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MELLON ON THE MARKETS

By Jim Mellon

It's late April in LA, it's raining, and it's time for the annual Milken Institute jamboree. Anthony Chow and I are here, having been relieved of a large sum in order to attend. As with most conferences, the true value is in the networking effect, not so much in what is said at the various sessions. Some of the thoughts expressed by the speakers are really interesting, but all of them are ultimately available online.

So, networking we have been, and there is still a day and a bit to go. After that, it's NYC and a final meeting before heading back to Europe. It's been a full round-the-world trip, since I've been hiking in Japan for ten days prior to that.

This hike took place in the poorest of the main Japanese islands, Shikoku, traipsing around Buddhist temples on what the guide described as a "pilgrimage" – but in reality, was a hard walk to gain as much exposure as possible to the beautiful countryside. Another side of Japan is visibly on display here: not the neon glitz of Tokyo or of Osaka, but the hollowed-out countryside, where there are very few children, where the average age of farmers is north of 70, and where people are mostly (relatively) poor.

Japan: defying the coming bear market

This is the Japan that reflects the grim demographics of the country, a country that is destined, in the absence of a baby boom/and or immigration to see its population decline from 125 million today to about 50 million by the end of the century.

Japan is a world leader in robotics and in automation generally, and a trip to Shikoku is a brilliant eye-opener as to why it needs both robots and home-service help for its ageing population. There simply aren't enough young people to go around, and unless Japanese attitudes to foreigners change, there never will be.

That doesn't mean that Japanese standards of living have to fall; indeed, it is noticeable that in my thirty or so years of going to Japan, the country seems to have remained prosperous despite stagnant economic growth. This is partly due to the fact that there has been literally no inflation for two decades, as well as the fact that with a shrinking population, the GDP pie is split between fewer people.

It also means that for we foreigners, especially now that the yen is undervalued and relatively weak, Japan is no longer expensive. Sure, if you want to shop in Ginza or stay in the luxurious five-star hotels in Tokyo, you can – and will – pay a lot. But outside of those, the eye watering prices of twenty years ago have become down-

I still think Japan is a market that can defy the coming bear market signals emanating from the US, and I still think that the Nikkei will go over 25,000 sometime this year, as the S&P and Dow stall.

Facebook: firmly in the crosshairs

On that subject, my call on **Facebook (NASDAQ:FB)** – a short – looked damn good post-Master Investor, but not quite so clever post their results, which were stellar. Those results are a lagging indicator of Facebook's glory days; it is now a company with the appeal of a tobacco company, and its pariah status is only beginning to become apparent. The FTC could levy a fine of $40,000 per infraction of data protection, and if it did, Facebook would be bankrupt. That is unlikely to happen, but the big pots of money the FANG stocks are sitting on, must be tempting to governments and agencies everywhere.

Apparently, 75 governments have now demanded information from Facebook, and although the latter can afford the best lawyers and is adept at making insincere apologies, this time they are firmly in the crosshairs. Take my word for it, Facebook is going down, and it represents the greatest short on the market today, along with Tesla (a cash crash in the making if there ever was one) and, probably, Snapchat as well.

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Speaking of maniacally crazy valuations, Bitcoin et al have reached the first plateau on their way to oblivion. If you still have any of these crypto things, and you're not a despot, money launderer or otherwise nefarious, it's time to get out. Despite some wild forecasts of vast appreciation to come, these cryptocurrencies are on the way down, possibly to where they started. Don't pay to play here, whatever the hipsters tell you.

Place your bets

Gold and silver keep on banging around in a range, buffeted by the winds of macro change. Those winds are now beginning to blow in one broad direction – and that is a move to higher inflation (good for precious metals) spurred by capacity constraints in many major economies, as well as incipient wage pressures.

My bet remains on gold and silver, especially in an environment of bond market bearishness. It is only a matter of time before the important US 10-year bond yield goes decisively above 3%, a key psychological indicator. The supply of bonds in the Trump era of tax cuts and deficit spending will be staggering, and as the supply increases and interest rates rise, there will of course be a bigger interest bill to pay, exacerbating those deficits. Not a pretty picture.

The US dollar is strengthening really because of this and because of “Quantitative Tightening” by the Fed. Charles Gave of Gavekal is forecasting a very nasty surprise this year, and I agree with him. Batten down those hatches and get ready for some incoming fire.

Meantime, at the Milken, the key themes appear to be: real estate everywhere is too expensive and in particular retail space is toast (minus 50% coming according to Sam Zell a grizzled veteran of the industry); and an agricultural revolution is taking place, based around healthier foods, plant proteins and lab-grown meat – the “meatless future”. This could indeed be a huge new industry – as much as $10 trillion a year– and should be watched very carefully. I intend to do a lot more investigation in this area and will report back to you on anything I find interesting.

From a geopolitical point of view, the consensus is that Trump is here to stay and that he is doing to Iran what he did to North Korea – bark hard until there is a retreat. He is doing more or less the same on trade and expect a “deal” with China sometime soon. He obviously doesn’t like Merkel, or the EU. This might represent a good opportunity for the UK, if Mrs May can apply a little magnetism to herself and to the forthcoming trip of the great man himself to Britain.

Overall though, the world economy is slowing. Europe has had its “dead cat bounce” and it was short lived. In Europe, the cheapest market is the UK, and **GlaxoSmithKline (LON:GSK)** has caught my eye, along with **BP (LON:BP.)** and **Shell (LON:RDSB)**, which given recently rising oil prices look dirt cheap.

Happy Hunting!

Jim Mellon