It’s a clear case of “Good Money After Bad”

18.5.2010

As I mentioned in my last report; Rescues sometimes have happy endings. Households, companies, and even governments can sometimes with enough self-discipline and some luck be pulled back from the brink. That said they must be at the brink, not beyond it.

For example, of Ireland. When world markets turned down in 2007, the Emerald Isle faced ruin. They had over done it, just like Britain and America. Its banks, its households and its government had too much debt. At the brink, it took a knife to public spending, pledging to cut 7.5% of GDP out of the government's budget. There was a lot of grousing and complaining. The Irish seemed to be taking their much needed surgery with good grace at the end of the day.

The most important detail being the fact that it was not too late!
The Irish have a national debt equal to only 50% of GDP - about a third of the Greek total. Roughly, with a modest GDP growth of only 2.5% annually the Irish could sustain their debt indefinitely. If they stick to the program, the debt problem could perhaps disappear.

Another example is South Korea. The Koreans faced disaster during the Asian Debt Crisis of 1997-'98. The banking sector had lent too much to the nation's conglomerates. When the latter couldn't pay, the former were in trouble. Emergency loan programs were put in place. The conglomerates were forced to merge, sell, or scale back. Most remarkably, the South Koreans showed a spirit of solidarity that revealed an alarming lack of cynicism. In 1998 the government began a campaign called "Collect Gold for the Love of Korea." Millions of people voluntarily turned in their gold jewelry in order to help the government pay off foreign loans, truly amazing!

South Korea was the best performing economy before the crisis. It was soon the best performing economy again. The national debt never rose above 30% of GDP and soon ceased to be a worry.

But when I take a look at the great European bailout? I am asked by members will the recently put in action “rescue plan” make the debt problem go away? I will waste no time and cut right to the chase: 'No' is the answer.

Many of the debts had passed the brink a long time ago. An in-depth look at the facts shows this to be the case. There is no way they can be revived it’s just that simple. To put it bluntly, Europe is wasting its blood transfusions on a corpse.

The problem with Europe is that some of the peripheral states can't keep up with the interest on the money they borrowed. Greece, for example, is scheduled to have debt equal to 150% of GDP by 2011. Even at 5% interest, it will take GDP growth of 7.5% per year just to keep up with the interest payments. Since growth in Greece is not expected to come in anywhere near 7.5%, and will probably even be negative, it will sink further into debt.

My point being that there is no reasonable assumptions one can make that show how Greece could ever repay the current debt, let alone more of it. My comment is that the debt has gone bad. It cannot be repaid, I predict that soon others will see the obvious.

This Bad debt will not just disappear!!!!
Europe's leaders have merely passed it along to a broader audience.

I would warn members that soon the short comings of Greece, Portugal, Spain will be added to all the bad debt of the subprime borrowers, this will begin to haunt the whole continent. And it will not go to its eternal rest until it is satisfied.

How do you satisfy a bad debt? The lenders for most part the bondholders - should write it off as soon as possible. That's not happening, Instead the horrible truth shows that the new bailout follows the pattern of modern macro finance. Small debts become big ones. Problems in the present are pushed into the future. And people who deserve to lose money are protected, while the public takes the loss.

It is hard to imagine how European leaders could have done worse. Money is transferred from the private sector to the public sector, where returns on capital typically are far lower and often negative. Debtors are allowed to borrow more, with no hope that it will ever be repaid. Overall, debt increases, as debt from the bailout is added to the original debt. Future industries are deprived of the capital now being re-allocated to bankrupt governments. And by paying off the bondholders, the government directs capital to people who obviously don't know what to do with it.

I see big trouble ahead and forecast that volatility in the markets are almost certain.

Having read my reports some members have astutely reduced their cash holdings after all the bank is offering a minuscule 0.5% return on deposits. Add to that the continued risk of reduction of the purchasing power of paper money and well, you get the picture.

Recommendation; buy RIO International Investors Fund this fund trades Gold which will very likely see further upside as the above scenario plays out. This fund gained 1.29% in April alone and is positioned to see a consecutive gain yet again this month as trades set are all closed in profit. Finally, I am confident that the current and continued debt situation will benefit this fund.

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