



THE PAIN REPORT

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Guess who is coming to dinner?

**One person who most definitely will not be going for dinner is
President Ahmadinejad.**

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Yes, you may have heard that the leader of the world's largest democracy has been invited to be the guest of honour at President Obama's first state dinner. This to me is great news and is rich in symbolism.

Prime Minister Manmohan Singh is, I believe, the world's best educated political leader with three degrees in economics, the first from Punjab, the second from Cambridge and a PHD from Oxford University. In addition, he has an enviable political track record, which is made even more impressive by the fact that he isn't a typical politician. In fact, he is a very un-political politician. No swagger, no nonsense, very little rhetoric and he actually knows what he is talking about. Perhaps some of the politicians in NSW's state parliament could take note.

Manmohan Singh is largely credited with the liberalisation of the Indian economy in the early nineties, when as finance minister he launched India on its current path. In fact, at that time, Margaret Thatcher described him as the best finance minister in the world.

I have long spoken and written about the remarkable rise of India. It is, as noted earlier, the largest democracy in the world, the largest English speaking nation and, for my Australian readers, the largest cricket playing nation. Also, it is worth noting that Australia exports more to India than they do to America.

Over the last decade or so we have all been mesmerised by the 'China story' and rightly so, however, the India story is similarly remarkable.

Mark Twain had this to say about India, "India is the cradle of the human race, the birthplace of human speech, the mother of history, the grandmother of legend and the great grandmother of tradition."

Albert Einstein was a little less 'wordy' and to the point when he said, "We owe a lot to the Indians who taught us how to count."

You all by now should know some of the amazing statistics; the Indian middle class has tripled to 300 million in the last 20 years, they produce 700,000 engineers and scientists per year, air passenger volumes are growing at about 25% per year (yes the roads are shocking), they sell about 10 million mobile phones per month, yes, per month.

In 2005, at the conclusion of a joint summit with his counterpart from China, Prime Minister Singh declared, "Together we shall reshape the world order."

I have used this quote in most of my speeches since that time and I have absolutely no doubt that his vision of the future will be proven correct. I have long believed that the IC in BRIC was by far and away the key driver and events over the last year have, I believe, proven that.

Coming back to the dinner party.

President Obama's invitation to Prime Minister Singh is a powerful acknowledgement of the significance and importance that America places upon their relationship with this new Asian power. There is much to celebrate in India; however, for those of you that have been there you will know that there is much work to be done, particularly with regard to the terrible poverty in which many hundreds of millions of Indians still find themselves.

I remain a long term believer in the India story. I remain fascinated by the possibilities and opportunities and I am very excited about who is going to dinner.

One person who most definitely will not be going for dinner is President Ahmadinejad. He too recently won re-election. However, his victory was greeted with the largest demonstrations since the days of the Shah of Iran and accusations of electoral fraud.

In recent weeks, the Iran issue has returned to the centre of the geo-political stage and Israel has been busily building a coalition to support a pre-emptive strike on Iran's nuclear facilities. There have been secret meetings with Medvedev in Russia, which suddenly and mysteriously became not so secret, and who knows how many other meetings took place, with the "Can we bomb Iran?" question on the agenda.

This is all brewing as Obama's first big foreign policy test and even the "neo-cons" have re-emerged from near extinction with their calls for Obama to get tough. I am not going to stay on this point for too long as the Middle East is a kaleidoscope of contradictions and geo-political manoeuvrings. What I will say, however, is that I am increasingly of the opinion that a number of powers have signed off on a pre-emptive and surgical strike on Iran's nuclear facilities. The jigsaw puzzle has certainly taken an alarming and clear shape in just the last few weeks; America's concession to the Russians on the missile shield and the sudden discovery of a secret nuclear facility in Iran (which some say was known about for years). So it looks like the Russians are in and we know that the Saudi Arabia and Egypt have never been very fond of Ahmadinejad. What about the Syrians? I don't know and I don't know if they know either. The Germans, French and British look like they have signed up, given their recent remarks. The big wild card for me is China and there is absolutely no way on earth anyone does anything without a nod from Beijing these days, as there are a trillion (\$) reasons why Washington would have to seek China's approval.

The 'dogs of war' may soon shed their leash and we now need to keep a very close eye on the region.

Regarding financial markets, and I will be brief, I remain cautious about the next few months. Yes, I did turn more positive in March, but issued a cautionary note in early September and, yes, that was a bit early. The economic data in 2010 will disappoint, in my opinion, and come in lower than the consensus currently predicts. Markets and policy makers have made the equivalent of a declaration of "Mission Accomplished", just as George Bush infamously did in relation to the Iraq war, way back in May 2003. Markets have now in effect priced in a return to normalcy in 2010, say that to the Irish, Icelanders and the Spanish and for that matter Americans and British too, all of whom will spend less and save more for many years to come. And, yes, developing Asia will spend more and save less, but in overall terms global growth in 2010 will be much lower than the consensus currently suggests. If Iceland was the canary in the financial coalmine, then Ireland was the Dodo and they both sadly provide a lesson to us all. Once the extraordinary fiscal stimulus fades we shall see the whites of the eyes of deleveraging at play. I also note that a number of Asian markets look like they are rolling over and this is most significant as they have surely been the pacesetters in the massive equity rally since March. Notable in this regard is that the Shanghai composite index has entered a bear market, having fallen 20% since their August highs. I think it would be reckless to ignore such signs of fatigue.

One of the more timely indicators of global trade, and hence economic activity, is the Baltic Dry Index, shown below, which measures on a daily basis, the worldwide shipping costs of moving dry bulk goods.

The Baltic Dry Index



Source: Bloomberg

What this chart painfully illuminates is the de facto cardiac arrest that the global economy suffered in the fourth quarter of 2008. It also shows a very sharp rebound from the lows in December 2008 to the recent high in June; however, since then it has fallen sharply. I am aware that there are some supply issues at play here, given that we have seen an increase in the number of new ships, but I still suggest that this very timely indicator is suggesting some slowing in economic activity and that it is too early to declare "Mission Accomplished."

I hope you enjoy your dinner Prime Minister Singh.

All the very best,

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