

Booms and Busts Report

In this Booms & Busts Report:

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- Inflation
- Global Growth
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- Energy shares
- Emerging Markets
- Gold
- UK election then British Independence
- UK House Prices, inflation-adjusted, update

In this last Booms & Busts Report of THE DECADE (!) there is a lot to discuss.

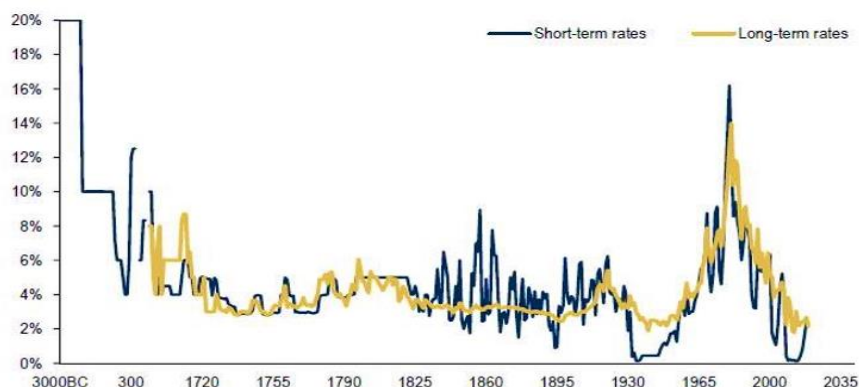
In this decade, we have seen the coming and going of Marty McFly's dystopian future year (2015). Well, it hasn't turned out like Back To The Future imagined it might, had someone had all the major sports results in advance.

What we have had is a decade of low inflation and even deflation. Hence, we have experienced a decade of unprecedented, practically zero, interest rates. Thus, the 2020s will begin with the lowest interest rates in 5,000 years.

FIVE THOUSAND YEARS...!

The 2020s will begin with the lowest interest rates in 5000 years

Chart 3: Interest rates since 3000BC



Source: Bank of England, Global Financial Data, Homer and Sylla 'A History of Interest Rates' (2005)

Sustainable?

I very much doubt it.

Yet, still I come across folk, investing in property (up to their eyeballs in debt) and, to them, it is IMPOSSIBLE that rates will ever rise. Thus property prices will never fall, sustainably. Actually, it's not just possible. It is LIKELY that rates will rise for years and this will impact, negatively, property prices, for years.

The maths are clear.

As rates have fallen, for decades, everyone borrowed more, as the monthly cost has been the same as, previously, for lower borrowings.

Thus, house prices rose.

For a decade, rates have stayed ultra low. So, borrowings have been flat, individually, or even slightly higher, with higher earnings allowing.

But if the Base Rate rises to, say, 1.5%, over the next 12-18 months, then mortgage rates will rise from around 1.5% to over 2%. ...A 33%+ increase. What is impossible is that a bank will lend up to the amount that they lend now. Thus, people will have lower amounts available to buy. ...Thus, sellers will have no choice but to meet the lower offers.

Why might rates rise? Because inflation is increasingly likely to rise, for all the reasons I have shown, repeatedly, over the last couple of years.

- Rising energy costs
- Individual earnings are rising at the fastest rate in over a decade
- Upward pressure to global commodities prices
- Emerging Markets are growing strongly
- Population growth in Most Developing Countries is huge.
- And so on

Above all, there is the fact (not opinion or speculation) that US Government 10 year borrowing rates have not been able to fall below around 1.5% all decade. The market has tried 3 times to break this level and each time rates have bounced. This suggests that we have seen THEE floor in global interest rates.

40 years of US Govt 10 year borrowing rates and a speculative outlook



Clearly, after rates falling for decades, they have not fallen this decade. That is a major change, suggesting reversal of direction.

Once the inflation cat is out of the bag they will not be able to put it back in. Why? Because governments and central banks will try to keep rates as low as possible for as long as possible. Thus, they will stoke inflation. Then they will be FORCED to raise Base Rates and mortgage etc rates will rise, too.

So, Jonathan, you said, above, your next point was Taxes.

Yes Mark, what is the biggest tax of all?

No, not Income Tax. Not VAT. Not IHT. Not Stamp Duties.

The biggest tax of all is Inflation.

Just like we adopt measures to avoid overt taxes, such as IHT and Income Tax (through such arrangements as trusts, Enterprise Investment Schemes, Venture Capital Trusts and pensions), we must ABOVE ALL take action to reduce the negative impact of inflation on our wealth and purchasing power.

Governments have succeeded in pretending to you that inflation is tamed and there is nothing to be worried about there.

Cash or equivalent still pays only 0.5-1%. OFFICIAL RPI is over 2%.

How many readers actually believe that the cost of living is rising just over 2% pa?

Paid a home energy bill recently? Bought a train ticket? Looked at credit card rates? Paid school fees? Bought groceries? Have you bought any (plastic) tins of chocolates for Christmas and noticed that they are MUCH smaller than even just a few years ago... but the same price as previously (Shrinkflation)?

If you believe that the cost of living is rising at just over 2% pa in the UK then I have a bridge to sell you (see [*I've got a bridge to sell you: origin*](#)).

The fact is the calculation of the inflation indices has often been changed - always downward. And, in the 2010s the calculation was altered beyond recognition.

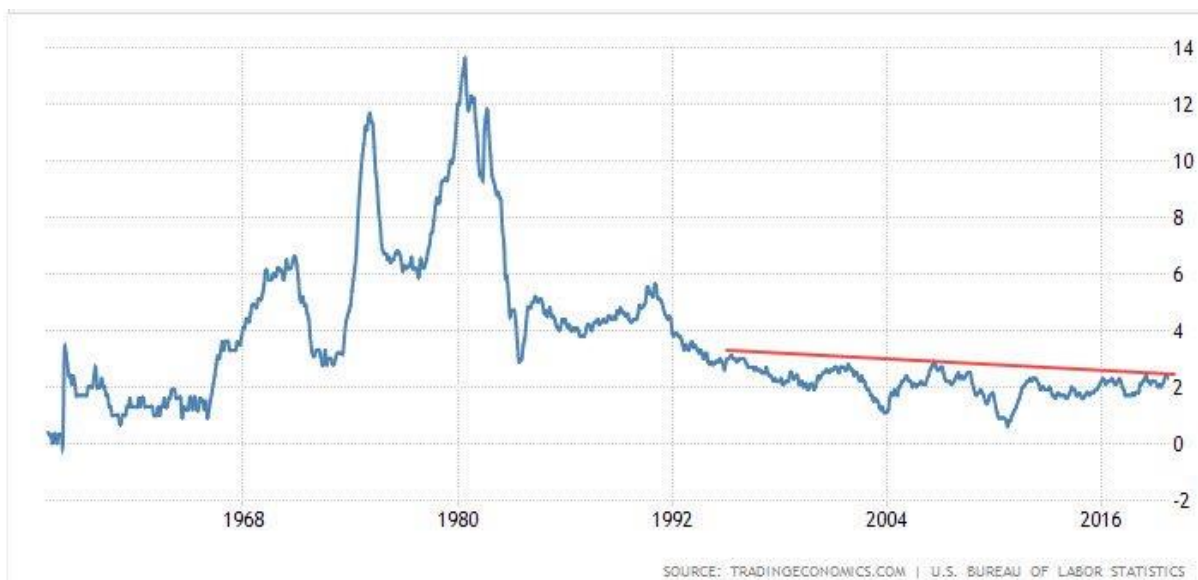
The inflation index is over 2% but the costs of living are rising much faster, in reality.

And, as more and more upward pressures on inflation come, that cat will be coming out of its bag.

2% pa inflation produces an imperceptible effect on your financial position. But it makes an effect.

4% will make a perceptible effect.

The next chart shows **US inflation over some 60 years**. The UK's is not dissimilar.



What I see is consumer inflation below that (red) level, for the last 25 years.

... and just about to pierce up through, for the first time in decades.

To counteract the effects of inflation, we should invest in assets that ought to grow well in inflation. **And we should stay away from assets that fall in inflation, such as Fixed Interest Bonds, Government and Corporate.**

How much of your portfolio is invested in these? If you too can see inflation rising, and sustainable for many years, the question you have to ask yourself is Why hold assets that fall, in inflation?

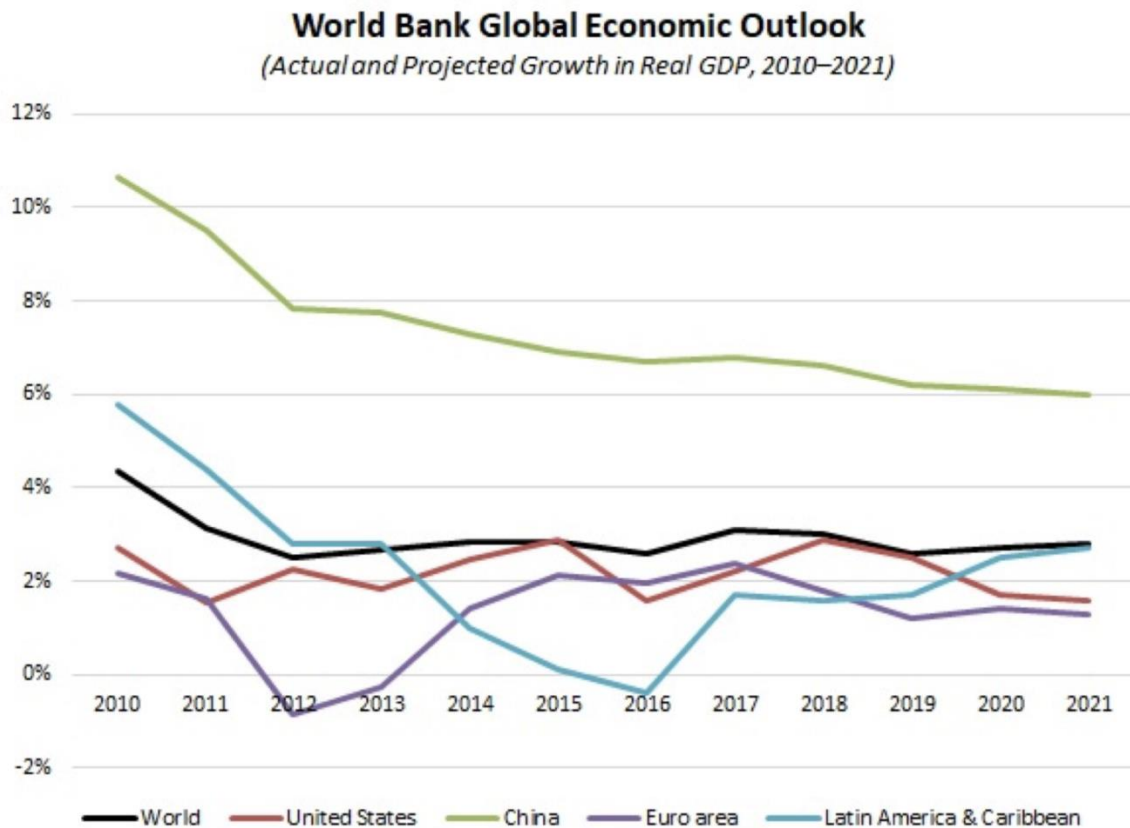
You may recall, months ago, I listed a dozen issues occurring in the World at that time (many still are) that markets bears say one or more of which will bring about a stocks crash and an economic recession.

John Stuart Mill summarised in 1828: **"I have observed that not the man who hopes when others despair, but the man who despairs when others hope, is admired by a large class of persons as a sage."** It's cool and strangely attractive to be gloomy. Some people make fortunes being bearish. Not by investing. But by selling newsletters, books on The World Is Going To End, paid speeches etc.

Well, Global GDP this year will likely be around 3% (it's only a month away to the year end).

And global forecasters expect around 3% next year and similar in 2021.

World Bank Global growth forecasts



Note, they assume a gentle decline (but still growth) for the US and the Euro Area countries and China. So, they're not wearing rose-tinted glasses.

Yet, the same POTENTIALLY damaging issues are still there and new ones will arise. The point is, you can have nightmares because of the narrative, as we call it, or you can just watch what is actually happening in the markets, and the economy.

What I do is watch the markets and, to some degree, analyse the economy.

Actually (and many will recall this), it's far more useful for investing to watch the markets. The narrative is generally spin. If the economy is going to soar then the markets will show it. And vice versa if the economy is going to plummet. Markets are forecasting mechanisms.

And look at **Global Stocks**



Global shares have grown only 40% in 20 years. Indeed, from 2000 to 2016, it was very little.

After prices broke upwards in 2017 and stayed up, Global shares, it seems to me, are now in a multiyear bull market, similar to 1995 to 2000.

Note, Global shares, especially Emerging Markets have gone nowhere for nearly 2 years, net, since an important peak in January 2018. The major bull restarted on Boxing Day 2018 and should last for a few years, growing double digits per annum.

Many investors believe we have had a 10 year bull market. So, contrary to what I see, they say we are at the END of the bull years.

Well, it is clear to me we have had THREE bear markets, since 2009. In 2011, 2015 and 2018.

Thus, the new cyclical bull market only started at the end of last year.

The new SECULAR bull market only started in 2017.

BECAUSE there has been little advance in 2 decades, what I am seeing is we are at the start of a 15-20 year bull market. Most folk have a good exposure to shares. However, they are often invested in sectors that HAVE DONE well. And often not in sectors that have a LOT of catching up to do. Different sectors behave differently if in low growth, low inflation periods or higher growth, higher inflation periods.

As example, I have discussed **Energy stocks**. Here is their performance **RELATIVE to wider markets**. Looks awful doesn't it? Exactly.



The chart DOES NOT SHOW Energy stock prices falling. It shows the RELATIVE move to the market, generally.

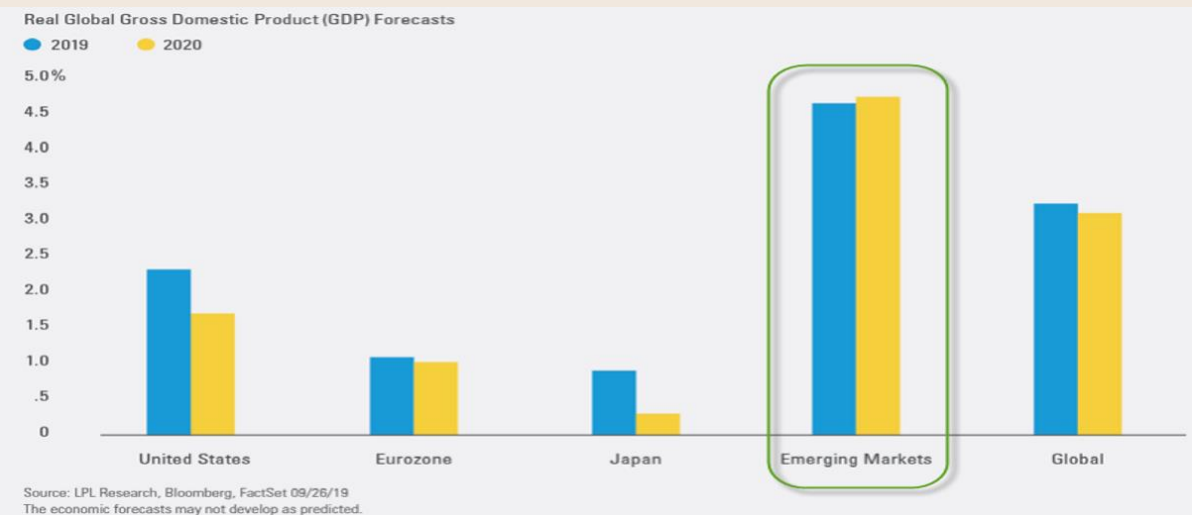
Markets have a tendency to 'mean revert'.

With global deflation, energy has been hated by investors for years. With gently rising inflation, this ought to reverse.

When Energy stocks rise, sustainably, relative to the wider market, the performance is going to be brilliant. Energy stocks are at their cheapest, relative to the market, in 50 years...!

One reason why Energy stocks are likely to perform very well in future years is because of the strength in Emerging Markets economies and share prices.

The chart, below, forecasts this and next year's economic growth, and uses generally accepted analyses.



Of course, what stands out is the superior growth in Emerging Markets, and expected to tick up next year.

Just like Global shares, EM share prices have done nothing for nearly 2 years.

Look at the **long term chart of EMs**.



When they started to join the global economy, at the end of the century, the rate of growth in prices was impressive.

EMs prices have done practically nothing for nearly a decade.

We have seen 2 distinct bullish periods of EM stocks, in recent times:

1999-2011;

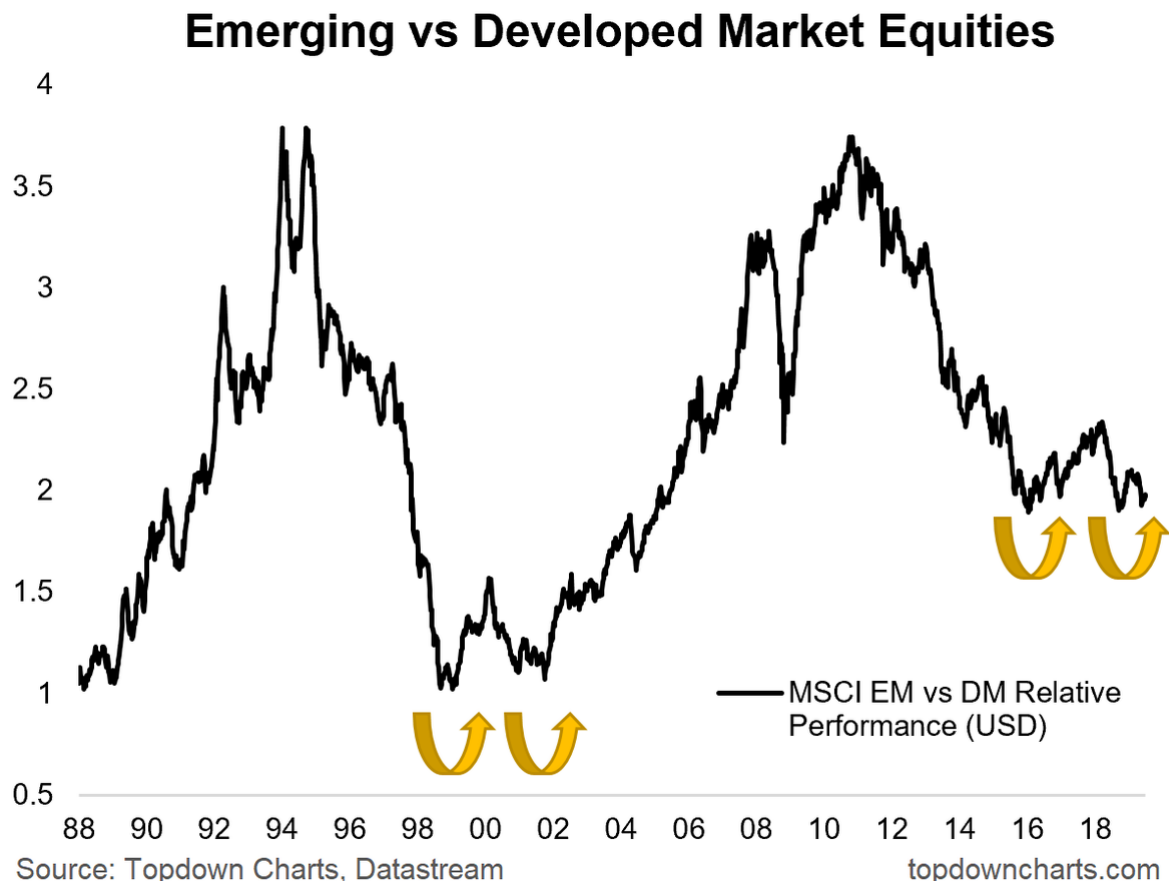
and 2016 to ... It seems to me it will be a multiyear bull market. Perhaps to the late 2020s.

If EMs are going well, we can take it global inflation is rising.

EM stock prices are a smidgen away from the All Time High, of January 2018. They are likely to breach that peak, shortly, and then rise for years, as I see it. And rise faster than Developed Markets prices - that portfolios normally hold, primarily.

In discussing Energy shares, above, I referred to relative moves against the wider market.

Here is an **EM index** (not the fund we use) **against Developed Markets** prices, over 30+ years.



Just like Energy stocks, when EMs get going again, and they have likely started, the returns will be excellent, both nominally and relatively.

You would do well to get your pins lined up. Or are you going to stick with, mainly, UK stocks? UK Mid Caps have done very well. Will they continue to do as well? The EM fund, in which we invest, doubled between 2016 and early 2018, as you see above (the first EM chart). It's just the start.

It seems to me that Gold (Precious Metals sector, generally) is in a multiyear bull market, started in 2016.

If we were not investing in Gold assets we will probably instead invest in Global Shares. So, here is a chart of **how Gold Mining Shares have moved, relative to Global Shares**.



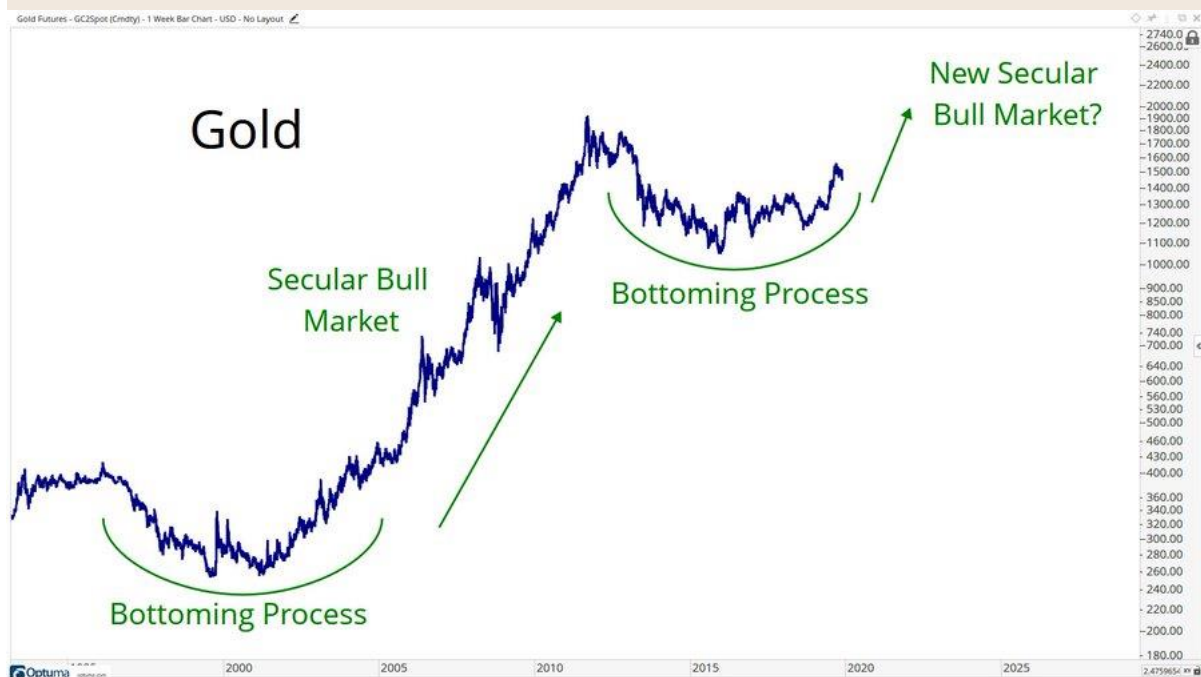
Gold Miners soared, relative to Global Shares, in the last decade.

From 2011 to 2015, they absolutely crashed and burned.

Relative to Global Shares, it seems to me that Gold Mining Shares, are now again in a multiyear bull market, and nominally.

And the bull has just started. Look at the next chart of Gold. It seems to me, we have just experienced the same Bottoming Process as we saw in the 1990s and early 2000s. A new secular bull market is likely.

Gold secular bull just starting?



In a couple of weeks, according to the polls (which are all saying the same thing), Boris Johnson's Conservative Party will win the UK General Election. We are likely to move, at least, slightly away from the EU in 2020. (Whether or not it will actually be Leave is moot at this point.)

The question for investors is what will a newly-elected government and British Independence maybe) do to markets?

Nothing.
Nil.
Nada.
Zilch.

I hope I have made myself clear.

I wrote, last time, that they said the Pound Sterling fell because the British people voted to Leave the EU. And we are closer than ever to Leaving, yet the Pound Sterling is rising strongly.

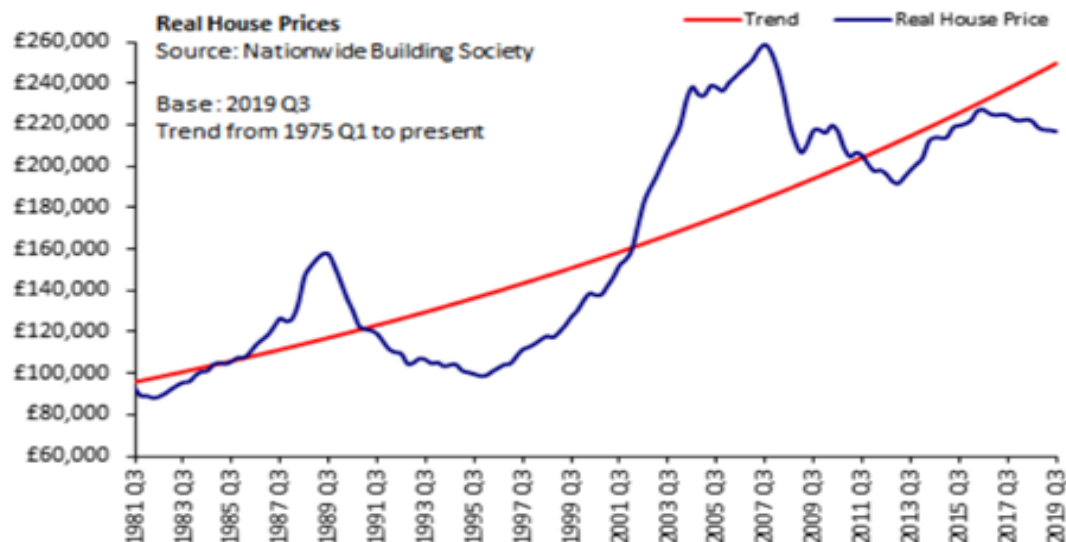
Thus, as I have said, for years, British Independence will do NOTHING to the £.

What matters to our currency are general economics, interest rates et al. It seems to me that (as I have said repeatedly), as inflation gently rises, interest rates will rise. THAT is what is driving £ strength. The markets also expect higher interest rates in the UK, as I do.

The Nationwide Building Society has updated its Real (Inflation-Adjusted) price chart.

UK Real House Prices

UK house prices adjusted for inflation



UK Real house prices reached an All Time High in 2007.

After years of falls, to 2013, they then rose. The new lower peak was 2016, since when Real house prices have fallen again.

Not exactly the picture everyone wants to believe...

I have said for a long time that, as we have likely seen the bottom in mortgage rates, we have, therefore, likely seen the top in house prices, nominally and inflation-adjusted, for perhaps a generation.

Yes, I know immigration, Green Belt restrictions, island et al.

But, you know, NONE of these are the reasons for huge house price growth over the last 50 years.

It's really not complex but the politicians and the banks don't want people to realise that house prices are largely determined by

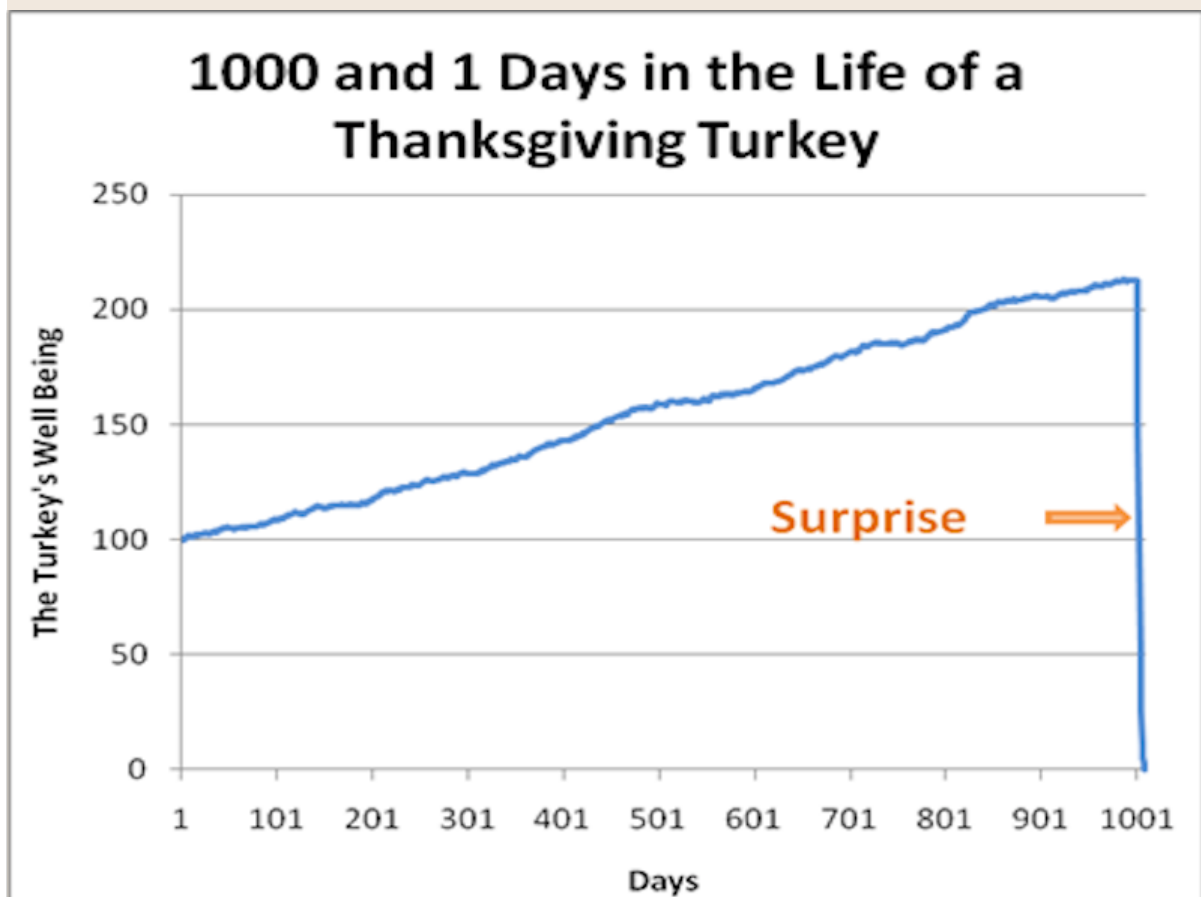
1. Ease of lending, and
2. Cost of borrowing (mortgage rates).

Easy lending will likely continue. However, as I have shown, it is unreasonable to imagine mortgage costs will stay down here for much longer. And when they rise, they will rise for probably 10+ years.

After 2+ years of price falls in Prime Central London, we can expect a bounce any time. I do not see it as sustainable, if interest rates rise.

And finally...

As it is Thanksgiving Week and Christmas, shortly, let us consider the **Life of a Turkey**



To American readers, I wish you a super Thanksgiving. No talking politics, now!

And to everyone, have a Very Merry Christmas and a Happy New Year.

The bulk of portfolio managers has NEVER 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.

Why not arrange a no-obligation discussion with me about your plans and objectives for your portfolio?

If you are at the saving stage and building your portfolio, I also advise high earners.

If you pay a lot of tax, you probably needn't.

If you think your estate beneficiaries might pay a lot of IHT, they probably needn't.

Do you insure your income, should you suffer a long-term illness and you cannot earn?

Do you really have enough life assurance, in case the worst happens?

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

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 also do not realise, in big picture, the excellent opportunities in our markets.

They will. But will they have benefited?

If you have any queries over any of the issues raised do not hesitate to call me or email me [here](#).

Follow me @j0nathandavis where I frequently comment and link to commentaries on markets and economics.

See [Jonathan Davis youtube](#) channel.

Kind Regards

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

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