The world has gone mad

By Vern Gowdie on the Gold Coast, 4 March 2017

Watching the world around me makes me question my sanity.
Do people not see what I'm seeing, or am I the crazy one for not seeing what others see?
Before letting you in on my latest session of psychoanalysis, here's a quick look at overnight markets.
The Dow Jones has taken a breather after its big run on Wednesday night…down 112 points.
Gold, too, has given up some recent gains, trading at US$1,235 an ounce.
Overall, not much to report from overseas.
The big news this week is that the 'Lucky Country' dodged the recessionary bullet.
According to the numbers released by the Australian Bureau of Statistics, the Aussie economy expanded at the rate of 1.1% in the December 2016 quarter.
Prime Minister Turnbull was overjoyed with the result; given his approval rating, it was a welcome distraction for him.
Turnbull told parliament: 'This is a very good outcome for Australian families, for Australian business and for jobs…'
Really?
When you barely scratch the surface of the data, you find that the household savings ratio fell from 6.3% to 5.2%. Households were raiding the piggy bank to spend up for Christmas.
That's a good outcome for families?
The last time the savings ratio was at this level was back in the third quarter of 2008…the same quarter that saw the collapse of Lehman Brothers.
The falling savings ratio prompted Bloomberg to issue this headline: 'Aussie consumers are putting away less for a rainy day'.
We're mortgaged to the hilt. We haven't had a pay increase. Part-time employment is on the rise at the expense of full-time jobs. And the cost of the non-negotiable budget items — energy, water, rates and government charges — keep increasing at a faster rate than the official Consumer Price Index figure.
For many households, this is not a 'rainy day', it's a tropical storm.
Households are drawing on savings to maintain the lifestyle we've become accustomed to after 25 years of being recession free.
The Australian Treasurer, Scott Morrison, gave us his take on the GDP result (emphasis mine):
'The treasurer, Scott Morrison, said the result was achieved due to strong household consumption, but warned that "weak wages growth" was still weighing the economy and budget revenue down.
'"[The result] confirms the successful change that is taking place in our economy as we move from the largest resources investment boom in our history to broader-based growth," he said.
'The treasurer said the principle driver for growth was "a solid rebound in household consumption" which occurred "despite subdued wages growth".
'"Of **concern in these accounts is that compensation of employees in the quarter declined by 0.5%.** It was up 1.5% in the year."'
The Guardian, 2 March 2017
Employee compensation declining by 0.5% in the quarter weighs down the economy and budget revenues? No kidding, Sherlock.
Yet, in spite of this stagnation of household income and tax receipts, the Lucky Country has managed to conjure up growth.
How?
People spent more than they earned **and** went deeper into debt for…consumption.

They call Australia the miracle economy for good reason. It's a bloody miracle that people believe spending money you don't have qualifies as genuine growth.
And right on cue, we'll bring in our PM again, with his positive spin of this destructive debt habit: 'This is a very good outcome for Australian families…'
Really, Malcolm? Where's the prudent banker within you saying 'stop this insanity as it will end badly'?
Instead, I'm the one on the couch trying to make sense of all this.
Doc, one of is nuts…
We're told our $1.6 trillion economy 'grew' by 24% over the past 12 months…give or take, that amounts to an increase of $40 billion in economic activity.
Australia's total debt — public, private and corporate — at the start of 2016 was near $6 trillion. Currently, our total debt is estimated to be $6.2 trillion…an increase of $200 billion in 12 months.
Going a further $200 billion into the red 'bought' us $40 billion in economic activity. It's now taking $5 of debt to produce $1 of GDP 'growth'.
Debt is a drag on the economy. Income that was once spent in the economy is now being diverted into loan repayments. So how do you keep up with the Joneses? Save less.
The banks are entering into a credit-card war…offering plastic with lower interest rates.
These bank execs aren't stupid. My guess is that the boardroom thinking went something like this:
Rising household costs. Increased mortgage expenses. No pay rise.
Hmmm, we think people are going to want access to low-cost, unsecured finance to maintain the façade. Let's drop the rate on credit cards and watch outstanding balances balloon.
Let's bring in the spin doctors and tell the brainwashed, credit-dependent consumers that we are being good corporate citizens by making credit cheaper.
But they know all too well that making the drug of choice cheaper will only increase the dependency habit.
Tell me Doc, am I going mad or what?

- We have the lowest wages growth in 20 years.
- Part-time employment is increasing.
- Australia has the dubious honour of being the most indebted private sector (as a percentage of GDP) in the world.
- Our government is bleeding red ink due to health and welfare expenses outstripping tax receipts.
- Sydney and Melbourne are among the most expensive cities in the world to live in.

And they call this the 'Lucky Country'.
One day our luck is going to run out, and a lot of unlucky households are going to find out the hard way that excess borrowing does not constitute economic growth.
Bringing forward consumption from tomorrow to today is not sustainable unless the following generation has the capacity to keep the Ponzi scheme going.
And from what I see, Doc, the next generation is saddled with HECS debts, mortgages high enough to give you a nosebleed, the tax burden of having to pay for boomer retirees, **and** it has to compete with lower-cost countries for jobs. We won't even talk about what an increase in interest rates might do…that would really do my head in.
Doc, am I not seeing something?

The nonsensical market

One final thing while I've still got a minute longer on the couch. What's with the US share market?
Earnings have declined 3% over the past three years, but this bloody market keeps going up.

In my more lucid moments, I thought investors bought shares on the basis that it was a claim on future cash flows. If the cash flow is falling, why are share prices rising? I must have lost the plot.
The cyclically-adjusted price-to-earnings ratio (CAPE) is now on par with 1929, and is only bettered by the madness seen at the height of the dotcom boom in 1999.
Could it be that investors are paying higher and higher multiples for declining earnings based on the greater fool theory? Do people not recall the stock market carnage of 2000? And have they not heard about what happened in 1929?
Please Doc, help me make sense of this.
‘Very interesting, Vern. But, unfortunately, time is up.’
‘However, I think we should schedule in more appointments to continue exploring this matter in more detail.’
‘To cover my fees, we can offer you a low-cost financing plan. Are you interested?’
Aaaaggghhhh!!!”