

THE BEST INVESTMENT OVER THE NEXT FIVE YEARS?

I have spoken for the past several years of my belief that the factors that precipitated the financial crisis of 2008 would reassert themselves later this decade. Various catalysts are in play that will produce dramatic economic developments in the coming years, with the current situation in Greece an example that has captured the headlines.

The underpinning of many things in life, but especially capital markets, is confidence. The Greek Crisis, whatever the short-term developments, has shaken the complacency that has swaddled capital markets with the aid of widespread central bank intervention. There is a very real threat of contagion in Europe as attention is turned to credit worthiness of countries such as Italy and France. A more sober repricing of risk will raise interest rates and make the fiscal status of highly levered nations more tenuous. We might well see a cascade effect.

Central banks will attempt to subdue rising concerns, but the remaining weapons at their disposal are limited. We will certainly see a continuation of the tacit competitive devaluations that have been a feature of the macro landscape. We can expect short term interest rates to remain very low for some time. They will remain low for longer than they should, if history is a guide.

The strength of the US dollar has been impressive, and an increasing number of observers have expressed the view that the greenback is at least fully valued. My view is that the US dollar will likely continue its bull market through the balance of the decade. There will obviously be periodic corrections, but the trend will remain higher. Whatever the flaws of the greenback, it's the best of a fundamentally flawed lot. A combination a fundamental and psychological factors will drive capital to the US dollar. The dollar's principal competitors, the euro and renminbi, are both compromised. The euro may not exist in 10 years given the stresses faced by the European Union. The Bank of Japan can be expected to continue to work for a lower yen, given Japan's dependence on exports.

The US dollar will be attractive to international capital because it retains the prestige of being the reserve currency. It also remains politically stable and militarily strong and enjoys the luxury of not having belligerent nations on its borders. The problems of America are well known, but they don't look so bad in comparison.

US denominated assets will exhibit comparative strength as confidence in sovereign debt is shaken. The US stock market will benefit as international capital seeks a refuge from rising interest rates and weakening currencies. US denominated assets appear to be the best choice for the balance of the decade, based on expectations at time of writing.

The balance of the decade proves to be most interesting from an economic and geopolitical sense. There will be great risks and opportunities. The US dollar will likely be the proverbial “last man standing” in even the most turbulent times.

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