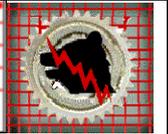




## THE BOOM - BUST ALERT



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"There is always a bull market raging somewhere on this planet" - Byron King

### Crunch Time for Debt.

By Joe Average,

July 2008.

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**"Consumer boom shows US out of the woods... Despite the jump in energy prices and the related collapse in measures of consumer confidence, retail sales rose by 1.1 per cent on the month, the strongest gain since November...If there were going to be a US recession in response to the credit crisis, it would have started by now. So let me stick my neck out and say without qualification the US is out of the woods."**

Anatole Kaletsky, *The Times* June 18<sup>th</sup> 2008.

Thank Heaven for the resilient US consumer, soldiering on stoically under an enormous burden of debt.

Perhaps Kaletsky (economics guru at the influential Times) is correct. We'll all find out soon enough. If, however, he is wrong...then his call will almost certainly go down in the history books along with that breathtakingly wrong call of **John Maynard Keynes** who on the eve of the Great Depression (Summer of 1929) reassured the world that ... **"There will be no more crashes in our lifetime."**

Not so sanguine about the future is Bob Janjuah (Credit strategist for the Royal Bank of Scotland) who has recently warned clients to brace for an all-out crash in global stock and credit markets within the next three months. His research team believe the S&P 500 could plunge up to 25% as **"the chickens come home to roost... A very nasty period is soon to be upon us – be prepared... Cash is the key safe haven. This is about not losing your money, and not losing your job... The Fed is in panic mode."** He also believes that the deadly force of **debt deflation** will grip the world over the next eighteen months.

A report out of **Morgan Stanley's** European office also sees trouble ahead. They fear a looming confrontation between the U.S. Federal Reserve and the European Central Bank over monetary strategies regarding interest rates and run-away inflation **"could trigger another catastrophic event"**. European countries to be hardest hit will be those that have accumulated extreme current account deficits like Greece (14%), Spain and Portugal (10.5%), Latvia (25%) and Bulgaria (22%), as will those countries that have allowed soaring credit growth to exceed 40 – 55% per year because **"A crunch is looming in 2009"**.

The reality is that the great love affair consumers have been having with debt over the past few years will likely end soon as they buckle under the unprecedented and onerous weight that the borrowing binge has built up... and the hangover will be nasty. At the same time, corporations that had relied on highly geared financial structures are now realizing that, with a global credit crunch and the rising cost of servicing debt, the highly leveraged model is unsustainable and dead.

### **Worth Their Weight In Gold?**

As enormous losses are crystallized in stocks, real estate markets, and hedge funds, the public mood is fast souring towards some of the high fliers responsible. Some who were held up or held themselves up as being super intelligent and clever ("gurus"...even "Masters of the Universe"?), are now seen to have had feet of clay.

The huge sums that some of these captains of finance were able to demand for their talents went unquestioned while the good times rolled; but now serious consideration is being given as to their real worth.

Phillip Adams (Weekend Australian Magazine, June 21-22 2008) may have tongue planted firmly in cheek when he writes about the new head of Macquarie Group, Nicholas Moore, who has stepped into the shoes of Allan Moss (who earned \$34 million in 2006-07 and retired with a controversial \$80 million golden

handshake). Adams is bemused that Moore ***“will be paid more than the entire (Australian) Federal Parliament. More than all the senators and all the members of the Reps. The whole 226 of them... he’ll get nearly 100 times what we pay the Prime Minister.***

***To get a feeling for Mr Moore’s awesome importance, compare his richly deserved salary to the token payments for lesser creatures in the fiscal food chain. Like teachers and nurses. Mr. Moore’s little finger is worth more than the entire staffs of public schools or major hospitals. The nail clippings that fall to the floor during his manicures exceed in value half the scientists at CSIRO. His dandruff, if he has any, is worth more than gold dust...He is our messiah of money.”***

Meanwhile, two senior executives at Bear Sterns (Ralph Cioffi and Matthew Tannin) have been arrested and led off in handcuffs to a Brooklyn courthouse to be charged with nine counts of securities, wire and mail fraud.

***“This is not about mismanagement of a hedge fund investment strategy...It’s about premeditated lies to investors and lenders. It’s about defendants prostituting their clients’ trust in order to salvage their personal wealth”*** said Mark Mershon, head of the New York office of the FBI.

They stand accused of encouraging naive investors to sink money into two funds they knew to be collapsing and which shortly later imploded wiping out \$1.6 billion of investor’s savings, triggering a global emergency that resulted in further losses of \$350 billion and the eventual demise of Bear Sterns.

Writing in The New York Times, Landon Thomas described how Cioffi lied to one rattled investor who was intent on withdrawing his \$57 million by telling him he himself had \$8 million of his own money in the fund (out of his net worth of some \$25 million).

Tannin supposedly gloated to a colleague ***“Believe it or not, I’ve been able to convince people to add more money”*** even as Cioffi was quietly withdrawing some of his own funds. When Tannin finally looked to be cracking under the strain of it all, Cioffi scolded him to stay the course by saying ***“We are not 19 year olds in Iraq!”***

Some compliment to the young men and women serving in Iraq.

## **The Worst is Over?**

***“Those who have been clinging to the view that the ‘worst is over’ were bowled over by those rushing for the exits.”***

*David Bassanese, Australian Financial review June 10<sup>th</sup> 2008.*

## **US Local Government Fails.**

***“The US town seeking bankruptcy protection may be the first of many...When Vallejo, a blue-collar dormitory town north of San Francisco, filed for Chapter 9 bankruptcy, the event sent fiscal shudders across a country in which state and local government finances have hardly been as precarious since the Great Depression.”***

*Tony Walker, Washington correspondent Australian Financial Review.*

## **Housing Woes Continue.**

***“We’ve seen a real change in the market... Finally the banks are capitulating and saying they will mark to market and flush this (foreclosed homes) all out. The market is going to get worse. We don’t want to hold on to this stuff.”***

*Ricardo Chance, KPMG Corporate Finance.*

***“I’ve been through three cycles, and this is the worst. You can buy new homes for less than the construction cost.”... (thanks to the glut of foreclosed homes).***

*Mark Connal, V.P. Michael Crews Development, California builder.*

## **Oil and Commodities Bubble?**

***“In my view the price of oil is at least 40 per cent overvalued. Twenty per cent of the current price is attributable to foreign exchange effects and the weakness of the dollar, another 25 per cent is down to***

**speculation. I expect a clear market correction and that the bubble will burst. In my analysis, the longer-term price trend is between \$US80 and \$US90 per barrel of crude.”**

*Klaus Gretschnann, EU Council of Ministers.*

**“The cost of food and energy is creating severe economic distress for millions of working families in America and around the globe... We are not, as some continue to argue, witnessing the ebb and flow of natural market forces at work. We are instead seeing excessive market speculation at work and that is why our government must step in (to curb speculation in commodities markets by large pension and government funds).”**

*Joel Lieberman, Independent US Democrat senator.*

All the best, Joe.

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