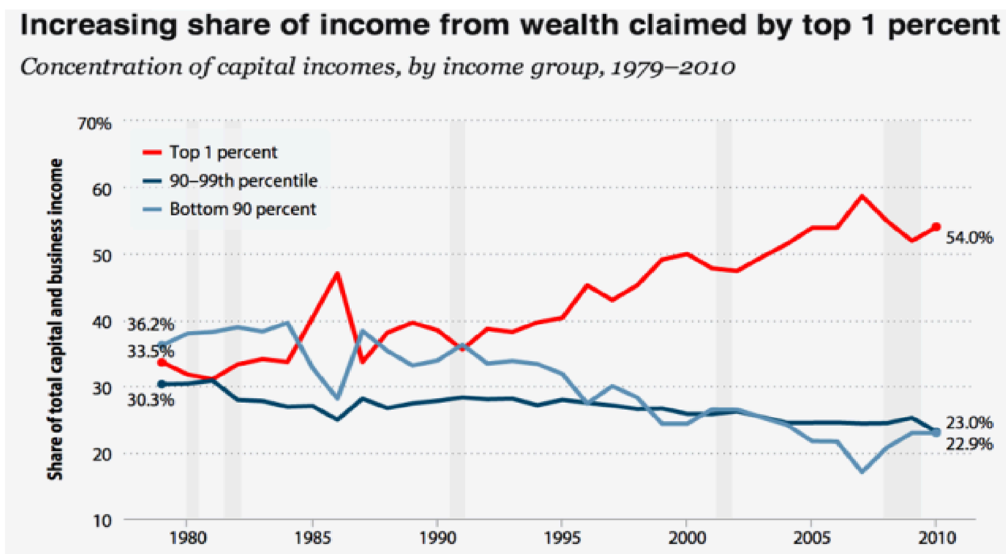
economics and gravity.



Additionally, there has been much hand ringing about the dramatic and growing disparity between the 'haves' and the 'have-nots'. The Fed Chair, Janet Yellen, was questioned about it in her testimony before the Congressional Joint Economic Committee a few days ago. She acknowledged the awareness of the Fed to the growing and serious problem that could, in her words, 'cause social problems', and expressed her grave personal concerns about it.



But, when it came to the question of doing something about it, she shrugged off the problem as not in the mandate of the Federal Reserve, but a problem to be tackled by the lawmakers. The Fed's mandate, in her words, was to try and engender economic growth for the purposes of gaining 'full employment', and the Fed's chosen path to achieving that goal was by creating the 'wealth effect'.

Global Risks Rise – As Recovery Reassurances Numb

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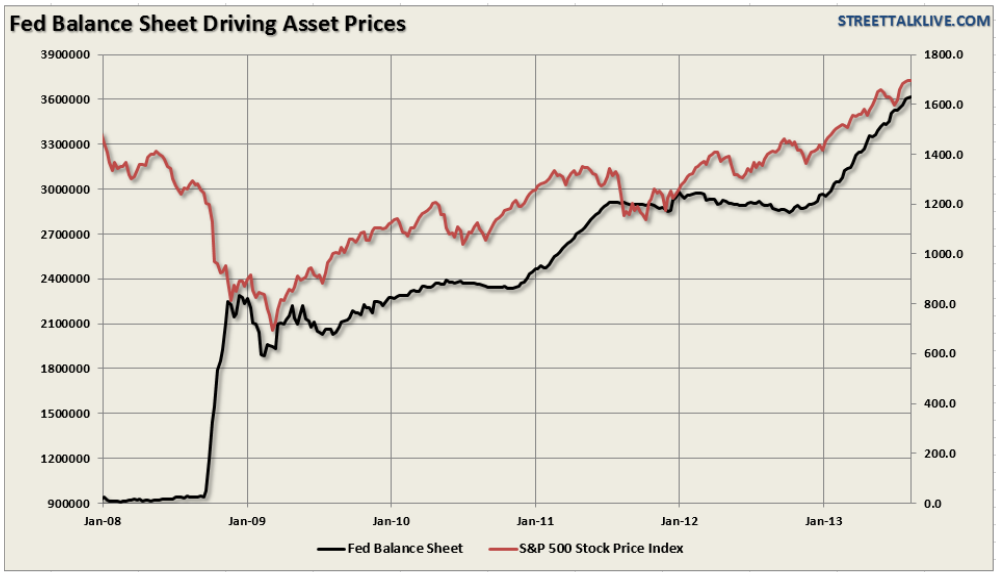
The financial markets loved the 'love' being directed their way and the Dow closed up that day. The stock markets, especially in the U.S. are pushing the boundaries of credulity in their ability to consistently ignore negative economic news, because of the promise of unquestioned support of the Fed. At least till targeted employment levels are reached in the U.S. economy sometime in the unspecified future. That support in the form of continuing asset purchases (*even as they taper*) and the 'however-long-it-takes' ultra low (*near zero*) interest rates that promise cheap money to the market players, maintains the ongoing irrational exuberance.



Janet Yellen was also asked by a member of the Committee, if high leverage in the markets, due to the ultra low interest rates, was of a concern.

Incredulously, she responded that according to the Fed members, who look out for such things, they found no sign of high leveraging in the asset markets. The monthly numbers of the New York Stock Exchange represented in the next Chart, categorically show 'margin' debt to be at record highs, which usually precedes a serious correction.

Global Risks Rise – As Recovery Reassurances Numb

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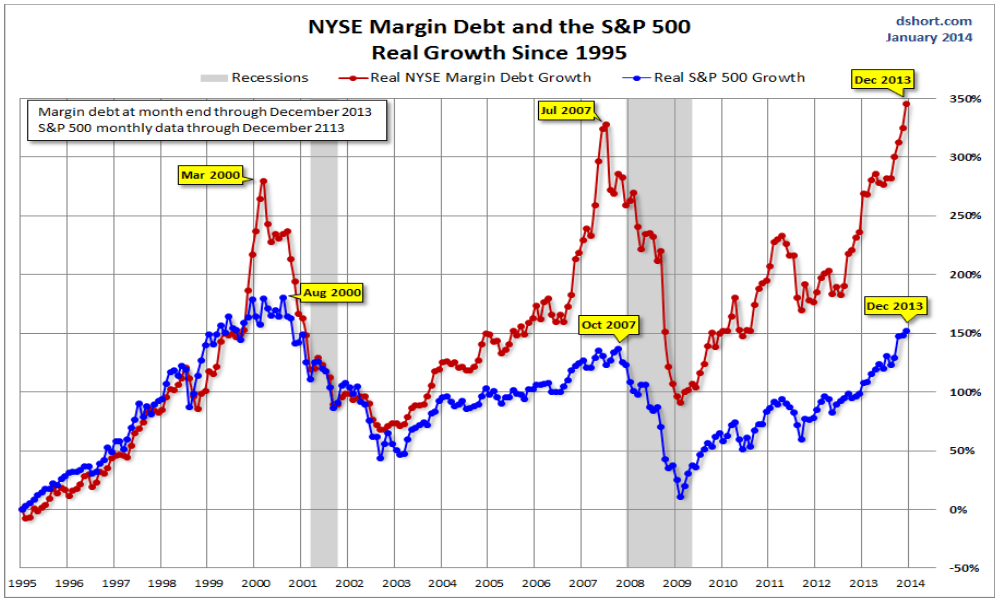
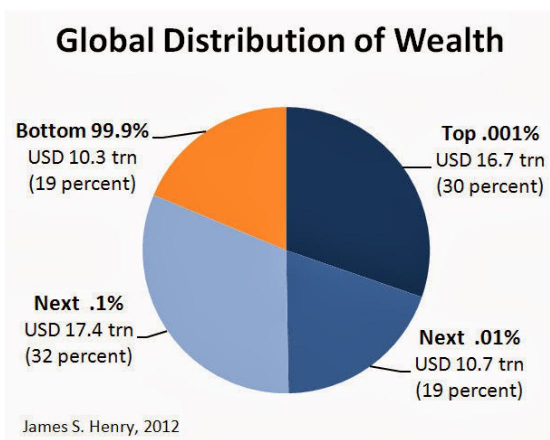
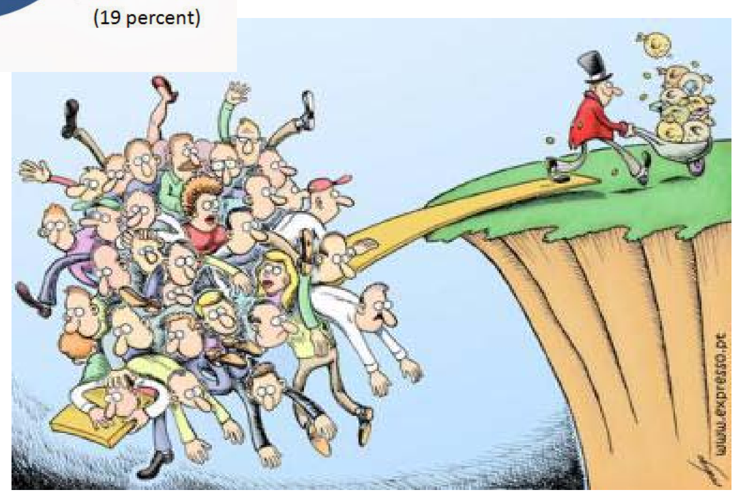


While inequality in wealth in the U.S. is a thing of concern to the Fed Chair Janet Yellen, the Chart below shows statistics that are simply shocking. Yet, a casual observation of economic conditions of the majority of the population in emerging and poor countries, where the World's vast majority lives, bears out the veracity of the stunning numbers in the Chart (*the other picture is just to lighten the tone*).





Global Risks Rise – As Recovery Reassurances Numb

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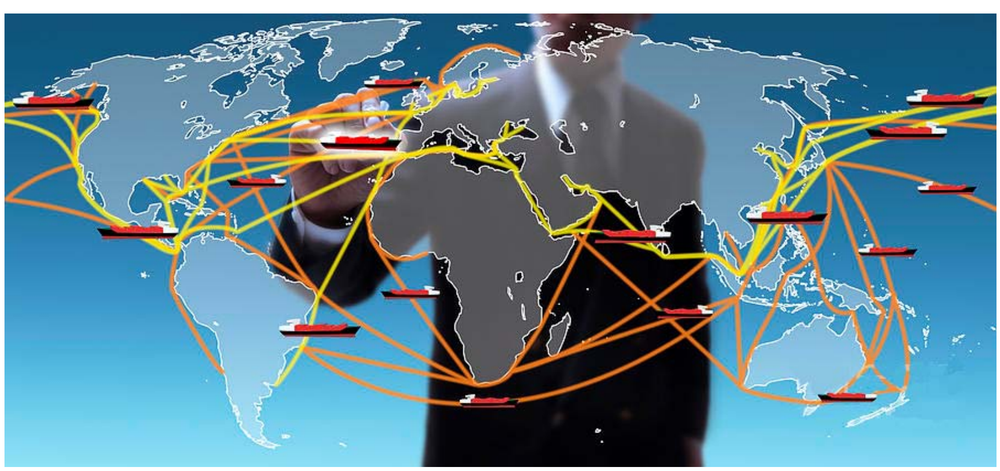
The picture below seemed to capture the point rather perfectly, in the scale of the difference between the yacht and the speed boat.

The disparity between the wealthy and the rest of the population is a universal and seemingly pre-ordained condition. But, the specific economic problems plaguing the individual economies, or the economic zones, are quite disparate. The U.S., EuroZone, China, India and South America etc. - each have unique problems to deal with that are hampering their individual economic growth, but just as – '*no man is an island entire of itself: every man is a piece of the continent, a part of the main*;' (- *John Donne*) – no market or economy today is isolated and independent enough to stand on its own. The interconnect of all global economies makes for a very uncertain outcome in the near future. The overleveraging of global economies will unravel and exact a heavy commensurate price from all, in its search for historical mean.



The Euro Zone being a formal amalgamation of many economies and

Global Risks Rise – As Recovery Reassurances Numb

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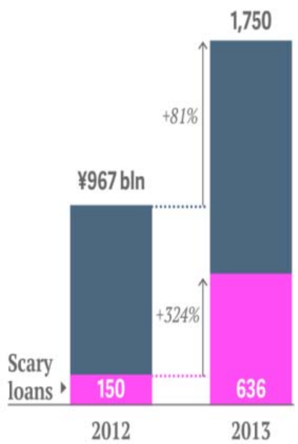
therefore more complicated to control, was savaged by the 2008 crisis far more seriously, and is still for all intents and purposes an invalid. Its many weak and struggling body parts, such as France, Italy, Greece, Spain, Portugal, Ireland, Cyprus etc. make it so. The President of the European Central Bank, Mario Draghi, has just indicated further 'easing' is being contemplated to stave off almost certain deflation, sending asset markets higher (*some recovery*).

Apart from the U.S. high flying financial markets, one of the gravest dangers at this time to the global economy, comes from the over built and over inflated real estate and credit sector of China. The severe over building of unused and therefore stranded infrastructure has locked in untold hundreds of billions of dollars of investment, with no returns. The rampant speculation in residential real estate, acting as a proxy for inadequate returns on savings, has resulted in the largest and fastest growth in debt, known in global history. The increasingly unstable and gargantuan credit market thus developed, especially over the last 5 years as part of the Government's stimulus plan, is starting to generate tremors that the financial markets are ignoring at the moment. But these tremors are a prelude to a very significant seismic shock that poses a growing risk to China's financial sector and economy, and hence to the global financial markets and economies.

Aggregate lending in April



Data: People's Bank of China
Ritchie King | Quartz

Fig. 9: Housing inventory

Source: CEIC and Nomura Global Economics.

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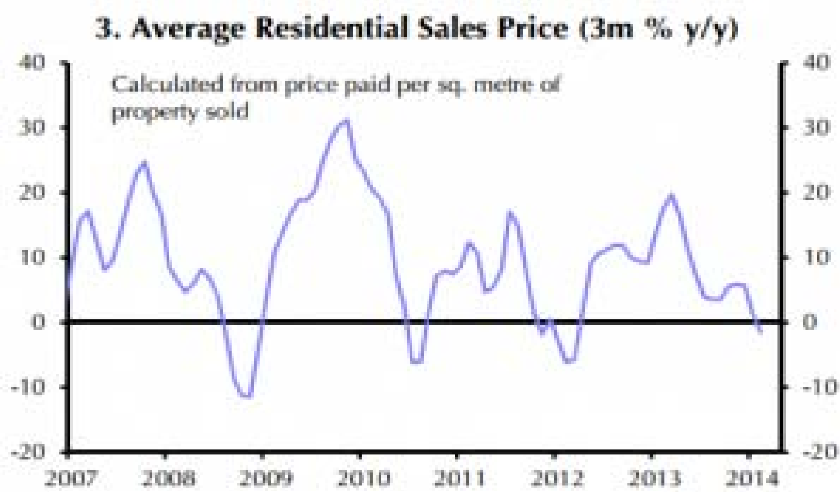
The Chinese Government is well aware of the impending danger, but this time it may be unable to prevent the developing implosion. The steady downward trend in home prices as shown in the Chart below (*source: Macrobusiness*) has the potential for triggering a panic selloff, with a cascading effect in the massive debt market.



Source: Houses & Holes in China Economy

To the financial markets the endless rounds of 'easing' from the Central Bankers means positive news, to the rest of the economic participants, businesses and the public, it's just more bad news, in that the economic growth is still too weak and unsustainable to rely on, and needs further propping for the foreseeable future.

In our view, in spite of the willingness of the Central Banks and the Governments to keep supporting the ever sagging economies, with additional injections of cash or lower interest rates to ease internal borrowing, and deflate currencies to boost exports, the time has basically run out as the overextension of years of artificial financial manipulation, and heavy debt, start to fracture the teetering edifice below.

As it is our self appointed task to keep you informed, and try and keep you positioned ahead of the curve, we are content to continue to yell 'wolf' and point at the beasts as long as we see them gathering for the eventual wealth destroying event. It is up to you the reader, to take the appropriate action to protect yourself from that which is inevitably coming. We can only analyze and opine.