Genie In A Bottle

"The four most dangerous words in investing are 'This time is different'"
- Sir John Templeton

"The six months under review have seen Central Bankers continuing what is surely the greatest experiment in monetary policy in the history of the world. *We are therefore in uncharted waters and it is impossible to predict the unintended consequences of very low interest rates, with some 30% of global government debt at negative yields, combined with quantitative easing on a massive scale."*
- Lord Rothschild's semi-annual letter to investors

"It is not impermanence that makes us suffer. What makes us suffer is wanting things to be permanent when they are not. Wilting flowers do not cause suffering; it is the unrealistic desire that flowers not wilt that causes suffering."
- Thich Nhat Hanh

That last quote I borrowed from one of John Hussman's June newsletters. I think it is brilliant and so appropriate for the issues we face today. Every time I write this newsletter I try to think about what is happening that I really feel people would benefit from understanding. This has been my hardest newsletter in the seven years I have been writing for two reasons: first, so many false narratives are breaking down regarding Central Banks' ability to control outcomes, but it is not obvious on the surface because stock and real estate prices continue to hold up. If there is anything we want our readers to know it is that we believe that the risk is higher than ever in financial markets. That is why Jeff Gundlach of Doubleline recently said on *CNBC*:

"Investors have entered a world of uber complacency. Sell everything. Nothing here looks good. You can't save your economy by destroying your financial system."

The second reason this is hard to write is because what is happening is that the status quo is failing. And that's ok, the status quo is supposed to fail occasionally, reference the quote above about the wilting flower. We celebrate the status quo failing every 4th of July. The failure and death of old ideas is part of progress and growth. But for some the status quo failing looks like being a property owner in London and watching values fall after the Brexit vote. Also, when the status quo fails, the process of change can be uncomfortable and does not always go in the right direction at first. It can lead, for instance, to opportunistic politicians leveraging fear and anger to reach for power.

However, the status quo is not working for people right now, at least not most people. Homeownership rates are back down to where they were in 1965. During the "recovery" since 2009 average household incomes have declined and are now back to where they were in 1996 adjusted for inflation. This year has seen more bankruptcies than any year since 2009. GDP is flat-lining, earnings are declining, and profits are receding. The combined approach of Keyensian and Monetarist theories are failing before our eyes. One thing is clear, those in the status quo, represented in this case primarily by Central Bankers and the politicians that support their policies, have tried to keep the Genie of real market forces in a bottle through artificial means. It may be that they have merely made that Genie more disturbed and bent on retribution.

(For a more detailed view on what is going on in the economy you can view a report put out by Harvard Business school at https://www.scribd.com/document/324137454/Harvard-Study-on-US-Economy-Under-Obama#from_embed.)

The largest and most systematically important European banks are crashing - and were before the vote of Britain to exit the Eurozone. Why is that? Japan just proposed another 27 trillion yen stimulus program and after 25 years of trying to rescue their economy they are failing again. **We keep piling debt on top of debt in a vain attempt to revive the patient by giving her more of what is killing her.** This is why Ray Dalio of Bridgewater recently said:

> *"We have reached the limits of Central Banks' ability to stimulate the economy and raise global asset prices. Only so much you can squeeze out of a debt cycle and we are there."*

And Gary Shilling in his August 2016 newsletter said:

> *"We continue to believe that monetary policies are impotent. Zero interest rates did little to spur lending and borrowing, and negative rates appear to be creating more confusion than help. Quantitative easing also has not stimulated purchases of goods and services and, therefore, economic growth."*

One third of all government bonds in the world, or over $16 trillion worth, are now trading at negative interest rates. The stock market is at a new high and home prices in many major U.S. cities have surpassed the bubble peaks of 2005. What does it mean? Does it mean it is a good time to invest or a bad time to invest in risk assets? Our answer should be obvious, but perhaps this time is different.

To be clear, we do think we are seeing the greatest spread between asset prices and economic reality ever. But we also think that for the well-prepared incredible opportunities await.

Matt and Tom

Visit Our Website

Executive Summary

Cycles and Deflation

If you get nothing else from this newsletter we would encourage you to watch this YouTube video posted by Raoul Pal of Real Vision in June of this year. Pal was a Global Macro Manager at Goldman Sachs before going on his own and pioneering Real Vision, a subscription based internet television network. In the video he captures the importance of understanding long and short-term cycles to growing and protecting wealth:

Boom, Bust, Rinse & Repeat: Predicting The Global Economy by Raoul Pal
https://www.youtube.com/watch?v=SDoIbFuKgfU

Quick Market Update - The S&P as of today is exactly where it was in May of 2015. Compare 2016 to 2007 and you will see similarities. In October of 2007 the market hit a new high and people cheered - right before the market fell 60%. We continue to think that U.S. markets are not done topping just yet but the risk/reward does not appear attractive.

Housing Bubble 2.0 - We know in hindsight that 2005 was an unsustainable bubble. Incomes for most Americans are lower now than in 2005 and housing prices in many cities are higher. Anything wrong with that picture?

Taxes, Tools and Transition - If you agree that this whole experiment is likely to end in tears, the question is what do you do? The greatest mistake investors made in 2000 was to not sell over-valued tech stocks because they were afraid of paying taxes. How do you create a thoughtful strategy for reducing risk? Warren Buffett's largest position, according to Barrons, is $73 billion in cash.

Why the Status Quo is Failing - Insight from Ben Hunt of Salient explaining Brexit and some thoughts on the upcoming presidential election.

Create Your Own Economy Corner - The power of vision.

"The empires of the future are empires of the mind." - Winston Churchill

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Genie In A Bottle

Cycles and Deflation
If you took the time to watch the video you will appreciate the following chart of the ISM (Institutional Supply Management). It has taken the dip that Raoul Pal expected. This indicator, he believes, is the best predictor of the business cycle. The ISM has been softening since 2011 and is now in contraction territory.

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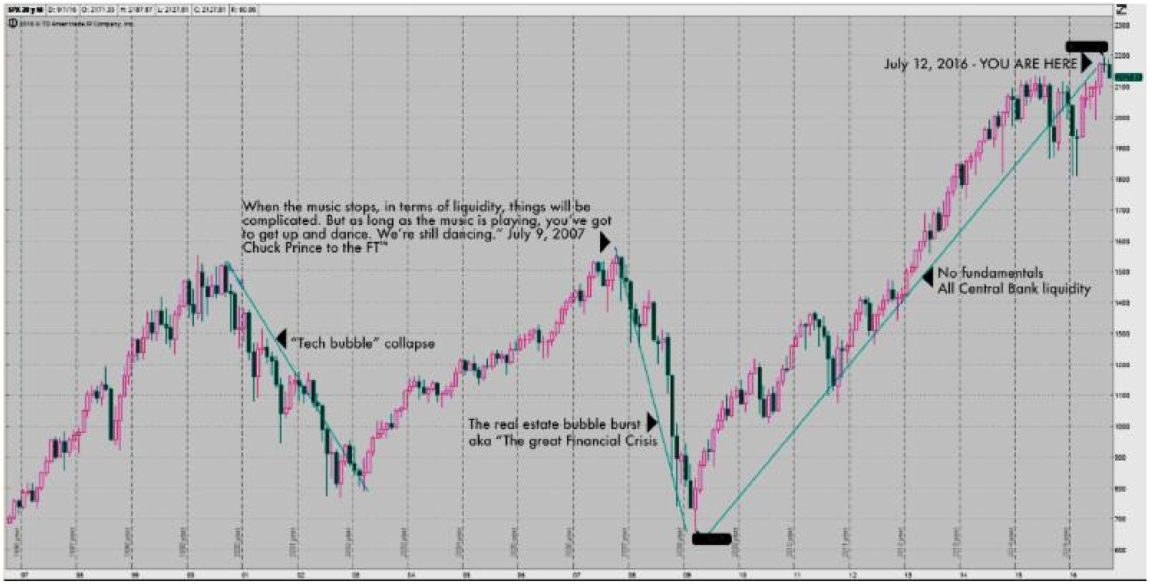
Quick Market Update
In August of 2007 Countrywide Credit was failing due to losses on sub-prime loans and had to be bailed out by Bank of America. The market sold off in response to Countrywide's problems, but quickly recovered to new highs in October of 2007. That ended up being the last new high before the market tumbled 60% in the greatest financial crisis since the Great Depression.

This year the market sold off in February on concerns that the Fed was raising interest rates but more recently sold off after Britain voted to leave the Eurozone. In July the market surpassed the high made in May of last year. This new milestone has triggered numerous headlines celebrating good times ahead.

As we mentioned in our introduction, our technical analysis allows for a continuation of the topping process and the possibility of new highs. However, contrary to many articles we read about the "most hated market rally ever" the statistics indicate that hedge funds and mutual fund managers are more fully invested than ever which is what one would expect to see at the top. In addition, significant divergences are occurring between commercial investors and speculators which is what is also normally seen at market tops. We point all of this out just because it is so obvious that risk is high just as it was in 2000 and 2007. We like visuals so below is one chart of the S&P 500 going back to 1997. Take a look and ask if now is the time to buy:



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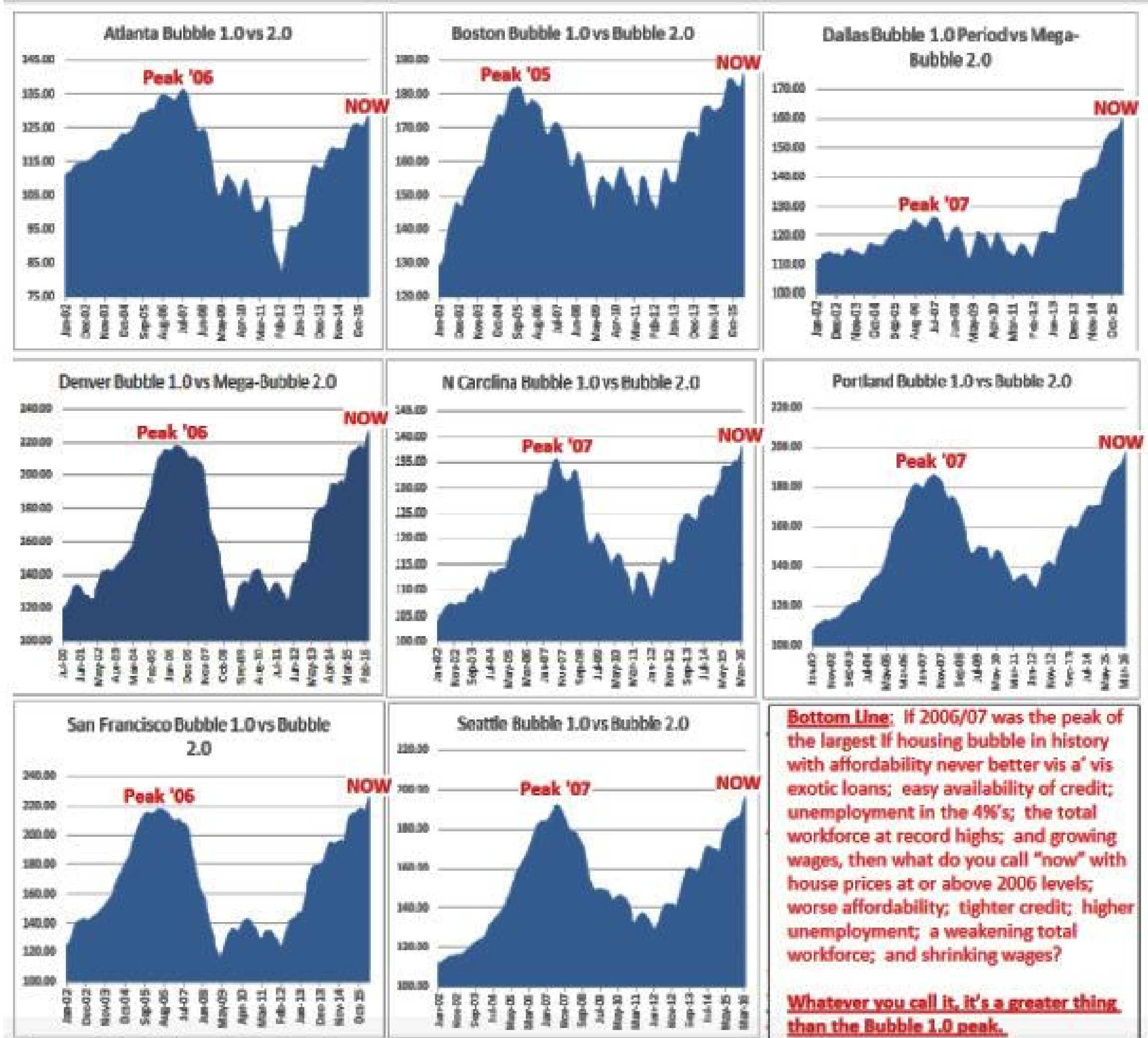
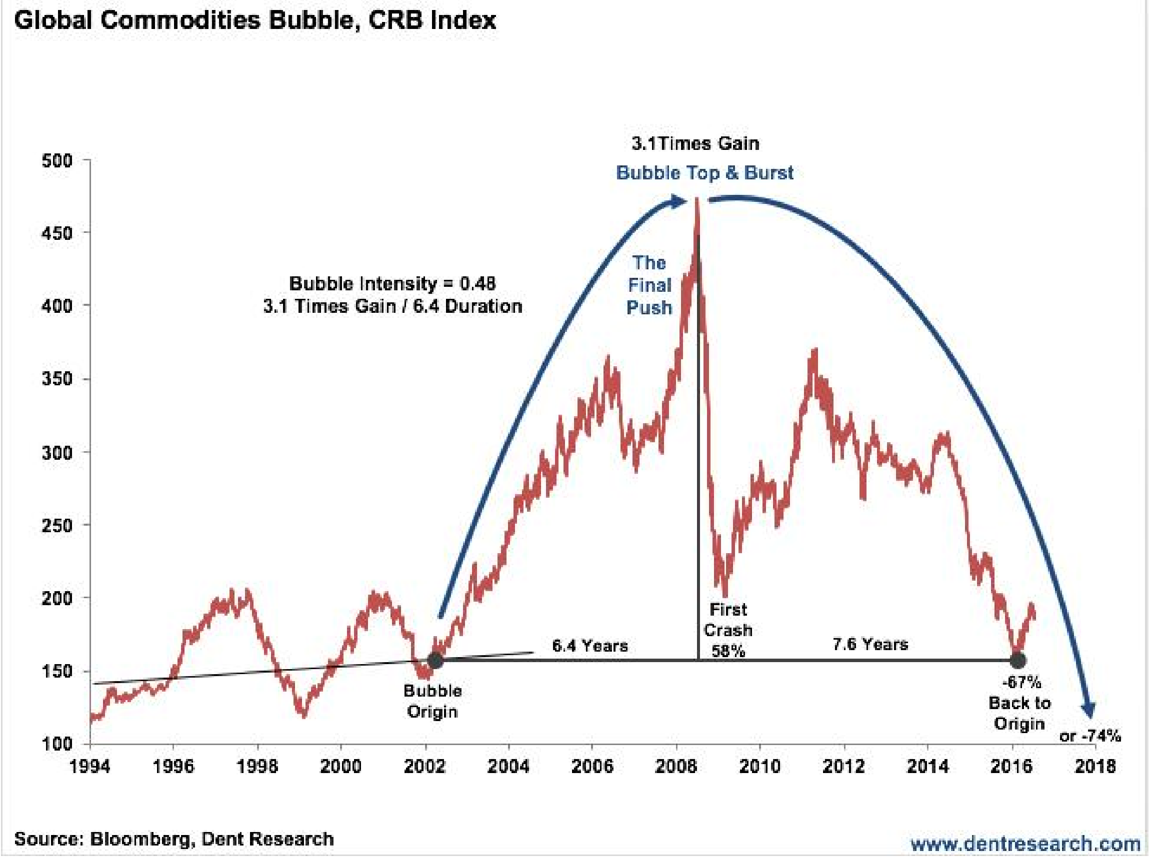
Housing Bubble 2.0
Very few people thought we were in a housing bubble in 2006, but most people recognized it after the fact. That is how bubbles work. Below we share a chart showing that despite income levels declining, housing prices in many major metropolitan areas have exceeded 2006 prices.



Source: Case-Shiller via ZeroHeadge

History shows that bubbles go back to where they began. Commodities have born that out already even though in 2011 most market pundits were arguing that inflation would drive commodities and farmland to the moon. Here is a look at the CRB, an index measuring the movement of a broad basket of commodities:



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Taxes, Tools and Transition

Our last newsletter discussed alternatives to investing in publicly traded stocks. That does not mean that we suggest getting out of stocks altogether. Rather, we simply recognize that the "smart money" has been reducing exposure to stocks for some time and that other investments may present better risk/reward at the time. In fact, we might argue that now is a great time to transition away from an equity heavy portfolio for the following reasons: tax rates on capital gains are historically low, equity valuations are historically high, and both of these factors are likely to change dramatically. However, even managers like Jeff Gundlach who we quoted earlier will say things like "sell everything" really mean to get more defensive and begin to raise cash or move away from risk.

Here is what we are suggesting clients consider:

1. Reduce leverage - this is the most disturbing thing we see in reviewing accounts held at other firms, lots of leverage in the form of margin and credit lines. In deflationary periods leverage works against you.
2. Have a higher cash balance than you may have historically - perhaps 30% of your portfolio - as Warren Buffet says - this is an option on buying all assets at a discount. In deflation, cash grows in value as assets decline. Buffet's largest portfolio position right now is $73 billion in cash according to *Barrons*.
3. Invest the core of your portfolio in absolute return and tactical strategies that can either profit from or at least protect against declining markets. Mostly these are traditional stock and bond portfolios with hedges.
4. Maintain some exposure to sector specific income opportunities such as health care real estate, data centers, apartments, mortgage REITS and master limited partnerships.
5. Utilize guaranteed income products offered through insurance companies where appropriate - fixed and indexed annuities.
6. Use actively managed fixed income managers that can react to rising interest rates.
7. Diversify your resources among the best banks, investment firms and insurance companies. And by best we do not necessarily mean biggest - especially when it comes to banks.

There may be opportunities to short various over-priced investments, but we leave that to people who have a proven process for doing that successfully. We are most focused on reducing risk, protecting our clients from loss to prepare for opportunities as they develop.

Given our historically high level of debt, we think it is reasonable to expect higher tax rates going forward. Also, given the record low interest rates and record high stock and real estate markets, it is fairly easy to imagine that most asset classes decline in value at the same time. Now is a great time to put together a strategy for intelligently reducing risk and future tax liability.

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Why The Status Quo is Failing

Brexit, the vote of Great Britain to leave the Eurozone, may be the most significant economic and political event since the fall of the Berlin Wall. This is not to say that it is good or bad, it is just significant. Why do we say that? It is not because of all the follow-on effects of trade agreements being renegotiated. We say this because it represents the largest blow to the status quo in Western democracies in recent history.

The rich, powerful, well-connected London property owning, moneyed class, all expected the "remain-in" camp to win. Polls had them winning until the day of the election. It came as an utter surprise, a shock.

Both sides used hyperbole to try to move people to their side. The "remain-in" camp said that Britain would experience financial Armageddon if they left the Eurozone. The "leave" camp said that immigrants would over-take the nation and grab what few jobs remained if they stayed. But both sides also had more reasoned, rational arguments to make.

The "remain-in" camp made the case for maintaining interconnectedness and the benefits to commerce and funding for research. The "leave" camp made a rational argument for sovereign integrity suggesting that ceding power to Brussels violated their constitutional rights.

In the end, what matters is that the status quo, those who wanted things to remain as they are, lost. Here is what Ben Hunt of Salient Partners had to say in his July newsletter:

> *"Why are the status quo protecting narratives faltering so badly? I think it is because status quo political and economic institutions - particularly Central Banks - have failed to protect incomes and have pushed income and wealth inequality past a political breaking point. They made a big bet: we're going to bail out/paper over the banks to prevent massive losses in the financial sector, we're going to inflate the stock market so that the household sector feels wealthier, and we're going to make vast amounts of money available for the corporate and government sectors to borrow really cheaply. And as the MckInsey Chart here shows, by 2014 they had largely succeeded on all counts, certainly getting the corporate and government sectors to borrow trillions in new debt. ($57 trillion in new debt)*
>
> *"The result, or so the thinking went, of all of this pump-priing or bridge-building or whatever metaphor you please would be for all four basic sectors of the global economy - households, corporations, governments and financial institutions - to consume more and invest more and fail never, which in turn create a virtuous, self-sustaining cycle of risk taking, real growth and real wealth creation.*
>
> *"It was a reasonable bet to make. But the bet failed. Why? There's a book or two to write on this, but I'll sum it up this way - you can no more force corporations to invest for growth if they don't believe it's safe than you can force people to watch John Oliver if they don't think he is funny."*

We at Global Vision Advisors have been arguing, that this has not been a reasonable bet to make. In fact, things are ending up very predictably, because this is how they have ended up every single time in history where economies have created huge debt bubbles. You can't get people to save less and borrow more if they are uncertain about the future - it's a behavior issue and while you can influence behavior you cannot control it. Baby boomers nearing retirement are not going to run out and buy a bigger home because interest rates are lower. They need to save more. Their future is uncertain. This is why you cannot solve a problem of too much debt with more debt.

Furthermore, as we have suggested in these pages and as Hunt is alluding to in his commentary, corporations have been taking on debt, impairing their balance sheets, buying stock, making them appear more profitable. However, they are not investing in new ways to generate revenue and add value. They are merely engaging in financial engineering.

As Hunt argues, the status quo is failing and in the U.S. that has been evident in the campaigns of Bernie Sanders and Donald Trump. Again, this is one more reason that it has been difficult to write this newsletter. We do not want to offend anyone with our observations about the status quo, but we do think it is important to understand. Frankly, no amount of qualifications change the fact that when many people look at Hillary Clinton in her $12,000 Armani suit, they see Goldman Sachs, Wall St., - status quo. When they look at "The Donald" as crazy as it sounds, many see change agent. And more likely for many it has nothing to do with Hillary Clinton or Donald Trump, rather it is just about change.

People outside the top 1% are not happy. But very few people have been willing to discuss the role of the Federal Reserve in creating these conditions. We think that is changing. And given that the only thing holding asset prices up is the belief in the Federal Reserve and other Central Banks' power to maintain stability, we believe that the change we are facing may be very hard on financial markets.

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Create Your Own Economy - Vision

"You either live in vision or you live in circumstance." - Dr. Kevin Elko

Global Vision Advisors is dedicated to one thing: helping our clients clarify and achieve what they most want out of life. Everything we do is dedicated to that objective. This means different things to different people. Everyone has a unique vision for what they want to get out of life. What excites us is helping people, through an effective, repeatable process, find for themselves what is truly important and help them craft a plan for creating the outcome they desire.

Most of what we do when it comes to creating an action plan comes down to matters in the financial planning world: saving, investing, insuring against unforeseen events, planning for the effective distribution of accumulated wealth, reducing taxes, etc. But most often other things come up, like changing careers, learning new things or creating great lifetime experiences.

These incredible visions are the magic of life. This is what we are dedicated to, to support and nurture for our clients. It is not about sales targets to satisfy upper management. We are the upper management and our target is to get our clients to where they want to go.

In the days ahead we believe it will be even more critical to have a clear vision for your future, a plan to get there and a practice to stay on target. This is our passion and our mission and we remain grateful every day for the role we get to play and the difference we strive to make.

Thanks for reading and for giving us the opportunity to do our life's work.

Matt and Tom

Giving Back

Global Vision Advisors believes that being involved in our community and giving back to causes we are aligned with is an important aspect of our business. We wanted to let you know how we're giving back and update you on where our efforts have been focused during the last quarter to show you some of the impacts the charities we support have made.

Tom led a successful spinathon raising and contributing over $5,000 towards the YMCA's Kid Campaign that is on pace to raise $25,000 this year and helped the SSYMCA's development team in raising over $65,000 from this year's major fundraisers.

The South Shore Hospital Golf Outing this year raised roughly $250,000 for the ICU and the annual Lawn Party/Croquet tournament raised $27,000 for South Shore Hospital's Pediatric Unit. Global Vision Advisors sponsors both events and Matt is the new co-chair of the golf outing pairing his support for the hospital with his love for golf.

Global Vision Advisors is sponsoring the upcoming Renegade Run which raises money for Type One Diabetes research. GVA is a founding sponsor and you can learn more about the event and the cause here http://typeonerenegaderun.com.

If you'd like to learn more about the causes we support, please contact us or visit their websites.

GVA In The News

Matt and Tom have been quoted in *The Wall Street Journal, CNBC, BusinessWeek, USNews and World Report,* among others. Below are some articles we feel you might be interested in reading.

CNBC.com http://www.cnbc.com/id/40719837

Health and Wealth
http://globalvisionadvisors.com/files/2014/11/HW-article-Better-investor.pdf

CBS MoneyWatch.com
http://moneywatch.bnet.com/investing/article/boost-your-returns-by-conquering-risk/341569/

Health and Wealth
http://globalvisionadvisors.com/files/2014/07/Tom-HW-article-May-2014.pdf

CNBC.com
http://www.cnbc.com/id/32643244

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Global Vision Advisors | 101 Longwater Circle, Suite 103 | 781-740-8883 |
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