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Better-Management Newsletter 20 October

A mixed bag as risks grow by the day – and a couple of other newsletters

How did relations between Russia and NATO countries get this bad? Well, it seems to suit them both that the media stories are bad...but are they?

Should we believe stuff they put out into the mainstream media? Perhaps. Seems the cyber-warfare may have started...from yesterday's Money Morning...

"*Fortune.com* reported yesterday (my emphasis added):

'*NBC News reports that* ***the CIA is developing scenarios for an electronic attack on Russian leadership. According to sources including current government officials, the intent*** *is to "embarrass" top Russian officials through "clandestine" and widespread hacking.*

'*Vice President Joe Biden seemed to be pointing to just such a possibility during an appearance on Meet the Press airing today, when asked by Chuck Todd why America hasn't responded to Russian attempts to interfere with the Presidential election.*

'*"**We're sending a message," Biden said, with a barely-suppressed smirk. "We have the capacity to do it. He'll know it. It'll be at the time of our choosing, and under the circumstances that have the greatest impact**."'*"

Threats everywhere...

http://www.msn.com/en-nz/news/world/russia-threatens-us-with-asymmetrical-and-painful-retaliation-if-tougher-sanctions-imposed/ar-AAj9iMb?li=BBqdg4K&ocid=EIE9HP

And the Russians feel squeezed...by the python...

http://www.internationalman.com/articles/has-world-war-3-already-started

So no wonder the public are feeling anti towards the West...remember that the first casualty of war is the truth...

http://www.moneyandmarkets.com/russias-march-war-82432?em=jcrofe%40xtra.co.nz&utm_campaign=MAM3618&campid=62178&utm_medium=email

There is a lot of muttering about WW3 in prospect. The Russians and Amerikans seem quite up for it, but the Chinese not so much. There are four things the Chinese would need to do before they even considered taking on the USA in the South China Sea.

1. Get the Renminbi firmly established as a globally accepted world currency.
2. Get rid of more of their US dollars.
3. Get another 1-2,000 tonnes of gold in store.
4. Complete their 90-day strategic petroleum reserve.

Points 1-3 are in train but what about their oil stocks? We don't know for sure but they seem to be getting there...

http://www.usatoday.com/story/money/markets/2016/10/15/china-oil-bust-winners-oilprice/91540480/

Pres Duterte is proving to be a wild card in the game between China and USA in the South China Sea...

http://www.forbes.com/sites/timdaiss/2016/10/18/china-philippines-oil-deal-underway-in-south-china-sea-says-report/#24dbb18f66cf

Russia is building in strength in Syria. It isn't just a new missile battery but also it has 10 ships in Syrian waters and a battle group to join them....

http://www.bbc.com/news/world-europe-37706425

and

http://www.reuters.com/article/us-russia-aircraft-carrier-commentary-idUSKCN12J1L2

But there are signs that the principle players in Europe are talking to each other... a ceasefire in Ukraine and staged troop withdrawals? Who knows...

http://www.reuters.com/article/us-ukraine-crisis-germany-poroshenko-idUSKCN12J2R7

As Russia deals with its nightmare in Aleppo (hint. Not one of the Marx brothers) the USA and allies struggle with gaining entry to Mosul...

http://www.bbc.com/news/world-middle-east-37701250

And the nightmare of civilian casualties in Mosul begins...

http://www.bbc.com/news/world-middle-east-37701235

And there will be a couple of months of bad news to come for the USA as casualties mount...

Meanwhile in the Middle East, everyone has forgotten about Israel and Israel has forgotten its need for strong friends...

http://www.mauldineconomics.com/this-week-in-geopolitics

The Economy

Globalisation has reached its peak for a number of reasons... the first being that geopolitics are becoming fraught after several years of currency wars, post GFC. There is also the breakdown of relations between major powers. But the most important influence is those concerns over the failing global economy and resource depletion... from Seeking Alpha...

"**"We believe globalization** has probably reached its peak," says a fund manager at Barings. "The market won't like it." The team at Barings gets together once a year to discuss its 10-year investment forecast. At the next one, they expect to mull reducing or even eliminating their "globalization premium" from stock price estimates. In more concrete terms, it means directing assets at the margin towards fixed income at the expense of equities. Globalization premium? Barings figures U.S. stocks trade at a P/E ratio one full number higher than they otherwise would have, thanks to this generation's boom in global trade. At issue now is a slowing in global trade this year - the weakest since 2007 - just as protectionist policies are on the rise and efforts for further open trade treaties have stalled. A continuation of the trend, says MSCI, could lead to near-20% declines in U.S. and European stocks. "Globalization is increasingly coming under siege," says a senior strategist with Allianz Global."

There are many signs that the reaction of the powers that be to the coming financial collapse are much more measured as central bankers and politicians have learned something from the GFC. Even if we avoid collapse this year (which now looks more probable), the continuing accumulation of dysfunctional problems within the global financial system suggests continued accumulation of debt and increased fragility. So I will leave probability of collapse by the end of, or during 2017 at 75% for now. Meanwhile, we know the markets are in trouble but the central bank fudging obscures the entire position...

http://www.bloomberg.com/news/articles/2016-10-19/wall-street-sees-graveyard-of-broken-indicators-in-reform-s-wake

I still hold that come what may, we have a probability of collapse by end of 2020 at about 95% (in other words I am still almost certain of that – unless something drastic changes).

The current US POTUS election confirms to many folks that the American dream is over. This article provides expert analysis of why this is the case, so it is well worth reading...

http://ggc-mauldin-images.s3.amazonaws.com/uploads/pdf/OTB_Oct_19_2016_2.pdf

So are we in the calm before the storm?

http://seekingalpha.com/article/4012539-calm-storm?source=email_macro_view_mar_out_2_8&ifp=0

How many more EU countries will need to endure what Greece is continuing to go through...with no end in sight...?

https://www.theguardian.com/world/2016/oct/16/eu-and-imf-auditors-to-visit-athens-as-greeces-agony-continues

Then again, oil exporters are all suffering as much or more than Saudi Arabia who have a decline in GDPof 13% this year to add to the problems of the previous year – as they go hunting for finance on the world bond markets...

http://www.reuters.com/article/saudi-imf-idUSL8N1CO2I3

Charles Hugh Smith is now writing about what can be the source of collapsing economic and political norms L...

https://www.peakprosperity.com/blog/101795/what-triggers-collapse

Even New Zealand is getting ever closer to zero interest rates...

https://www.youtube.com/watch?v=JoGfik5ivis#t=442

The Saudis are starting to have problems due to the low oil price affecting the Kingdom's revenues...perhaps they will need to sell more than just a stake in Saudi Aramco as they continue to live beyond their means...

http://www.bloomberg.com/news/articles/2016-10-16/saudi-bank-stress-builds-as-kingdom-s-cash-injection-falls-short

From Money Morning...here is an article by Jim Rickards on the central banks...

"**The Fed's Legacy: Asset Bubbles and Lost Confidence**
Jim Rickards, Strategist, *Currency Wars Trader*

For most experts, failure is a learning experience that leads to a search for new methods. That's not true for central bankers. When their policies fail, they try more of the same in the vain hope that quantity will make up for the lack of quality in their ideas.

In the past seven years, major central banks have created over US$15 trillion of new money, mostly through purchases of government bonds.

These money printing and bond purchase programs have been called QE1, QE2 and QE3 in the US, Euro-QE in Europe and QQE (quantitative and qualitative easing) in Japan.

All of these programs and exotic variations such as 'Operation Twist' have failed to achieve self-sustaining growth anywhere near former trends, and have failed to achieve the 2% inflation targets of those central banks.

When investors ask, '*Where's the inflation after all this money printing?*' my answer is, '*Don't look at the supermarket shelf; look at the stock market*'.

In other words, we have not had much consumer price inflation, but we have had huge asset price inflation. The printed money has to go somewhere. Instead of chasing goods, investors have been chasing yield.

Part of this asset bubble inflation has to do with a flawed theory of bond/equity 'parity'. The theory says that once you adjust for credit risk and term premium, bonds and stocks should yield about the same. Right now, safe ten-year Treasury notes yield about 1.65%.

Many stocks have dividend yields of 3% to 5%. Investors know that stocks are riskier than safe bonds, but how much riskier? Under the parity theory, investors can keep bidding up the price of stocks until their dividend yields get closer to 2%, leaving a small margin over bond yields to cover 'risk'.

There are many flaws in this theory — including the fact that companies go bankrupt all the time, and boards of directors can and do cut dividends in recessions. But one of the biggest flaws is the complete disconnect between what's driving bond yields in the first place.

If bond yields are falling because deflation is ruining the Fed's plans to reflate the economy, is that a reason for stocks to go up? If bond yields are signalling recession, should you really be bidding up stock prices to extreme levels based on a theory of yield 'parity?' This behaviour defies common sense and economic history, but it's exactly what we're seeing in the markets today.

At some point, probably sooner than later, the reality of central bank impotence and looming recession will sink in and stock valuations will collapse. The drop will be violent, perhaps 30% or more in a few months. You don't want to be over-allocated to stocks when that happens.

This analysis applies to more than just stocks. It applies to a long list of risky assets including residential real estate, commercial real estate, emerging markets securities, junk bonds and more.

It only takes a crash in one market to spread contagion to all of the others.

The inability of central banks to deal with crisis and the complete loss of confidence by investors in the efficacy of central bank policy.

The last two global liquidity panics were 1998 (caused by emerging markets currencies, Russia, and Long-Term Capital Management) and 2008 (caused by sub-prime mortgages, Lehman Brothers and AIG).

Another smaller liquidity panic arose in 2010 due to problems in Middle Eastern and European sovereign debt — caused by Dubai, Greece, Cyprus and the European periphery. In all three cases, central bank money printing combined with government and IMF bail-outs were enough to restore calm.

But these bailouts came at a high cost. Central banks have no room to cut rates or print money in a future crisis. Taxpayers are in full revolt against more bailouts. Governments are experiencing political polarization and there's political gridlock around the world. There is simply no will and no ability to deal with the next panic or recession when it hits.

Consumer inflation expectations have fallen to the lowest level since late 2010 — not long after the last crisis — and the trend is clearly down, toward levels not seen since the depths of the panic in 2008: With central banks around the world doing everything possible to cause inflation (QE, ZIRP, NIRP, helicopter money, currency wars, forward guidance, etc.), what does it say about confidence in central banks that inflation expectations are falling, not rising?

The systemic dangers are clear. The world is moving toward a sovereign debt crisis because of too much debt and not enough growth. Declining productivity is the last nail in the coffin in terms of countries' ability to deal with the debt.

Inflation would help diminish the real value of the debt, but central banks have proved impotent at generating inflation. Now central banks face the prospect of recession and more deflation without any policy options to fight it.

The impact of deflation and the strong dollar have caused a shortage of liquidity around the world.

Since private debt has expanded faster than central bank balance sheets, a dollar shortage has arisen as debtors scramble for dollars to pay back debts. This raises the prospect of a new liquidity crisis and financial panic worse than 2008.

Persistent low rates have not caused inflation, but they have caused asset bubbles, which threaten to pop and unleash a financial panic on their own — independent of tight financial conditions.

When this new panic hits — either from a liquidity shortage or bursting asset bubbles — investors will have no confidence in the ability of central banks to limit the panic. Unlike 1998 and 2008, the next panic will be unstoppable without extreme measures — including IMF money printing, lockdowns of banks and money market funds, and possible martial law in response to money riots.

You should have gold and other hard assets to weather this storm.

But you want to own gold now, before the next crisis strikes. It could be here much faster than you think.

Cheers,

Jim Rickards,
Strategist, *Currency Wars Trader*"

China may be growing but it is growing debt at a much greater rate L...

http://www.reuters.com/article/us-china-economy-gdp-idUSKCN12J060

Bill Bonner puts the net effect as a reduction in the global economy...or de-growth...from today's Daily Reckoning for those who don't get it...

"**Impoverished by Too Much Money**
By Bill Bonner in Baltimore, Maryland, US

Author Raúl Ilargi Meijer explains that the '*entire model our societies have been based on for at least as long as we ourselves have lived is over!*'

Meijer again:

'*That's why there's Trump…*

'*There is no growth. There hasn't been any real growth for years. All there is left are empty, hollow, sunshiny S&P 500 stock market numbers propped up with ultra-cheap debt and buybacks, and employment figures that hide untold millions hiding from the labor force. And most of all, there's debt, public as well as private, that has served to keep an illusion of growth alive and now increasingly no longer can.*

'*These false growth numbers have one purpose only: for the public to keep the incumbent powers that be in their plush seats. But they could always ever only pull the curtain of [The Wizard of] Oz over people's eyes for so long, and it's no longer so long.*

'*That's what the ascent of Trump means, and Brexit, Le Pen, and all the others. It's over. What has driven us for all our lives has lost both its direction and its energy.*'

Shipping decline

None of this will come as a surprise for *Diary* regulars… We know nothing makes people poorer faster than too much 'money'.

The feds provided the economy with an almost unlimited quantity of credit-based funny money. The money was phony. But it bought real resources. And then, with no need to think carefully about how the capital was put to use, the resources were wasted.

Corporate defaults are running at their fastest pace since 2009. Nine out of 10 households have lost income. And tax receipts for the last quarter fell from the same quarter in 2015.

Adjusted for inflation, real growth in the US economy — as measured by actual tax collections rather than the feds' squirrelly statistics — is falling.

The world economy, too, is slowing. Lambert Strether of the blog Corrente Wire explains:

'*I started following shipping…partly because it's fun but more because shipping is about stuff, and tracking stuff seemed like a far more attractive way of getting a handle on "the economy" than economics statistics, let alone whatever books the Wall Streeters were talking on any given day.*

'*So, what I noticed was decline, and not downward blips followed by rebounds, but decline for months and then a year. Decline in rail, even when you back out coal and grain, and decline in demand for freight cars. Decline in trucking, and decline in the demand for trucks. Air freight wobbly. No Christmas bounce at the Pacific ports.*

'*And now we have the Hanjin [shipping company] debacle — all that capital tied up in stranded ships, though granted only $12 billion or so — and the universal admission that somehow "we"* *invested w-a-a-a-a-a-y too much money in big ships and boats, implying (I suppose) that we need to ship a lot less stuff than we thought, at least across the oceans.'*

Get-rich system

As we reported last week, China's exports are falling at a 10% annual rate, in US dollar terms.

If you're not exporting stuff, you don't need ships to send it anywhere.

But as the global economy sinks, debt rises, financed by central banks. Bloomberg:

'*The world's biggest central banks are bulking up their balance sheets this year at the fastest pace since 2011's European debt crisis to boost lackluster economic recoveries with asset purchases that are supporting stock and bond prices.*'

Let's see… How does this work again?

The world has too much debt and too much capacity. Growth slows. Defaults increase.

So what do central banks do?

They facilitate governments adding to their debts…and they finance more capacity.

The feds used fake money to give the economy fake credit…which was used to buy real resources…which were squandered. Now we have an abundance of claims (debt) against declining future output.

How was that ever supposed to work?

An economy is a moral system, after all. It is not a get-rich system. You get what you deserve, not what you want or what you expect.

Over the long run, the economy punishes waste, error, foolishness, impetuousness, laziness, arrogance, and indiscipline.

Americans now are being punished. Gently, so far.

The lash will sting much more later.

Bill Bonner,
For *The Daily Reckoning, Australia*"

Energy

We humans have not lost the ability for mass self-delusion...

http://www.petroleum-economist.com/articles/events/wec-istanbul-2016/2016/the-great-transformation

So this move from fossil fuels will happen by 2030? Heck by then the Indians and Chinese will still be doing more polluting! Despite efforts to divert funds away from exploration and production of oil, gas and coal, the fact is that demand for all is increasing, but with gas taking over some of coal's role. But while in the last 15 years we have seen more rhetoric than ever about climate change and the need to reduce CO2 discharges, our CO2 production has increased by 30%. As they say, "Good going Batman! J". The only things that will slow down growth of fossil fuel production is oilfield depletion hastened by low prices...and that will bring on crash time.

Oil demand continues to rise each and every year. We cannot seem to to hold that back. Yet oil production vaccillates...partly due to depletion and other factors...

https://www.youtube.com/watch?v=ow1w33VAPII

If I lived in Scotland I would be more concerned about how to keep the lights on and maintaining English subsidies for the Scottish unemployed, rather than independence...

https://www.theguardian.com/environment/2016/oct/15/energy-storage-vital-to-keep-uk-lights-on-say-mps

The end of sanctions against Iran did not result in the country being able to ramp up oil production as much as some analysts had predicted. They need both capital and US knowhow to get their declining field going and get new ones started....

http://www.csmonitor.com/Business/2016/1016/Can-oil-bridge-ties-between-Iran-and-the-West

Unless the mythological EESU can store and hold energy (and we are awaiting the results of polymer trials for this), the lithium-ion electrical energy storage business will grow and prosper.

Strangely, it turns out that two of my investments have substantial lithium leases. Who knows, while I bought the shares for their uranium or gold prospects, one of those shares may surprise me and make a profit? But the EESU that uses CMBT could change all that and yet the lithium players remain blissfully unaware of that possible market disrupting threat. It would sure rain on their parade J....

http://seekingalpha.com/article/4012850-tesla-apple-uber-push-lithium-prices-even-higher?source=email_macro_view_gol_pre_met_5_16&ifp=0

Some lessons from the State of South Australia on what happens when the power goes out over a wide area....

http://charleshughsmith.blogspot.co.nz/2016/10/what-happens-when-electricity-is-off.html

Will the price go ballistic when oil production drops? That would certainly be a game-changer for the global economy because the price of everything would go through the roof....

http://oilprice.com/Energy/Oil-Prices/Why-Oil-Could-Head-Back-To-90-Sooner-Than-Thought.html