# Richard Cluver Predicts

*In our 27th year of service to the investing public of South Africa*



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**Writing in their Quarterly Review, US economic research group Hoisington Investment Management direct readers to important new research by four distinguished economists (three in Europe and one in the U.S.) that is contained in a report titled "Deleveraging? What Deleveraging?" (Luigi Buttiglione, Philip R. Lane, Lucrezia Reichlin and Vincent Reinhart, *Geneva Reports on the World Economy 16* September 2014). It provides additional evidence on the role of "debt dynamics" and the state of the global debt overhang.**

They write, "Contrary to widely held beliefs, the world has not yet begun to de-lever and the global debt-to-GDP is still growing, breaking new highs." Further, it is a "poisonous combination" when world growth and inflation are lower than expected and debt is rising. "Deleveraging and slower nominal growth are in many cases interacting in a vicious loop, with the latter making the deleveraging process harder and the former exacerbating the economic slowdown."

This research also identifies two other highly significant trends. First, global debt accumulation was led by developed economies until 2008. Second, the debt build-up since 2008 has been paced by the emerging economies. The authors write that the rise in Chinese debt is especially "stunning". They describe China as "between a rock (rising and high debt) and a hard place (lower growth)." In addition to China they identify India, Turkey, Brazil, Chile, Argentina, Indonesia, Russia and **South Africa** as belonging to the "fragile eight" group of countries that could find themselves in the unwanted role of host to "the next leg of the global leverage crisis."

At the heart of the Hoisington report is recognition that as the global debt bubble continues rising, the probability of a series of economic "Hard landings" becomes increasingly likely. Their calculations suggest that the combined debt of the US Government and its citizens has now exceeded 334 percent of US Gross National Product with the result that so much income is having to be re-cycled to meet repayments that very little remains to fund economic growth which explains why against a 200-year GDP growth rate average of 3.9 percent the average US GDP growth rate for the past five years has been a dismal 1.4 percent.

While business conditions are poor in the US they are infinitely worse in Europe and Japan. The issue for Europe is whether that economy triple dips into recession or manages to merely stagnate. For Japan, the question is the degree of the erosion in economic activity. This is for an economy where nominal GDP has been unchanged for almost 22 years. U.S. growth is outpacing that of Europe and Japan primarily because those latter economies carry much higher debt-to-GDP ratios. Based on the latest available data, aggregate debt in the U.S. stands at 334%, compared with 460% in the 17 economies in the euro-currency zone and 655% in Japan.




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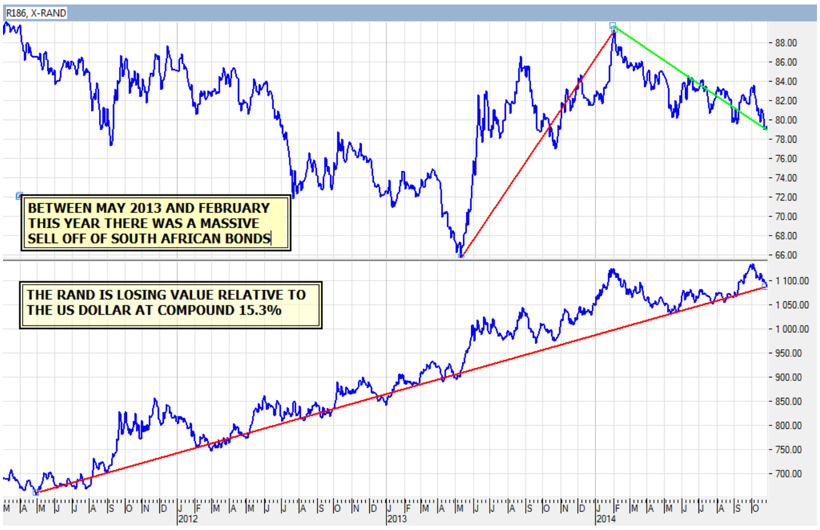
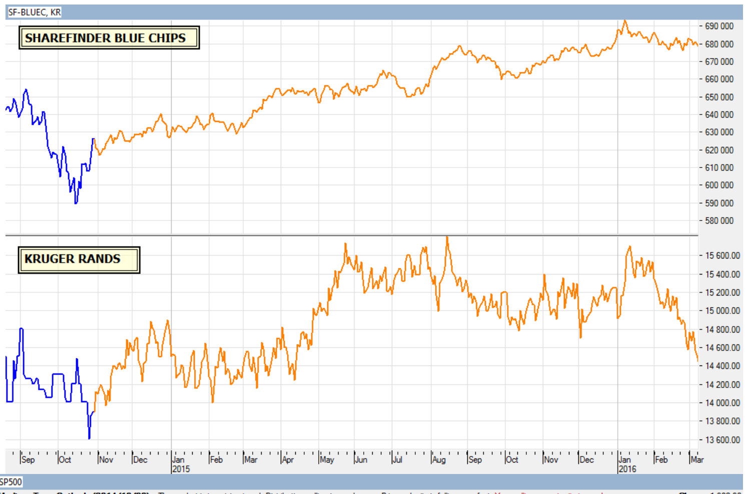
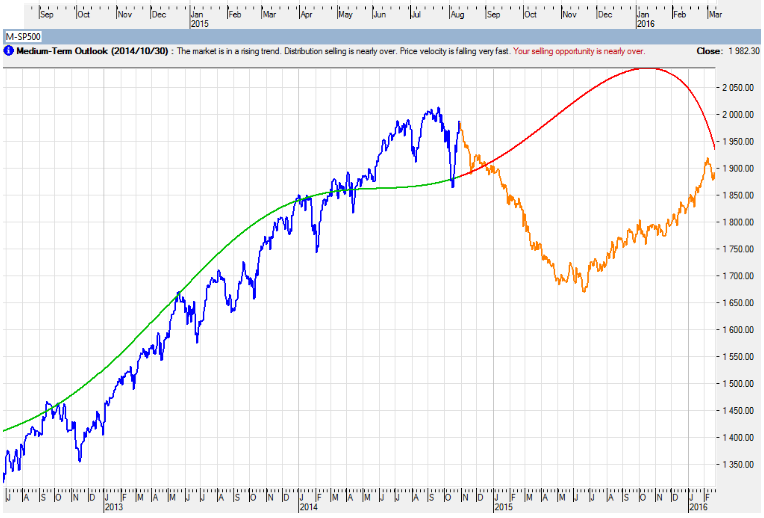
Here in South Africa where ten percent of all State income now goes to servicing debt, the risk to the day to day buying power of ordinary folk is a probable collapse of the Rand\Dollar exchange rate as the “carry trade” unwinds. I have written frequently in the past about this danger, but to briefly recap, the artificially low interest rates that have been the consequence of the US Federal Reserve’s Quantative Easing policy have enabled international traders to borrow US dollars at insignificant cost and they have employed this money to buy comparatively high yielding South African treasury bonds. Now that Quantative Easing has ended and interest rates are beginning to climb, those positions are beginning to unwind. Although most of 2014 has been marked by renewed bond buying, the probability is that we could in the future witness a massive sell off as carry trade positions are unwound like they did between May 2013 and January this year and the consequence could be a catastrophic loss of the value of the Rand which is anyway losing value at 15.3% compound relative to the US dollar.




In a bid to counter this outflow of capital which has up until now been shoring up loans to the government to fund its growing fiscal deficit, we might expect the SA Reserve Bank to raise interest rates which will cause great hardship to a very overborrowed South Africa, further slow an already sluggish economy and significantly weaken the Johannesburg Stock Exchange.




What can ordinary investors do to protect themselves against the consequences of this deadly cocktail? If you have followed my recommendations in recent months you have already accumulated significant percentages of cash in your portfolios. Now it is time to use this cash to invest in the very bluest of blue chip shares, preferably those with significant overseas exposure, and in Kruger Rands.




My projections of both Blue Chips and Krugers suggests that both have now bottomed out and are likely to continue rising for the foreseeable future. But, just a note of caution, Wall Street is poised for a significant correction which, if ShareFinder’s Fourier projection system is as accurate as it has been over the past 20 years, could mean that we can expect a double dip process lasting until late 2016.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## The next month:

**New York's SP500:** I correctly predicted the start of an Indian Summer recovery which I see ending on Monday.

**London's Footsie:** I correctly predicted further recovery which I continue to see lasting until late November.

**JSE Industrial Index:** I correctly predicted losses until the middle of the past week followed by fresh gains which I expect to last until mid November.

**Top40 Index**: I correctly predicted gains until Wednesday followed by brief weakness. Now I see gains until Tuesday followed by declines for the rest of the week with gains in the following week.

**The ShareFinder Blue Chip Index**: I correctly predicted a brief recovery which I now see continuing until mid-November.

**The Rand**: I correctly predicted a recovery continuing until the end of the month. Now I see weakness beginning and continuing until November 12 before a volatile recovery trend begins.

**Golds:** I correctly predicted continuing declines which I foresee lasting until mid-November.

**Bonds:** I wrongly predicted weakness. However I continue to foresee weakness lasting until mid-November before the next bout of recovery begins.

***The Predicts accuracy rate on a running average basis over the past 522 weeks has been 82.61%. For the past 12 months it has been 89.1%.***

**Richard Cluver**