Is Cash King For Now?
Don's Blog 2018.05.29

For the first time since 1974, I no longer own government bonds. Last week, I sold out my position scaling into a nice rally and at week end owned $0. You might wonder why, of all times—when I believe the economy is likely to trend downward—would I sell out of the asset which would benefit the most from a weak economy? The answer is: one should always sell when people want them and not when they don't. And as you know, I have used leverage ever since they did away with Regulation D which forbid the carrying of securities by way of bank loans. So, another answer is, you sell them when you don't have to. In other words, don't let the bank pick your time to sell—that will always be the wrong time. Always leave money on the table.

Do I believe long government bonds will go up in value (down in yield)? Yes I do, but again, remember all the pigs end up in the slaughter house. As you know if you have followed me all these many years, it is my opinion there is no way that our government and may of those in the private sector can ever pay all their debts. If I am right in that judgement, then we are headed for debt deflation, to be followed by run-away inflation. What is the asset to own under those circumstances? There may be others, but energy and gold seem certain to be high on that list.

Over the next several years I expect to make investments in those two areas. However, as an interim move if the stock market gets mashed converting cash, which I now have, into stocks for a trade would be in order. Please note chart #1. Margin debt is at an all-time high and as mentioned previously, I believe the market has topped out for this cycle. Cash may very well be the best asset to hold over the next year. But certainly, it is not for the long-term due to the aforementioned run-away inflation.

It seems to me all of the above makes common sense, but of course that doesn't mean it will be right. As Yogi Berra says, "predictions are hard to make, particularly if its about the future." Maybe the best reason for going to cash is the extreme overvaluation of most long-term assets—i.e. stocks, bonds, and real estate—which has been the case for several years. Please note charts 2 and 3 in that regard. Almost everything is, on a historical basis, predicted to achieve 3% annual returns or less per chart 2.

Based on Haver Analytics information, the S&P 500 for example, carries a 17.3 P/E ratio for 2.1% real GDP. In 1949 one paid the same P/E ratio for 4.6% real GDP. The old bug-a-boo levels of debt continue to advance sharply. Each day sets a new record (see chart 4), and please note what the little dip in 2007-2009 did to the economy and stock market. As for a last item, note chart 5. Does it look like a possible top in corporate debt? Yes, it does; and to add insult to injury, most of the debt over the last ten years has gone to pay out dividends and buy back stock. I ask you: what are those companies doing for reserves when the stuff hits the fan? Will banks and or stockholders come to the rescue? I have my doubts.

Chart 1

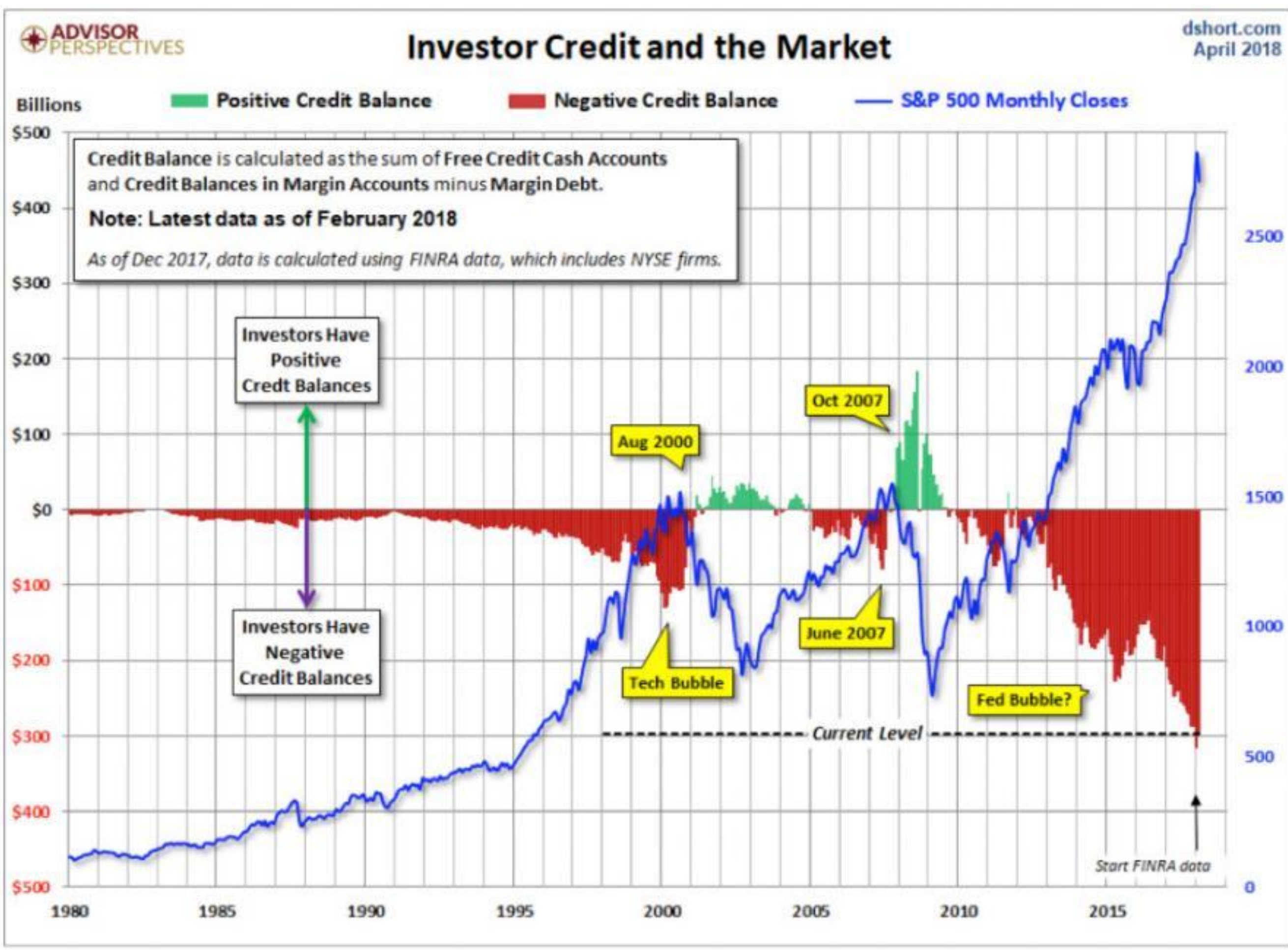

Chart 2

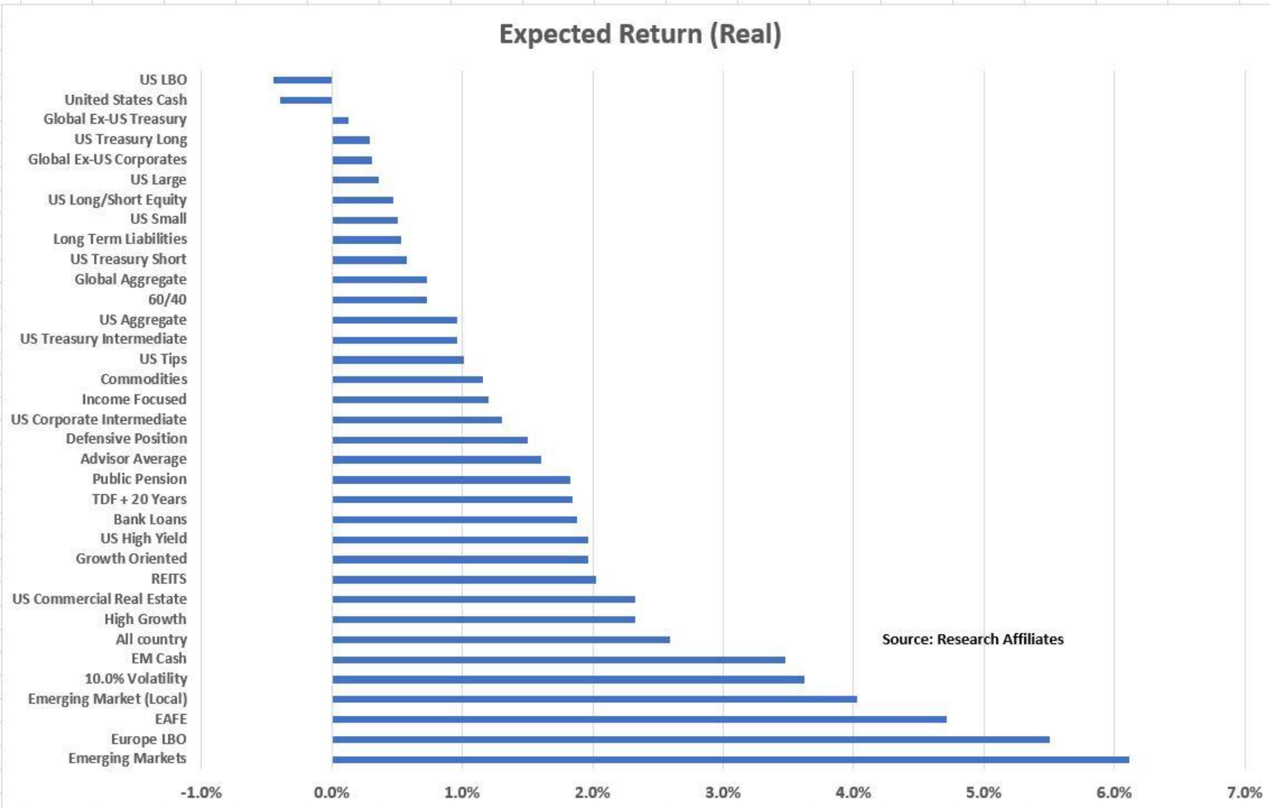

Chart 3

PAYING MORE FOR SLOWER GROWTH!

United States: Historical Bull Markets

(annualized percent change)

Trough Date	Peak Date	S&P 500	Nominal GDP	Real GDP	Months
13-Jun-49	15-Jul-57	17.3	7.3	4.6	97
22-Oct-57	3-Jan-62	15.4	5.4	3.8	51
26-Jun-62	29-Nov-68	12.0	7.7	5.0	77
26-May-70	11-Jan-73	23.3	10.0	5.1	32
3-Oct-74	28-Nov-80	14.1	10.8	3.2	73
12-Aug-82	16-Jul-90	17.5	7.6	4.2	95
11-Oct-90	24-Mar-00	19.0	5.6	3.5	113
9-Oct-02	9-Oct-07	15.0	5.8	2.9	60
9-Mar-09	16-Jan-18	17.3	3.6	2.1	106
Average		**16.8**	**7.1**	**3.8**	**78.2**
Median		**17.3**	**7.3**	**3.8**	**77.0**

Notes:
Source: Haver Analytics, Gluskin Sheff

Chart 4

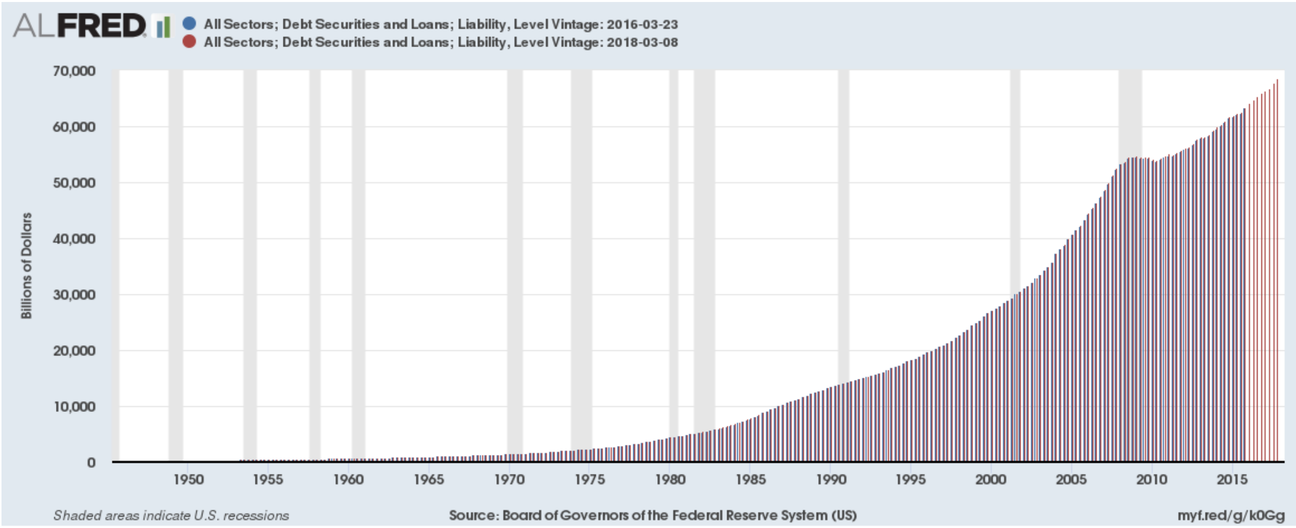

Chart 5