THE BOOM - BUST ALERT
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"There is always a bull market raging somewhere on this planet" - *Byron King*

Lonely in the Bear Camp.

By Joe Average,
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"BIG PICTURE – Cash is trash! …In the world of investing, it all comes down to supply and demand…the supply of assets is not keeping pace…(with) the explosive growth in the supply of currencies. The central banks know full well that given the high debt levels, such drastic measures (genuine monetary-tightening through significantly higher interest rates and a sharp increase in the banks' minimum reserve requirements) would probably cause a global depression…
…I am inclined to think the global boom in stocks and commodities will continue for several more years ." (emphasis added).
Puru Saxena (www.purusaxena.com)

Much comment has recently been made that highly revered analyst Richard Russell has also moved to a similarly bullish outlook. The bulls see nothing ahead but soaring inflation (perhaps even hyperinflation), rising asset and commodity prices, and ever worthless currencies as Central Banks continue to increase liquidity in a desperate attempt to stave off any economic downturn.

Contrarians are thin on the ground…an endangered species in danger of extinction.

Robert Prechter (www.elliottwave.com) is still convinced that the Central Bank's best efforts will soon fail, leading to a devastating implosion of the massive debt overhang their easy-money practices have allowed to develop, and that inflation will rapidly be snuffed out and swamped by deflationary forces.

Robert McHugh (www.technicalindicatorindex.com) also is warning his readers of an imminent major plunge in stocks. The warning comes as a result of the emergence of a cluster of **three Hindenburg Omens** in June. "***Confirmed Hindenburg Omens are very rare…This Omen has appeared before all of the stock market crashes, or panic events, of the past 22 years".*** McHugh explains that a Hindenburg Omen is ***"the alignment of several technical factors that measure the underlying condition of the stock market – specifically the NYSE…"*** When a large number of stocks register both new highs and new lows then an unhealthy extreme divergence appears, which sets the warning bells ringing of the possibility of major fallout ahead.

Another Asian Crisis?

Adam Hamilton's (www.zealllc.com) latest article "China 2007 vs NASDAQ 2000" provides compelling charts that clearly show that the Chinese stock market bubble is unsustainable and ***"the odds overwhelmingly favour an imminent sharp decline in these markets".*** Hamilton's analysis shows that the recent ***"SSEC'S*** (The Shanghai Stock Exchange Composite Index) ***mania ascent is not only comparable to the NASDAQ's, but it is considerably more extreme"!*** His work shows that indexed from 18 months out from their peaks, the SSEC has so far soared 286% versus the NASDAQ's 218%. Just as amazing is that whereas ***"The NASDAQ mania capped a monster 17-year secular bull that launched way back in 1982…China's bull, on the other hand, actually began in mid-2005. To see a market go from a secular bear to a mania in just two years is extraordinary".*** Hamilton warns that a Chinese stock market crash can't help but have profound effects around the world.

July 2nd 2007 marks the tenth anniversary of the Asian meltdown that swept through Thailand, South Korea, Indonesia, Malaysia and the Philippines and devastated what the World Bank had called the "Asian Miracle". Ten years later Indonesia's gross domestic product per capita is only now returning to levels seen before the crisis; while question marks still hang over at least one of Thailand's major banks and property developers there are still trying to finish some developments aborted at the time. The question is…"How would China's neighbours handle a financial crisis today were the Shanghai stock market to crash?", given the amount of their exports heading in that direction.

According to Soedradjat Djiwandono (a US educated economist who was Governor of Indonesia's Central Bank in 1997 but was sacked shortly afterwards and lives in exile in Singapore)… ***"I'm afraid if suddenly things happen they are still not really ready yet…(a future crisis) will come from these two giants – China and the US…it can be dangerous for the other countries like Indonesia, which is not too stable in terms of its recovery effort".*** (Greg Earl, Australian Financial Review, 25 June 2007).

The man who was Governor of the Reserve Bank of Australia at the time of the Asian Crisis also recently expressed some concerns to Alan Mitchell (economics editor Australian Financial Review, 26 June 2007).
"The man who steered Australia through the Asian financial crisis has warned that the global economy is still suffering from the policy consequences of the upheaval that struck the region 10 years ago….Mr (Ian) Macfarlane <u>said the destructive policy consequences of the upheaval of 1997 were the regimes of low exchange rates, current account surpluses and big foreign reserve holdings that had been followed by China and the other Asian economies, partly as insurance against another crisis.</u>
<u>It is significant for the global economy because it is this massive surplus of savings over investment in Asia that is contributing so much to the easy credit conditions in the world and the overvaluation of assets that worry so many observers, including central banks and a lot of commercial bankers as well".</u> (Emphasis added).

So, once burned, the Asians quickly began squirreling away their reserves "partly as insurance against another crisis". Alan Greenspan called this phenomenon a **"Savings Glut",** which he acknowledged played a large part in driving asset prices to dizzying new heights and contributed enormously to the **"Wealth Effect"** that kept Western consumers spending for so long (more on this later)**.**

Spanish Flu?

The prospect of an imminent property debacle in Spain has Europeans very worried.

This nation of 40 million which experienced one of the biggest building booms on the planet (prices rising almost 300% in ten years) now finds itself facing a looming disaster. Over 800,000 homes were constructed last year in Spain, more than the total number built in Germany, Italy and France (with combined populations of 203 million).

Many were built to sell to speculators and foreign buyers (4 million homes are already owned by foreigners).

Tempted by the lure of low interest rates and easy finance, Spaniards borrowed up big, the majority at floating interest rates. Average household debt is now estimated to run over 135% of disposable income.

Rising eurozone interest rates are now cutting deep prompting fears of a panic sell off by both overcommitted local and foreign investors. Bank of Spain's foreign currency and gold reserves have fallen to the equivalent of 2 weeks of imports forcing the bank to sell off 80 tonnes of gold as well as British gilts and US Treasuries. Spain's current account deficit has soared to 9.5% of GDP, while Morgan Stanley estimates that the building boom has contributed almost !8 % to GDP.

Since Spain is tied to the Euro it cannot devalue its currency so a very painful deflation seems inevitable.

Bernard Connolly of Banque AIG has been quoted as predicting… ***"Spain is going to face the very direst of economic circumstances … a cycle of recession, deflation and widespread private sector default… a depression in fact."***

How this Spanish malady affects its European neighbours remains to be seen. The International Monetary Fund has previously warned that the structure of the European Monetary Union leaves it vulnerable to "systemic financial risk".

The "Wealth Effect".

Former Federal Reserve Chairman Alan Greenspan is credited with inventing the now famous "Wealth Effect Theory".

Robert J. Samuelson (Newsweek, 17 October 2005) described the "Wealth Effect" thus;

"Ours is a wealth-driven era, when huge increases in home values and (before that) stock prices make people feel richer and cause them to buy more. They spend more of their regular incomes, borrow more…You can imagine this "wealth effect" as a powerful afterburner that's boosted the economy for roughly 20 years".

Well, it now seems that the BIS (The Bank for International Settlements) may see things somewhat differently.

Adrian Rollins (Australian Financial Review, 25 June 2007) writes ***"Households have accumulated large liabilities that could put them at risk if inflation accelerates or the global economy stalls, the Bank for International Settlements has warned.***
…(current conditions) have encouraged households to spend and take on debt… households have become increasingly exposed to the risk of a downturn in the economy.
<u>The BIS said rising house prices implied a redistribution of wealth from future buyers to existing homeowners, rather than a net increase in wealth, and warned that increasingly indebted households might be hit hard by an economic downturn.</u>" (Emphasis added).

Hang on a minute! Did I get that right?

Is the BIS now telling us that that all this talk about the "Wealth Effect" is so much delusional nonsense? That the supposed wealth created by this massive property boom was merely our generation taking away the wealth from future generations?

Now *that* may not be a legacy our kids thank us for.

All the best, Joe.

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