

## Credit Crunch

29<sup>th</sup> February 2008

Is inflation is just what the doctor ordered it may well be in the USA's case. The old quacks that run U.S. monetary policy prescribe inflation as an antidote to deflation. Are we to take it that they are saying its better to let the fever rise, than let the patient die?

My comment on this would be the death they fear is the kind suffered by the Japanese economy after 1989. It was as if they had subjected the Japanese economy to water boarding and forgotten to pull it up out of the water. The economy drowned. Members should note that even now, 18 years after the Nikkei Dow went under; the poor thing is still coughing up the dregs.

RIO is in a helpful mood again. Last week, I promised some buy-side suggestions. Here's one:

The story in a nutshell: While credit and speculation ran wild in Britain and America – from the mid '90s to 2007 – the Japanese struggled to raise themselves up off the floor. Each time they tried, they just fell down again. The Nikkei Dow, once at 39,000, bounced around at the 12,000 – 15,000 level. Each time it looked like things might be looking up, wham. Back down on the floor.

The latest bruises came in 2007. After getting roughed up for 17 years, finally, it looked like Japan, Inc. was back in business. And then, along came sub prime and the worldwide credit crunch. Japan didn't have any sub prime debt. Its bankers, investor's consumers and businessmen had grown cautious and conservative over the years. In America, a downturn is believed to be temporary. Almost everyone believes it will be over by July. Some think it is over already – after only a modest pullback in GDP growth. Our research indicates that in Japan, people think a downturn is permanent. "It will never get better," they say to one another. "It will get worse."

"In Japan, the opposite psychology [from the USA] has been in effect," in recent e-mail to a member I wrote that Japan was in deep recession for 13 years after its bubble burst in 1990, so traders and analysts had grown used to discounting the government's positive announcements as mere spin. When the sub prime mortgage crisis occurred in August 2007, while U.S. analysts ignored the problem, Japanese analysts decided it must be very bad news for Japan, even though no Japanese banks had more than minor exposure to the market.

In America, investors ignore gloomy circumstance. In Japan, they pay attention to gloomy circumstances that don't even exist. So when the credit crunch hit world equity markets, it fell upon the Japanese like kamikazes on the U.S. fleet. Japan's great companies were sunk...with the Nikkei Dow suffering more than twice the losses of its American counterpart. Did any members notice that the Japanese stock market was the worst performing major market in the world – following the sub prime crisis, even though Japan has no sub prime mortgage debt? Well I did and would sight that this market has discounted bad news that has not happened.

In my opinion the Japanese market has ignored the continuing evidence of Japan's fairly strong growth and negligible inflation. Even a housing problem, that has led analysts to forecast a huge drag on Japan's economy similar to that in the United States, turned out to have resulted from new tighter housing permit regulations, which caused a dip in new construction that is already ending. There is no sub prime mortgage problem – how could there be? The Japanese housing market had a catastrophic downturn in the early 1990s, when Tokyo house prices dropped in some cases by as much as 70%, so there was no possibility of a price spike or lending bubble against that background.

Even with the market sharply down, the economy continuing solid (fourth quarter GDP growth was 3.7% double the forecast) and analysts negative, Japan appears a safe haven in an uncomfortable world, this is why I have not sold the positions take previously for those members who still hold Hansard Pinnacle investment as this is a long term investment product. I would say that it is more than likely that the Japanese market it is likely to lead the world upwards at the end of the current unpleasantness.

With my right flank is in retreat. My left flank is giving way. And the centre cannot hold. Conditions perfect for RIO, I will attack!

Likewise, conditions are perfect for precise positioning in Japan. My extensive research has indicated that many foreign investors have given up. Domestic investors aren't interested. And stocks are trading at very low prices, with half the companies listed selling for less than book value.

Where to put your money now?

### **RIO Professional Investors Fund**

As it will benefit from the above opportunity with the current active management strategy employed. Add to that the advantage of this fund excellent trading record since inception and then top it all with the fact that it also offers the investor exposure to the explosive investment potential above, without the negative of being totally exposed due to advanced trading and the funds obvious diversity.

For those members who followed my recommendation last weeks to buy Sterling at below 1.95 for a move to 1.9870 in the short term i.e" very soon". I am glad that this trade closed for you, thank you for your e-mails on this subject. Those who are still processing your applications for inward investment to our Sterling based Funds with the proceeds of the above I appreciate your continued support.

**William Gray**  
**Executive Chairman**  
**The RIO Club**