BPM BERLIN PORTFOLIO MANAGEMENT

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Brexit is just the start

A much bigger problem is the extremely high level of global indebtedness

A guest contribution from Uwe Günther

The foreseeable end of the debt-cycle that has been going on for some fifteen years now is much worse than Brexit. Investors who fail to act now will end up casualties. Ten actions provide some protection.

Britain's vote to leave the EU triggered a Black Friday on the financial markets. However, the enormous rise in levels of international indebtedness constitutes a much greater risk for securities portfolios. It's still a bit too soon to panic or to predict the end of the world, but given the expanding bubbles of debt, investors would be well advised to strategically restructure their holdings sooner rather than later.

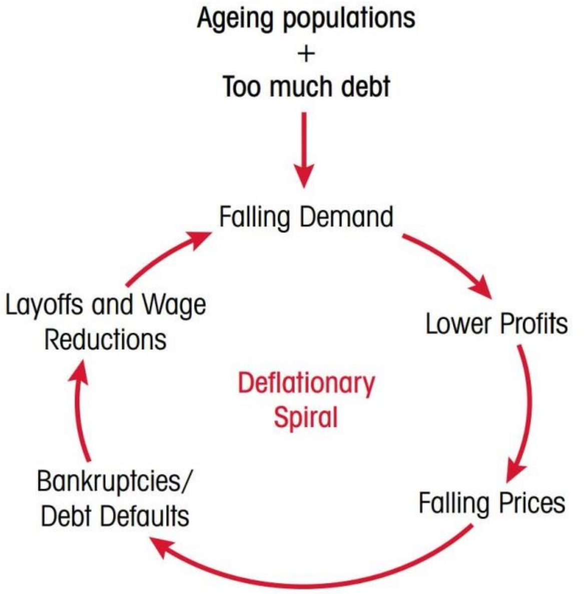
The equivalent value of bonds alone (securitised debt!) in circulation throughout the world is more than 100 trillion US dollars, a lot of which is not backed by real assets. This massive mountain of debt will become a problem once it is no longer possible to fully service it by means of economic growth and/or issuing new debt - and once this will become part of public perception! Once this happens, holdings will have to be liquidated, real estate sold, loan capital repaid and financial positions revalued.

However, we can hardly claim to be in a period of sustainable economic growth at present. Corporate profits have been falling across a wide front in the world's biggest economy - the United States - since the middle of 2014. Transport indices - a reliable indicator of economic activity - have also been trending downwards for several quarters. Even mergers and share buybacks - often the financial markets' final drivers - have been declining recently. Europe is preoccupied with the consequences of Brexit, while serious doubt remains about China's economic growth.

Consumption and investment levels too low

When households, firms and countries become less and less willing or able to consume or to invest, this causes a lack of economic growth, inevitably resulting in problems to service debt, as we have known for centuries. Central banks have been reinforcing this development with their loose monetary policies. Thanks to ECB & Co unabashed purchase of securities, more than 9 trillion Euros' worth of bonds are now producing negative returns. In a few years' time creditors will receive back less money than they are currently lending to countries and corporations. That's a sort of expropriation and counteracts the protection of private property in our economic system.

It's hardly any wonder that savings ratios are rising in lots of countries. Given that, to all intents and purposes, yields have disappeared, people have to put more and more money aside for their retirement rather than spending it on consumer goods or investing it. Far from creating inflation and economic growth, central banks are actually causing prices to fall and making consumers reluctant to buy! That's not what the ECB had in mind.



Debt bubbles have to be burst and will be bursting. The only thing that is unclear is when exactly that is going to happen and what the trigger will be. Investors are taking the following actions to secure their savings from the threat of debt collapse.

1. Reduce the ratio of savings you hold in the form of shares. Stay clear especially from investing in companies whose debt levels have risen substantially.
2. Part company with high-risk bonds that promise "great" returns.
3. Build up your liquidity in a range of currencies other than the Euro. The most suitable are the US dollar, the Swiss franc and gold.
4. Enquire about possible hedging strategies for extreme events, even though they might appear highly improbable at present.
5. Go for market-neutral or uncorrelated solutions whose growth is substantially independent of share and bond market trends.
6. Reduce your borrowings or repay them in full - especially Lombard loans which involve pledging securities for the funds borrowed.
7. Check and optimise your bank and management charges, especially the hidden ones.

8. Take action now and don't let yourself get "turned around" by people who are trained to sell financial products. Always ask yourself "cui bono?". Who is this benefiting - you or your bank?
9. Know your own mind: limit your losses and let your profits run - not the other way round.
10. Keep your nerve and trust in the long-term effectiveness of economic interrelationships. Processes can drag on during periods of fluctuation - triggers often happen overnight. But you're already prepared.

These measures will improve the stability of your savings and put you in a position where you can act while others have to capitulate.

Best regards,

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