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This is the time of year to sit back, review pertinent information and evaluate the events coming our way. Let us begin with developments in three important arenas: The US and world economies, the wave of violence perpetrated by religious fanatics and the political power shift in the US.

Economic expansion has been surprisingly strong with GDP growing at the rate of 5% in the last quarter, corporate finances are resilient, and stock values are in a historic midrange. What could go wrong? Well, how about the notion that a government that consumes more than 18% of total domestic output is suppressive to the economy? Our government now consumes one-third more than 18% and still seeks to increase.

To that financially stressed condition, add the approaching conflict between entitlement spending and demographics: We are going to have a big advance in the proportion of Americans becoming beneficiaries. The arithmetic is so potent that it scares people away, especially politicians. At the close of 2013, the US debt was approaching \$20 trillion which does not count the future payouts by Social Security and Medicare in excess of projected tax inflows. The cash inflow from payroll taxes will be suppressed as the working proportion of the population will be shrinking at the same time that the number of beneficiaries will be rising and living longer, thereby adding to the financial shortfall. That shortfall is \$54 trillion, a number that dwarfs the national debt. It can be honored only by reducing the promises or using inflation as a tool to devalue them.

Medically, the evolution is toward a second class delivery system for the poor (currently named Medicaid) in which a request for medical help would secure a place on a waiting list. The more under funded the program gets, the longer the wait. Medicare is evolving as a program which will be paying a declining portion of medical costs, and will need to be supplemented by separately purchased insurance.

The European economy is facing trouble. The extent of social spending is beyond the means of most individual states and the imbalance has reached the breaking point in Greece. Soon, we will see which path will be chosen: the one in which Germany lends money to Greece to keep the EU together, or the one where Greece drops out of the union and bondholders take the losses.

In addition to being a weak element in the world economic outlook, Europe also is trying to cope with moves by Putin to dominate nearby nations, as Hitler's Germany did 85 years ago. Incidentally, note the extreme shift in Putin's position on the world stage in only six months. In the early part of the year, he was a heroic warrior restoring Russian domination of the region as in the time of the Soviet Union, which he reveres. Then the price of oil dropped in half, crippling his government's cash flow, reducing the value of the currency in world markets and Russia's ability to

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borrow. Let's hope that he does not, in desperation, move into Eastern Europe to take what he can get before the coffers are drained. Market upsets are possible from this source.

Jihadi violence has become a daily news item, and realization is dawning that a widespread war is underway. The French are gathering in the streets in recognition and fear of the enemies among them, many of whom reside in enclaves governed by Sharia law which substitutes for the national and local institutions in charge everywhere else. Muslims are ten percent of the French population as compared with one percent in the US. Opinions are forming about the appropriate way to deal with a situation in which all the terrorists are Islamists but only two percent of Islamists are terrorists.

A worsening of the condition would include larger scale acts of destruction, followed by intense fear and attempts to get control, such as by sequestration of Muslim neighborhoods, penetration by spies of mosques and other Islamic organizations, jailing of known activists, restrictions on new immigrants, even concentration camps as was done in America in the 1940s, to suppress imagined threats by Japanese immigrants and citizens.

Meanwhile, political argument in America is focusing on basic subjects such as serious violations of our Constitution by the Administration, the need to repopulate the membership of both houses of the federal legislature, and the concept of reducing the size and reach of the government by about one-third.

In all of this, we are pleased to have the intelligence and sanity of the American public to make it all go right.

Essential assets for this mix of realities are stocks, real estate, gold and inflation protected bonds. Cash will be declining in value when inflation becomes more evident, and would be the asset of choice only in a deflationary depression.

Sincerely,

John May