



## **My View**

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### ***A Double Scoop?***

Last week I wrote informing you that I had spent a number of days in New York City and Washington D.C, speaking with and listening to some not only fascinating individuals but also legends in the capital markets. Over the next several weeks, I had also promised to share with you some of their thoughts, projections, and observations which I would capture in bite sized pieces.

***So the first question is; with all of this volatility and recent pull back in the markets, are we going into a global double dip recession? The unanimous answer from each and every person “NO”***

Last quarter, Canada’s annualized Gross Domestic Product growth rate stood at 6.1%. A stellar number by anyone’s standards. Companies are reporting higher than forecasted profits, unemployment figures (a lagging indication) are dropping, consumer confidence is returning, and the Fed’s just raised interest rates because of the strong economic results. ***So with all that being so good, why the pull back in the market?***

The answer is a number of various factors coming together to create the scenario. The emerging markets which represent growth and opportunity rely upon the mature economies to purchase products that they manufacture. Europe and North America, by and large has a number of such mature economies whose consumers are older and require less “stuff”. The fear is that countries like China and other emerging nations will see their exports reduced, prior to having the opportunity to develop their own middle class consumer. China’s economy is slowing down from the torrid pace it has been on for the last fifteen plus years to a more manageable and sustainable level. This is good, as it will not drive inflation upwards and allows the economy to grow at a much more controlled and sustainable level. Let us not forget it is still clocking in at just under 9% GDP growth, in fact China’s exports are up a staggering 36% over last year, while India’s industrial production numbers have also improved.

Trade barrier concerns seem to be less of a concern today versus a few months ago, however, depending on how the next few months play out, this once again may become a real area of concern as select economies put in measures to make their own goods more attractive financially, while making imports more expensive.

Greece, Portugal, Spain, Italy and Ireland are all member countries of the EU. Due to the lack of oversight and prudent government management of revenues, they find themselves in a situation which is garnering a lot of attention as it relates to their sovereign debt. One of the most interesting things to note is, lets say Germany owes Greece one hundred billion, Greece

owes Germany two hundred and fifty billion, France owes Italy one hundred and seventy five billion, and Italy owes France three hundred billion and so on and so on. Everyone owes everyone else money which is all subject to interest payments. Would it not make sense to do an accounting of debits and credits, wipe out the overlap and just be left with the balance owing? Pay interest on just the remainder and free up the excess cash flow to pay down the balances, lower taxes, or stimulate sectors of their economies. I admit that this sovereign debt solution is over simplified, however, is it really much more than that?

The challenge with the euro zone, specifically the P.I.G.S (Portugal, Italy, Greece, Spain) is not that they represent that much debt, or their economies are that significant in relative terms, but it's the perception and trickle down effect that is causing emotions and speculation to run rampant, which has an overall reflection on the European community.

The recent adjustment of interest rates by the bank of Canada is an attempt to take us away from the 0.25% crisis rate which just can not be maintained indefinitely. With this upward pressure Canada should also see a strengthening of our currency. Canadians are taking on too much debt, and the government wants to lower housing prices by raising interest rates as well. Canada is a resource based economy and if globally the need for oil, gas, copper etc is weak, then that will hurt economies like ours. However on the other side of the coin, the world needs what we have. Add to that, we are safe, friendly, accessible and willing to sell it..... we should fair well. Our economy represents less than 2% of the worlds GDP and roughly 60% of that is in just a few sectors. This contributes to our volatility, hence the need to diversify out side of this great country, in order to find a better, long term, and sustainable balance.

Closer to home in 2009 we have seen Alberta and Ontario tied for the worst performing provinces. In 2010 we will witness the start of growth, however we will probably lag the rest of the country in job growth. By 2012 we will once again be experiencing a labor shortage for niche and highly skilled labor. Oil is profitable for Alberta but we have a lot more natural gas, which has been underpriced and subsequently affecting provincial revenues. Currently there is a surplus of natural gas and our biggest customer, the U.S has discovered their own shale gas. Fortunately for us, the reserves of U.S shale gas are small and there are issues surrounding its extraction. Over time natural gas will return to sustainable cost levels and Alberta as well as the rest of Canada will once again benefit from that. In 2011 we should once again lead Canada or at the worst be in the top two.

Since most of the worlds eyes seem to focus on the U.S.A for its production, lets examine how they are doing.

Housing and unemployment remain the two big concerns.

2009 Fourth quarter GDP growth was up 5.6%.

2010 First quarter is estimated to be up 3.2%, while the second quarter is projected at 3%, third and fourth at a little over 2%.

Leading weekly indicators are up; employment is improving but still continues to be a drag. Housing starts have stopped their slide; however prices are still slipping in value. Consumers are once again starting to spend and much earlier than expected. Personal saving rates had jumped to 6% but are starting to drop a little. Leverage is still too high, currently at 120-130% of disposable income; household net worth is showing positive numbers growth. The U.S dollar must decline in relation to other currencies in order to assist in solidifying their recovery. The Euro must gain in strength otherwise the Americans will impose tariffs to make the European imports more expensive and safeguard their own manufacturers.

The last investment decade was a net sum zero one, however the next one should be good. ***Currently we are in the beginning stages of a bull market. Historically we have always experienced pull backs, not unlike what we are currently going through even during a bull market.*** In fact they are good for the overall health of the markets. The current equity markets are not over priced, there still exists plenty of opportunity and if we look at the private placement market, mergers and acquisitions sector, they have been pedal to the metal since the beginning of the year. Those areas are leading indicators of things to come.

Commodities also go through cycles; the shortest one in history was sixteen years. We are now in year nine. Countries like China and India are and will continue to have a huge impact on the commodity sector. Gold has taken on a whole new shine. There are three major influences:

- The baby boom retirement sector
- Deep government budget deficits
- Conversion of interest rates in the Euro currency.

Governments typical ease monetary and physical policies in a recession. Running 100% debt to GDP is a possibility that may become a reality for several nations. Unfortunately that will result on some renegeing of sovereign debt obligations, cuts to social spending, and raising of taxes for those nations.

There was an unprecedented amount of stimulus injected into the global markets as a reaction to our perfect storm of 2008 - 2009. We need to remove financial stimulus in order to de-couple that action. The trick, as I said way back when, will be to do that in such a way that will not stall the economic engines while over time allowing economies and markets to return to a sustainable equilibrium.

In my next “my view” article, I will share with you what Mr. Wilbur Ross (Mr. Distress) and a close colleague of Warren Buffet, has to say about the current goings on.

Finally a nice weekend!

That’s my view

Victor

