



On My Radar

September 7, 2012

By Steve Blumenthal

As I dive through a broad range of independent research each week, I include several pieces that I found important. Following are the *bullet points*, in no particular order:

- **Deleveraging Studies by Ray Dalio:**

Ray manages the world's largest hedge fund and he and his team are among the smartest investors on the planet. From Ray's piece: "As deleveragings are very different processes than recessions, and as we believe that we are now in a global deleveraging, we know that we must thoroughly understand the deleveraging process in order to successfully manage money. These deleveraging studies were done for this purpose." Ray Dalio.

http://images.mauldineconomics.com/uploads/overmyshoulder/Delevergaing_Studies_BridgewaterDraftConfidential.pdf. My partner John Mauldin sent this out a few weeks ago. It is long but well worth the read (focus on the first 20 or so pages).

- **Brinkmanship as Spain warns over bail-out terms:**

"Spain has issued a veiled warning that it will not accept a full bail-out from Europe if the terms are too harsh, a move that would paralyse the European Central Bank and call the euro's survival into question." This will give you a sense as to the enormity of the problem in Europe. Here is the link:

<http://www.telegraph.co.uk/finance/financialcrisis/9521465/Brinkmanship-as-Spain-warns-over-bail-out-terms.html>

- **From NDR Research. September 6: The ECB Meeting: "The Worst Possible Decision... Except All Others?"**

Mario Draghi had set expectations with his July 26 comments and he delivered with today's decision announcing Outright Monetary Transactions (OMTs). This potentially means unlimited purchases of troubled sovereign debt in the secondary market. This is ONLY for countries that accept the EFSF/ESM macroeconomic program or a precautionary program. That would not include Spain or Italy at this point (see above bullet on Spain). There remain a number of very gray areas. For one, Spain matters.

- **September 12, 2012:** On September 12 the Federal Constitutional Court of Germany will rule on whether Germany has the right to support the ESM. We wait... risk exists.

- **Global Recession Watch: Asian exports crumble**
“Exports from Asia, the world's manufacturing hub, are often regarded as a bellwether for the health of the global economy.” The link below takes you to a chart on Asian aggregate export growth to the US, EU, Japan and the rest of the world. The world is in slow down or recession. This from Ambrose Evans-Pritchard citing research from Nomura.
<http://blogs.telegraph.co.uk/finance/ambroseevans-pritchard/100019794/asian-exports-crumble/>
- **US Recession Watch:**
“Since retail sales were first reported in 1947, there were 27 times that retail sales were negative for three consecutive months. 25 out of the last 27 times retail sales were negative for three straight months, the US economy was in recession or within three months of a recession.” Gary Shilling

June 2012 marked the third consecutive month of decline. To watch the Bloomberg TV interview: <http://www.businessinsider.com/gary-shilling-collapse-in-retail-sales-signals-a-recession-2012-7>

The problem is simply too much debt. No small problem. Whether there is a magic rabbit that Mario, Japan or the US, for that matter, can pull out of their bag of tricks remains to be seen. We'll get through it, but it will be bumpy. This will be a period marked by more frequent recessions as we work our way to a better secular destination. I'm alarmed at the immediate US recession risk. Few are expecting it.

I believe that from the depths of the greatest difficulties arise the greatest solutions. This time is no different. We creative human beings will find our way. In the meantime, include a number of non-correlating tactical trading risk diversifiers to your more traditional portfolios.

Finally, a quick aside: I printed out the first 20 pages of Dalio's Deleveraging piece and asked my two boys to read it. I told them it would give them a better understanding of how the world works. That idea didn't go over so well as you might imagine. Ages 14 and 13, they looked at me like I was nuts and said, “Come on, your kidding right?”. Followed by, “what's for dinner”. Great. Ugh. Perhaps a capitalistic solution is required: \$5 bucks to the first kid who can correctly answer just three questions. I'm going back in. The quiz will be on Sunday night.

With warm regards,

Steve

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