



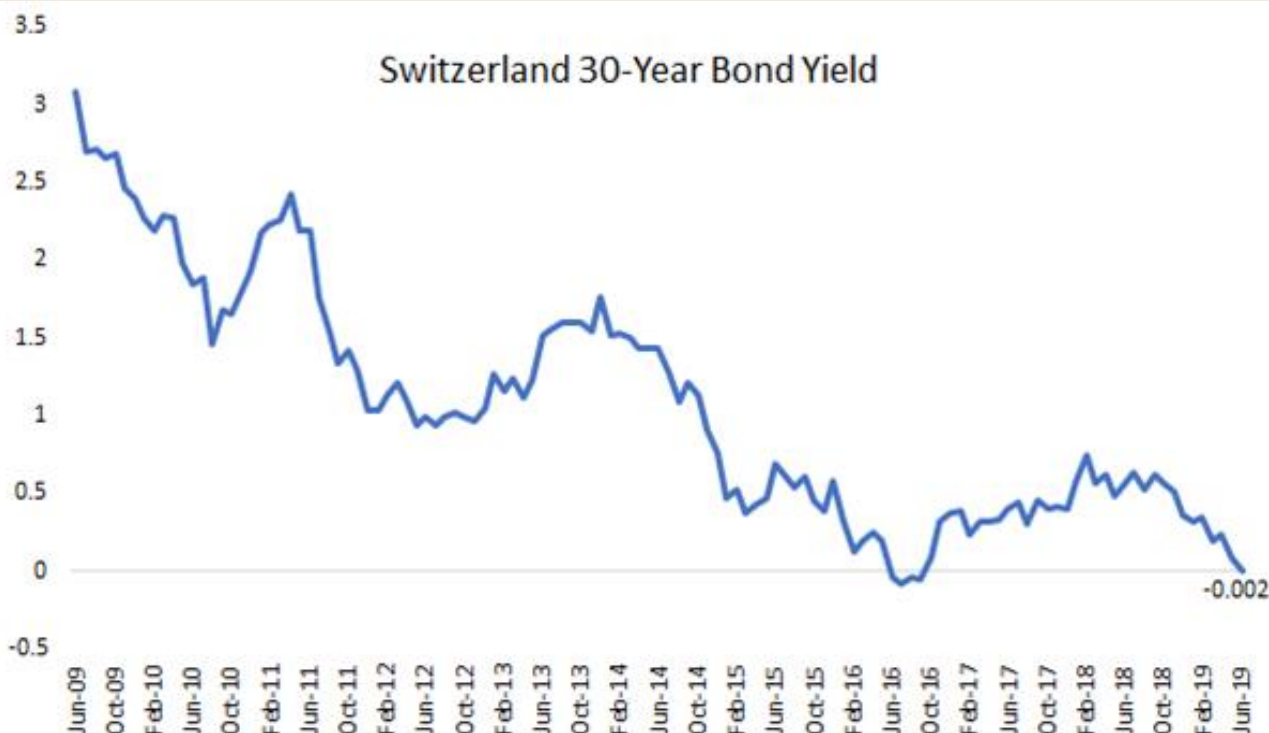
In this Booms & Busts Report:

1. Interest rates
2. Energy investments
3. (Commercial) Property funds
4. Gold

Have you heard the one about investors lending to Switzerland, for the next 30 years, and 'receiving' a negative interest rate, for the 30 years?

Normally, I start Booms & Busts Reports with some kind of a less serious comment, to start off with a bit of a laugh. But I can't think of anything funnier than lending for 30 years and PAYING the borrower to borrow!

Swiss 30 year lending interest rates



So, Jonathan, are you saying that the rate of 'interest', on loans to the year 2049, is MINUS .002% per annum???

Yes, that is what Switzerland was borrowing 30 year money at, earlier this Summer.

The idea that Switzerland will have deflation, for a third of a century is preposterous, to my mind. It's even more preposterous that portfolio managers are investing in that way.

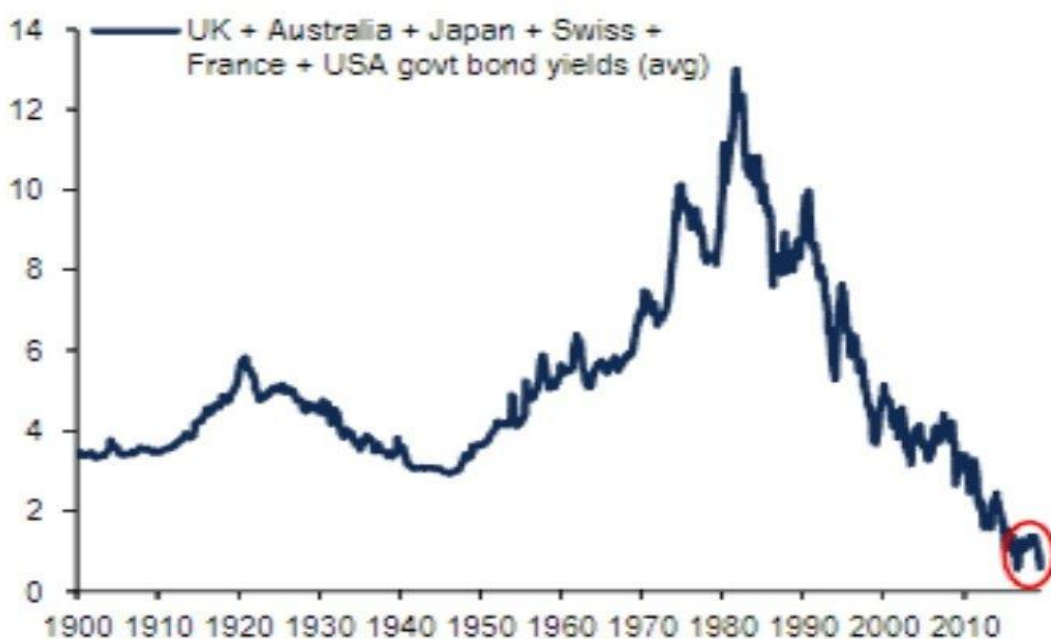
Or, they need to park money, safely, (and there is nowhere safer than Switzerland) and To Hang with the returns. They also say to themselves, if inflation comes to Switzerland (If? In 30 years?!) then we'll pull the money out and put it into inflationary assets.

Well, wouldn't they be the smartest guys in the room if they could do that. And no-one else can, who also made this investment. It seems to me they're all piling on, like lemmings, and they will all, in due course, jump off, like lemmings.

Thus, that is why we have such incredibly low global interest rates. Practically every market sentiment survey indicates that global market participants anticipate a stock market bust - at or near All Time Highs! (An ATH is not normally associated with a bear market.) So, they put their money (their clients' money) into government bonds. This, of course, boosts Bond prices and cuts yields (market interest rates).

Global Interest Rates at 120 year low

Chart 4: Global bond yields at 120-year lows



Source: BofA Merrill Lynch Global Investment Strategy, Bloomberg, Global Financial Data

This is what I call extreme! (And they wonder why house prices are so high...!)

So, to be clear, pension funds and other investors have so driven up Bond prices to such an extent that, globally, rates are not just the lowest since the year 1900 (even lower than the 1930s! and the 1960s!) but at practically 0%!

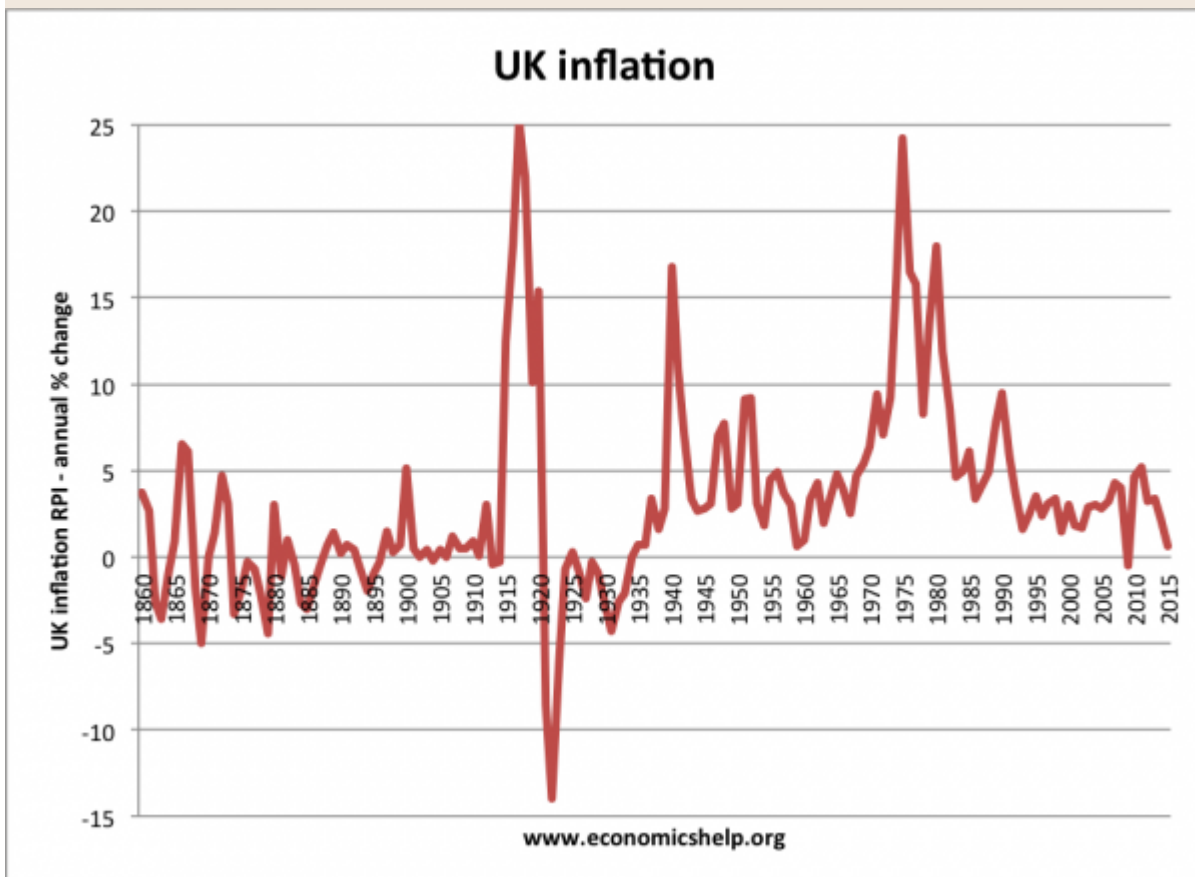
You know, there are over \$13 TRILLIONS of Bonds (Government and Corporate) with NEGATIVE yields. That's a quarter of Bonds out there. In fact, 87% of all bonds pay less than 3% pa.

It will not take much of a tick up in inflation, globally, for all these to lose money (higher interest rates means lower Bond prices).

How much of your money has been invested, without you knowing, on a NEGATIVE interest rate basis? You might want to ask your wealth manager.

So, might all these fund managers be right? That inflation can only fall into deflation, for 10, 20 even 30 YEARS?

UK Inflation, from 1860



The chart is UK inflation, from 1860 to 2015.

We had DEFLATION in the 2nd half of the 19th Century, as technology and globalisation kept bringing down our costs of living.

World War 1 *suddenly* brought MASSIVE inflation as did WW2, unsurprisingly.

So, from nowhere, in 2014, after DECADES of deflation or very low inflation, suddenly we had an inflationary shock.

The same occurred after the 1930s Deflation. *Suddenly*.

The same occurred after the 1960s very low inflation. It was *sudden*.

And we have had falling inflation since the 1970s.

UK inflation from 1947



Zooming in on UK inflation, we see the 1970s inflation 'shock' more clearly.

And the last few decades of falling inflation. It might surprise you to realise that inflation has been sub 5% since 1990. And, indeed, has been sub 5% for the bulk of the time since as long ago as 1983.

36 years!

So, all those super-intelligent (!) fund managers have invested your money on the basis that UK (and global) inflation is going to stay low, and for decades. It's already been low for decades.

History (and just an ounce of common sense) suggests that the era of falling inflation is coming to an end, if it didn't already end. With UK CPI at 0% in 2015, and now above 2%, it is surely at least possible that we saw **THEE** low in inflation in 2015, for an ERA.

That is my contention, given what I am seeing in Emerging Markets, commodities and normal living.

Just this weekend, **TESCO** - UK's largest supermarket group, by far - announced it had raised the prices of over 1000 groceries by a notable average 11%.

And, recently, we saw that U.K. earned incomes are rising at the fastest pace in 11 years, in the three months to May 2019.

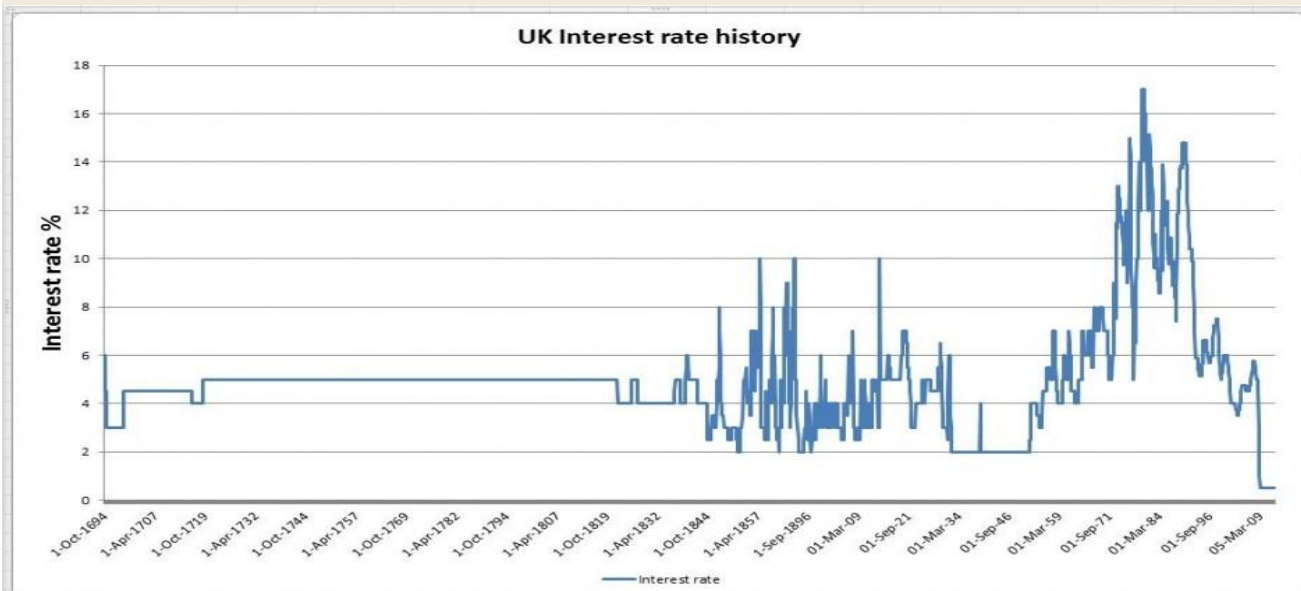
Short to medium term I have little doubt that inflation is on a mildly rising trend. 0% in 2015 to 2% today is hardly soaring. But it is a trend. Up.

In the last Bank of England quarterly report, the Bank strongly indicated Base Rate rises over the next year. This is not at all surprising, except that it is taking so long to do it. I remind you, the US raised from December 2015 (!) to the end of 2018. We have had one paltry rise in 10 years.

It is true that the US will actually cut on the 31st of this month (take it as read). However, they will still be at 2% whereas we are only at 0.75%.

So, what could happen to UK interest rates, longer term?

UK Base Rates since 1694 (when the Bank of England was established)



UK rates were flat, at around 4-5%, for 150 years, to the mid 19th Century.

Then they had a huge range, from 2% to often up to 10% for the next century.

UK Base Rate since 2000

UK interest rates



Source: Bank of England

BBC

The rate rose earlier this year to 0.75%. In my analysis I do not count the politically-driven cut in October 2016, which was almost immediately reversed.

Post war, rates rose in the 60s and soared in the 70s. And fell steadily for 30 years.

Until 2009. When they were slashed to near 0%, and they have, essentially, stayed there for over 10 YEARS!

Looking at over 3 centuries of Base Rate history, what is the likelihood that rates stay this low, still, for many years?

I put it at a low probability. What do you say?

What's more likely?

A 1% Base (1 rise)?

A 2% Base (5 rises)?

A 3% Base (9 rises)?

I would say somewhere between 3 and 6 rises is more likely i.e. 1.5% to 2.25% Base Rate, within a couple to a few years.

Incidentally, that would take mortgage rates from 1-2% to 2-3%, probably. That's a 50% rise in mortgage costs for borrowers over the last decade or in the near future.

Of course, I would also put a significant minor probability (say 30%) on an inflation shock, in the medium term.

Imagine Iran seizing a UK oil tanker, and this escalating, for example...

In fact, nothing of the kind would be required. Just simply that Emerging Markets continue to grow, as they have been doing for years, and commodity prices soar. \$100 oil is absolutely to be expected in the medium term, for example.

In an inflation shock, we could easily see 5-10% inflation and 3-6% Base Rates within a year or two of the shock. **It is vital investors do not forget history.**

Everyone still cannot even imagine house prices falling, sustainably. 'It's not possible' I hear you shout. In markets, there is no such thing as 'not possible'.

I am not saying that house prices are falling and they will fall for years.

I am saying house prices are falling, marginally (5-10% in London and now the South East, and spreading) and, IF Interest Rates rise sustainably, then so too, will house prices. The risk (i.e. probability) is substantial.

DO NOT ASSUME INTEREST RATES WILL STAY AT THESE **EXTREMELY** LOW LEVELS FOR EVER. Is lowest in (centuries of) recorded history not extreme enough for you?

Finally, you may have noticed the Pound (Sterling) starting to rise again recently. For me, this is a continuation of a multi year uptrend. And is indicative of the markets expecting interest rate rises.

Certainly, on a personal note, I dream of a much stronger currency. Lower import costs for the stuff we buy from China, and cars from Europe, lower costs of foreign holidays. All while our industries have lower input costs. Ah, well, we can but dream to live like the Swiss.

So, if interest rates and inflation are to bottom or have bottomed for an era, we should be investing in assets that do well out of rising inflation.

Energy Stocks Vs S&P 500



As you see, in the reflation, post the DotCom / 9/11 recession, the prices of energy companies rose more (much more) than the market, generally.

Post the 2008 bust and the subsequent deflation, energy companies' share prices have fallen and fallen, relative to the wider market.

Energy companies, have actually risen, for the last 3+ years, since oil bottomed in early 2016. But the market, generally, has risen faster.

There will come a point when energy companies will rise, sustainably, MORE THAN the market.

Energy companies, relative to the market, are at near 20 YEAR LOWS! Their relative value is astonishing. They are stupid cheap, even though they are up some 70% on the 2016 lows. 70% and they are still stupid cheap!

Commercial Property

In looking at interest rates, I have noticed there has been a flood of investors redeeming investments in Commercial Property funds. See [this](#), for example, from this month. "A £4.4 billion UK property fund stopped people withdrawing money after investors all rushed for the exit." This is the third such company to do this.

M&G said "Investor redemptions in the Fund have risen markedly because of the high levels of uncertainty in the UK commercial property market since the outcome of the European Union referendum."

They are blaming Brexit even though all you have to do is look around the country and all you see are hundreds and hundreds of cranes and skyscrapers going up everywhere. Clearly, developers aren't blaming Brexit. They're building because of what happens after Brexit.

The point is many property funds have seen enormous redemptions and they've just stopped people getting their money out.

It seems to me that property is so highly priced that pension funds etc were getting out while the going is brilliant and cashing in handsome gains. Before interest rate rises?

And where have the property sellers put the proceeds? It seems they have gone from Property to Bonds, thus driving up Bond prices to 120 year highs...!

Good strategy? Not if they hang around to see interest rates rise, which is why they left Property!

And this leads nicely to the final area for consideration - the **Gold** sector (which includes Silver and Mining Companies).

I wrote, extensively, of this most recently, in the [**April 2019 Booms & Busts Report**](#).

The multi year bull case has been clear for some while. WHEN it was going to resume was the question. Well, in June we got the price of Gold breaching the 2016 high, which was a requirement for the resumption of the multi year bull, which started in December 2015.

At the low, nearly 4 years ago, Gold was c \$1050/oz. It's now over \$1400.

It seems to me, it should get to the All Time High (in 2011 over \$1900) by 2021.

For now, it's soaring (having been \$1160 last August.
Silver has risen from \$14 to over \$16 in weeks.

Gold miners are up 30-50% since the end of May.

There is years of incredible growth to come in this market.
In the last multi year bull (2001 to 2011), gold went up **550%**.
Silver went up **1000%**.
Miners went up **1400%**.

Not in a straight line.

How much Gold etc do you have in your portfolio?

If less than 10% then that's a problem for you.

If less than 5% then your portfolio is, arguably, mismanaged.

You might be interested to check out our new website, just launched.

jonathandaviswm.com

No portfolio manager has managed money in an era of rising inflation.

They have only known falling inflation, throughout their careers. Just like you.

What is your portfolio adviser / manager saying and doing?

What should YOU do to secure and grow your wealth and purchasing power?

Don't put it off till it's self-evidently too late.

If your portfolio, altogether (pensions, ISAs, other investments), amounts to at least £500k, why not arrange a no-obligation discussion with me about your plans and objectives?

We work for clients all over the UK and indeed on 3 continents.

We also have an association with an excellent financial planning firm who can advise interested parties with portfolios materially under £500k. Contact me for details.

Our most important and most often repeated philosophy is:

"We advise you based on what we would do, were we in your shoes, given what we know".

Call me personally to see how we can help.

Please note, carefully, the following important message:

I think most folk do not realise the excellent medium and long term opportunities in our markets.

They will. But will they benefit?

If you have any queries over any of the issues raised call me or email me [here](#).

Follow me [@jonathandavis](#) where I frequently comment and link to useful commentaries on markets and economics.

See Jonathan Davis youtube channel - [JOnathan Davis](#).

Kind Regards

Jonathan Davis BA MBA FCII FPFS
Economist and Wealth Adviser
Chartered Financial Planner

Presenter of The Booms & Busts podcast on [audioboom](#) and [itunes](#).
See [@boomsbustsshow](#)

0345 862 2919

[jonathandaviswm.com](#)

20 Glenwood, Broxbourne EN10 7LP

Please note that investments can fall as well as rise. And they do!

Nothing in this message should be considered as advice.

Jonathan Davis Wealth Management will, under no circumstance, be held liable for any action taken or not taken as a result of commentary herein, unless we have provided bespoke and specific advice, formally.

Registered in England No. 05942730 Registered Office: The White Cottage, 29 London Road, Sawbridgeworth CM21 9EH
Jonathan Davis Wealth Management Ltd is authorised and regulated by the Financial Conduct Authority.