

Quote of the week - “Unfortunately, only when the poor enter the halls of the rich, the rich notice that the poor exist ... Until we had this massive movement into Europe, there was no recognition in the developed world of how serious this crisis was.” - Antonio Guterres (age 66 & a one-time Prime Minister of Portugal) has been UN High Commissioner for Refugees (UNHCR) since 2005.

A bad way to find out you no longer have a job - Yesterday, October 8th, a number of employees of a major oil company in Calgary arrived at their place of work only to find that their access cards-, & their company cell phones-, didn't work any more - *a company spokesman explained later that 'some staff did lose partial access to the system before the company had a chance to formally notify them they had been laid off' and "We're truly sorry this happened and ... caused additional stress for people on an already stressful day."*

A blow struck for Chinese traditional medicine - Tu Youyou is one of the three co-winners of the 2015 Nobel Prize in Medicine (*she got half, while the other two shared the other half since theirs was a joint effort*) for discovering anti-malaria-, & anti-roundworm parasite-, drugs respectively. She is an 84 year-old pharmaceutical researcher long associated with the Academy of Chinese Traditional Medicine who during the Mao Tse Tung era developed an anti-malaria drug, artemisinin, from the sweet wormwood plant after having learnt from her study of ancient traditional medicine books that an extract from the plant had been used as far back as 400 AD to treat fevers.

Canada passes a milestone - On September 29th StatsCan announced there are now more seniors in Canada (aged 65 or over) than juniors (14 or under). But this is not universally so across the country; for it does *not yet* hold true for the three Prairie Provinces & the three Territories (*in part since they have a higher proportion of indigenous people who start earlier producing, & have more, offspring*) - *this is quite a change in just three years; for in 2012 seniors, now at 16.1% of the population, accounted for only 14.9% (vs. 16.1% for the juniors).*

Does the Fed have its head in the sand or ...? - Earlier this year Wall Street raised *partially self-serving* concerns that, with dealer corporate bond inventories down 76% since the financial crisis, banks are no longer in a position to act as *effective* market makers that will buy corporate bonds when investors want to sell. But, in a blog posted on the New York Fed's website, three Fed researchers dismiss the idea & claim there is “ample liquidity in corporate bonds markets” because investors are filling the void created by Wall Street's retreat from trading - *If this report had emanated from the (Central) Bank of Russia it might have been deemed 'dezinformatsyia'/ misinformation; for common sense suggests that a 76% decrease in trading inventories at a time of a 37% increase in the volume of bonds outstanding could at some point become problematic in terms of the market's liquidity. And in a best case scenario the report's authors display a deplorable, & for Fed officials unworthy, understanding of how financial markets work; for the very investors whom they expect to provide liquidity, are the very ones who tend to panic & need liquidity at a time of a real, or perceived, market crisis.*

Downtown Edmonton going to hell in a hand basket? - This morning at about half past two, as I was working on Gleanings, there were three bursts of what sounded like gun fire, seemingly right under my eighth floor window. But when I looked out, I couldn't see anything unusual. This morning, however, I found out that it had indeed been gunfire, only a block up the street, that had sent three men to hospital. In the last year or so, there have been at least three murders in a four block square area around my apartment, two of them on the street in broad daylight. And, generally speaking, in the past year or so there has been an uptick in both domestic-, & street-, violence (for which the Chief of Police blames the slowdown in the oil patch).

Fed shot itself in the foot? - Once upon a time it looked at 26 indicators to determine their potential usefulness/reliability as harbingers of recessions. One, an inverted yield curve (when short term interest rates are higher than long term ones) stood head & shoulders above the others, having correctly predicted every recession in the post-WW II period (incl. the last two, in 2001 & 2007) - *unfortunately there is little, if any, scope for an inverted yield curve in a near-zero short-term interest rate environment.*

German exports - In August they slumped by 5.2% MoM (the worst performance since January 2009), whereas a decline of only 0.9% had been expected, as a slowdown in demand from China & emerging market countries took its toll. While the optimists aren't worried since 'YTD exports are up 7% YoY', pessimists worry about the effect of the Volkswagen debacle on exports in the months to come (*bad as this may have been, this shortfall from expectations was nowhere near as bad as that for machinery orders in Japan, a proxy for private capital investment : in August came in at minus 5.7% while a positive 3.2% had been expected*).

QE4 - Given the economic headwinds that seem to be developing, rumours are emerging in the market place of a QE 4 initiative early in the New Year despite the fact that the Fed's own studies have shown QE3 had been less effective than QE 2 in stimulating accretive real economic activity, just as QE2 had been less effective in doing so than QE1 (*which had not been no screaming hell in doing so in the first place*).

Russian bombing in Syria - While Moscow stoutly maintains its bombing is targeting ISIS targets, a map produced by a reliable source shows that of the almost 30 bombing attacks it had been able to identify as of October 1st, three each had been in ISIS-, & government-, held areas and the remainder in areas held by US/Saudi-backed rebels in the Northwest of the country who threaten the Alawite homeland & the Russian naval base at Tartus that lies therein.

Silver - While the silver price is at a six-year low of < US\$14 per ounce, demand for silver coins has gone ballistic. In July the US Mint set weekly quotas because it couldn't meet demand (& is currently running three shifts, & paying overtime, at its Westpoint, N.Y plant that makes its flagship American Eagle silver coins), and in the Third Quarter it sold a record 14.26MM ounces of them, the most for any quarter since 1986. In August the Royal Canadian Mint followed suit in setting weekly sales quotas after record sales in July. Australia's Perth Mint sold over 2.5MM ounces of silver coins in September, up 300+% MoM. And the Austrian Mint also has experienced higher-than-expected demand for its Philharmonic silver coins - *While the CW holds this is due in part to a shortage of manufacturing capacity that panicked people & in part to a silver price slump by 7% YTD & by 70% from its US\$50 all-time high price of April 2011, driven by disinvestment by institutional & retail speculators, one must wonder whether there might be an element of Mom & Pop retail investors heading for the hills (of physical security).*

The global debt picture - Total global debt grew from US\$87TR (246% of global GDP) in 2000 to US\$142TR (269%) in 2007 & US\$199TR (288%) in mid-2014. Although households slowed down the compound annual rate of growth of their indebtedness from 7.3% in the earlier-, to 2.8% in the most recent-, period & the financial sector from 9.4% to 2.9, and that of the corporate sector's increased marginally (from 5.7% to 5.9%¹), the growth rate of all government indebtedness went from 5.8% to 9.3% (i.e. it would double in 7.7-, rather than 12.4 years).

¹

A significant portion of it in America going into a non-productive use, i.e. share buybacks, that artificially boosted per share earnings & made companies more vulnerable to adversity by leveraging their balance sheets.

The mother of all traffic jams – On October 7th, the last day of China’s Golden Week Holiday, the 50-lane Beijing-Hongkong-Macau Expressway became totally gridlocked for hours as millions upon millions of Chinese sought to get back home..

US Syria strategy - On Sunday October 4th Fareed Zakaria on his GPS program on CNN described it, rather aptly, as having moral clarity but being strategically incoherent, and featuring “maximalist rhetoric and minimalist action”.

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RECESSION WATCH (Thoughts from the Frontline, John Mauldin)

- The last few weeks’ data tell us we should be on ‘recession’ watch, the only question being whether it will be V-shaped, as in 1997, or U-shaped as in 2007. Global GDP is slowing down and in the US we are seeing disappointing employment *growth* numbers, earnings forecasts² & credit spreads³. Last Friday’s new job number was outright ugly : private payrolls increased by just 118,000, while government payrolls added another 24,000 *for a total of 142,000*. And the major downward revisions of the July number by 22,000 & August’s by 37,000 mean that Second Quarter monthly job growth averaged just 167,000 *not enough to keep up with labour force growth*, down from 231,000 in the First Quarter & 260,000 in the Second Half of last year. And the reduction in the average work week from 34.6 hours to 34.5 hours was the equivalent of the loss of 348,000 jobs *in consumer spending power*. And while the unemployment rate didn’t budge from 5.1% this was because the participation rate continued to decline (*to a post-1977 record low 62.4%, down from 62.7% YoY & from 62.9% from last May*).

While this is not the CW, most “talking heads” don’t go beyond the superficiality of the data.

ONCE THE BIGGEST BUYER, CHINA STARTS DUMPING US GOVERNMENT BONDS
(WSJ, Min Zeng)

- For all but two months⁴ in the nine years prior to 2014 foreign central banks were net buyers of USTs on a rolling 12 months’ basis. In early 2014 this changed, albeit only briefly, as their net purchases resumed before midyear. But since last March, the global central bank complex, led by those of China, Russia, Brazil & Taiwan, has (increasingly) become a net seller again, at last report (July 31st) at a US\$123BN annual rate

They bought because their countries’, in many cases strong commodity prices-driven, trade surpluses boosted their official FX reserves but now are forced sellers due to the depressed commodity prices & their resultant weaker economic growth (& in China’s case because, since

² According to Thomson Reuters analysts expect a 3.9% YoY **decline** in S&P 500 earnings (and earnings forecasts more often than not are shaded down as their publication date approaches..

³ Resulting in growing signs of distress in the high-yield market where yields in the 10% range now are and where new issue volume has gone from a US\$6+BN monthly average rate in the First Hal to less than one-third that amount in the Third Quarter.

⁴ When they were net sellers of negligible amounts

its August 11th yuan devaluation it has had to buy yuan with dollars to keep its price up, albeit recently at a decelerating rate). But the impact of their selling has been masked by the much of proceeds of the private capital flight from their countries going into the traditional safe haven asset, US government bonds.

DRILLERS BET CHOKING BACK WELLS WILL PAY OFF LONG TERM **(Bloomberg, Dan Murtaugh)**

- *Historically oil companies have let production from new wells 'rip' to shorten their payback period. But a growing number of them from North Dakota to Texas are now restricting the initial flow from new wells, a practice called "choking", in the expectation this will lead to smaller production declines as the well ages &, over time, to higher cumulative production or, as Encana Corp's CEO Allen Gilmer puts it, "You're losing a barrel of production today to get two or three more barrels tomorrow."*

This has at least four interesting aspects. The companies have to spend less money to artificially maintain pressure in the well & need to drill fewer wells to maintain production. One shouldn't read too much in any decline in US shale output. And it is an unintended consequence of the Fed's zero interest rate policy; for the lower the discount rate, the greater the value of a barrel of oil in the ground (with there being a possibility of a double whammy effect if the price tomorrow were to be higher than today). Be all that as it may, this represents a sea change in the mindset for an industry in which, as in many others, the traditional attitude far too often has been too unduly focus on this quarter's earnings, at the expense of those down the road.

SOLAR AND WIND JUST PASSED ... BIG TURNING POINT (BB, Tom Randall)

- According to Bloomberg New Energy Finance (BNEF) wind power is now on a non-subsidized basis the cheapest source of electricity in both Germany & the UK. And it is getting closer to that in the US⁵. To understand what is happening, one must understand the capacity factor concept, the percentage of a power plant's capacity that is actually achieved over time. Thus while the capacity factor of a solar plant may be as low as 20% (because there is no sun at all at night & during the day the brightness of the sun can, & does, vary greatly), that of conventional power plants may be as high as 70% (but seldom more, due to fluctuations in demand & the need for maintenance down time). But what is starting to happen is that the growth of installed wind-, & solar-, capacity is starting to eat into the capacity factor of fossil fuel plants; for once wind-, or solar-, capacity is installed, the marginal cost of using it to generate electricity is only a tiny fraction of the cost of production of fossil fuel-powered plants. So it makes sense for management to max out the use of their wind-, or solar-, capacity; but to the extent this results in a lower capacity factor for conventional plants, their unit cost of production goes up, thereby creating a virtuous circle for wind & solar (the greater the installed capacity of the latter, the higher the cost of conventionally-generated electricity, & the more competitive renewable power becomes). And while wind & solar still account for only a tiny fraction of installed US electricity-generating capacity, it is growing at an exponential rate & getting to the point where it will start affecting the capacity factor of fossil-fueled plants.

⁵ Solar at last report was, on a subsidized basis, competitive in nine states (Ark., Colo., NC, Okla., SC., Tenn., Utah, Va. & WV), actually less costly in nine others (Ala., Ariz., Cal., Ga., La., Miss., Nev., NM. & Texas, and on a non-subsidized basis rapidly closing in on being fully competitive in Ariz., NM, Nev. & Texas.

But the real competitive edge of both solar & wind will come from two other facts. Their generating facilities can be built, & come on stream, in a matter of months, not years (thereby eliminating the need to take a fifty-year view & less need to capitalize the opportunity cost of interest on the capital tied up during instruction). And last, but by no means least, while adding to conventional electricity-generating capacity is 'lumpy', i.e. it takes years to build 500MW installations that, upon completion tend, at least for a while, to create overcapacity, both wind & solar lend themselves to incremental expansion as small as 5 or 10 MW, making it possible to tailor capacity growth closer to demand growth & eliminate the temporary overcapacity problem.

NETANYAHU VOWS TO HALT PALESTINIAN PROTESTS (AP, Ian Deitch)

- A rash of violence began on September 30th when a five member Hamas cell shot & killed Eitam Henkin, a 30 year old rabbi with American citizenship, & his wife near the West Bank city of Nablus, in front of their four children⁶. It continued two days later when a Palestinian stabbed an Israeli to death & seriously wounded his wife as they were walking in the Jerusalem's Old City, and then attacked & killed another Israeli. This prompted Netanyahu to warn on October 5th he will use a "strong hand" to quell violent Palestinian protests & deadly attacks & announce he had sent thousands of soldiers & police to the West Bank & Arab neighbourhoods of Jerusalem with a mandate "to take strong action against those who throw rocks and firebombs" [that same day two teenage stone throwers were killed in the West Bank, one only 13 years old (*which the IDF later said had been 'by mistake*) &, according to the Red Crescent, *the Muslim Red Cross clone*, eight Palestinians were wounded by live fire & 45 by rubber-coated steel pellets].

While Netanyahu⁷ told his fellow countrymen "Trust me, and we'll beat this war of terror too", growing social unrest among Arabs inside Israel proper behind the security fence built to keep trouble makers out⁸ will pose the most serious threat to Israel's existence. For there were Israeli Arab protests that turned violent on Tuesday night in Lod & Wednesday night in Jaffa, and three stabbings on October 7th & four more on October 8th, all over Israel (that prompted Jerusalem's Mayor to close all city high schools on the grounds the funding provided by the government for security staff was insufficient to provide real security), and nine Israeli soldiers were hurt on October 8th in a raid to destroy a terrorist's home (SOP in Israel) in the 80,000 inhabitant Shuafat refugee camp (that supposedly is the most dangerous-, & most weapons-rich-, place in Israel). For local unrest striking close to home may cause some Israelis with dual citizenship to start thinking, if only for the sake of their children, of decamping to somewhere safer (which would start a 'hollowing out' of the Israeli economy since they tend to be its the most dynamic, highest value-added component. As to the West Bank, the problems the Israelis face there now in keeping the lid on, will only be minor compared to those they will have if Abbas were to give in to the pressures to close down the Palestinian Authority, thereby depriving Netanyahu of his West Bank security hand maiden & creating a situation of endless friction between an increasingly restless Palestinian population & vastly outnumbered Israeli security forces whose life will be complicated by the provocative settler minority.

⁶ Which prompted the IDF to immediately deploy no fewer than four battalions (2,500+ soldiers) in a massive man hunt for the perpetrators (that quickly produced results)

⁷ After calling off a high profile visit to Germany.

⁸ That the UN General Assembly, after consulting with the The Hague-based International Court of Justice, in 2004 declared "in violation of international law" by a vote of 150-6, with 10 abstentions.

PALESTINIANS TARGETED BY 'SURGE' OF SETTLER VIOLENCE (al-Jazeera, Patrick Strickland)

- When, in the evening of October 3rd Israeli settlers flooded Jerusalem's historic Old City, shop owners closed their stores & residents locked their doors, listening to settlers banging on their doors & shouting "Death to Arabs." Israeli settlers have been attacking Palestinians and vandalizing their homes, vehicles & agricultural land throughout the West Bank ever since the September 30th killing of the rabbinical couple. Those involved are hardline settlers & ultra-nationalists calling for the killing of Palestinians.
- According to the rights group Ahrar, since September 30th settlers have carried out at least 126 attacks on, or acts of vandalism against, Palestinian property as well as 25 attacks on Palestinians. On October 1st settlers set ablaze dozens of Palestinian-owned olive trees & the next day a group of settlers accompanied by soldiers raided the Nablus area village of Burin & attacked at least three homes while elsewhere they set up road blocks on highways, not allowing Palestinian motorists to pass through them.

One Palestinian likely reflected the sentiment of an overwhelming majority of his community when he observed "The settlers enjoy total impunity. Why should they be afraid when their government protects them and the international community sits quietly and watches." (While al-Jazeera obviously 'has a dog in this fight', it has acquired a reputation for responsible reporting.

RUSSIAN FLIGHT INTO TURKISH AIRSPACE 'UNACCEPTABLE', NATO SAYS (Reuters, Ayla Jean Yackley)

- On October 5th both the US & NATO denounced Russia for violating Turkish airspace (not just once but twice on successive days), and Ankara threatened to respond.

For Putin there is little downside risk & much upside potential in humiliating the US & NATO; for what can they really do about this that would not risk a direct confrontation with Russia (that both Obama & the Pentagon are known to want to avoid at all costs).

GERMANY MOVES TO AN ... APPROACH THAT SEPARATES REFUGEES FROM ECONOMIC MIGRANTS (G&M, Joanna Slater)

- Among the host of 'refugees' that have arrived in Germany tens of thousands are fleeing persecution & violence in countries such as Syria, Iraq & Afghanistan with their right to protection enshrined in international law but many also are just trying to escape poverty or to improve their families' lives. Germany is now moving to differentiate between them & to that end the German Parliament on October 1st passed a law to make it easier to eject economic migrants⁹ & to reduce the perceived incentives for making the journey to Germany from their country of birth. Chancellor Merkel is engaged in a delicate dance between reassuring her compatriots that her government is up to the challenge posed by the largest wave of refugees since WW II & wanting to prove that, to paraphrase Margaret Thatcher, 'The lady is not for burning' (*or rather for being burnt by pretend refugees abusing her people's goodwill*) or, as her Interior Minister, Thomas de Maiziere, put it "We are clearly committed to integrating those who are worthy of protection" while adding that 'those who are not will have to leave'. The new law adds three countries

⁹ With the objective being to reduce the application processing time to the point where the removal of economic migrants from German soil could be achieved in weeks, if not days.

(Albania, Kosovo & Montenegro) to the list of mostly Balkan countries¹⁰ deemed safe enough to be returned to.

*Good luck with this; it will be easier said than done; nor is it likely to stop the flow of economic migrants; the only way to stop that is with a huge-, & costly-, 21st Century Marshall Plan that will make them **want** to stay where they are. And to make that work would require a drastically different approach than the traditional OFA (Official Foreign Aid) one that provided far too much scope for a very few to get very rich by “dipping their beak in the stream” as it came by, thereby immensely ‘thinning the gruel’ for the hoi polloi.*

AFRICAN COUNTRIES TO SEE SUBSTANTIAL SLOWDOWN (G&M, Geoffrey Stevens)

- An October 5th World Bank report forecast their growth will decline to 3.7% this year, down from 4.6% YoY & from the 4.5% *annual average* since 2009. It attributes this not just to the lower commodity prices but also to the Chinese slowdown & electricity shortages in some countries. Among the worst-hit, *not surprisingly so*, are the producers of oil (Angola, Equatorial Guinea, Nigeria & Republic of Congo) & of metal (incl. Botswana & Mauritania), while electricity shortages are plaguing Ghana, South Africa & Zambia, and political turmoil Burundi & South Sudan. On the other hand, Ethiopia, Ivory Coast, Mozambique, Rwanda & Tanzania will grow by 7% or more this year, due to higher consumer spending and more investment in energy, transport & resources. But the World Bank expects the overall growth rate to recover to 4.8% by 2017 on the assumption that commodity prices will recover some & electricity supplies will start to increase (*with the latter having a much higher probability of coming true*). But it also warns of the advent of higher inflation & growing fiscal deficits due to rising wage bills & military spending at a time revenues are shrinking.

This year’s overall growth rate is totally warped out of shape by the fact that the continent’s largest two economies by far are performing abominably, with Second Quarter growth in Nigeria being just 2.3% & in South Africa actually a negative 1.3%.

¹⁰ In the first eight months of this year 40% of the 257,000 asylum applications received by Germany came from Albania, Kosovo, Macedonia & Serbia (of which less than 10% was accepted) & only 29% from Eritreans, Iraqis & Syrians (over 80% of which were accepted)