Deluge

We hear about bearish put/call ratios and heavy put buying, we hear about flights to cash and we hear lots about how financial system problems will lead to economic problems and, by extension, stock market problems. There is some justification for this last point, particularly with regard to traditional cyclical shares.

But nowhere in the main street media do we see, hear or read about the value of, the integrity of, or the prospects for money. Any money. Well, we will. All these headline problems will affect the value of money far more than any stock market.

"Après moi, le déluge" is attributed to Louis XV of France, as a reference to his country's prospects after his demise. Pretty prescient, really – less than twenty years later the revolution, the assignats (paper money supposedly backed with confiscated church lands) and the guillotine arrived. Today there are so many harbingers of deluge that we don't know where to begin. But then, it doesn't matter – if the circumstances are right, all it takes is one.

High on the list is the US debt ceiling. Again. Amazingly, it seems some legislators feel that if the ceiling is not lifted and stays at *x* trillion, somehow this will impose the budgetary discipline so badly needed. God knows the deficits are out of control. But these legislators don't seem to extend their agitation to the point of arguing who/what gets cut if the ceiling is adhered to.

In the abstract, who/what could get cut? Transfer payments? Almost without exception these represent income to somebody. Cut transfer payments and you cut people's income, government tax revenue and GNP. Hardly palatable. Cutting military spending could help, (and would be cathartic) but it couldn't be enough. Big savings could come from cutting debt service but that would instantaneously cause a global financial panic, the dollar to lose its reserve currency status and obliteration of trillions of savings. Not exactly palatable either. So it's odds on everybody swallows hard and up goes the ceiling. Once again, kick the can down the road.

The vaunted ability of the masters of the universe to exert their mastery over the universe is rapidly evaporating and sooner rather than later the pompous brinkmanship we see every day on the news will be blown away. What on earth is motivating Mr Papandreou (fine old family, born in the US, educated in England) to try to lead Greece completely into the abyss? More debt, another trip to the loan sharks, is hardly what his country needs. Maybe he just likes being a member of the poshest club in Europe.

Most of the establishment say a Greek default would be catastrophic. But for whom? Not the indignant people demonstrating in Athens' Syntagma Square. They think default would save $10 billion or more in debt service and the financial and political elite who got them into this mess should bear the pain.

Greece is a template for many jurisdictions. Hundreds (thousands?) of them have collectively floated trillions of paper with neither asset coverage nor earnings coverage. None at all. In fact, most of these governments (and all the ones near and dear to us) float ever more debt just to pay interest on debts already issued. And this raises what should be a serious point.

In Canada and elsewhere there is growing pressure on brokers to judge whether or not an investment is "suitable" for a given client. What happens when pension plans and big brokers, now mindful of regulations, credit quality and S&P ratings, note that some bond has no interest coverage and balk at buying more rotten paper? As they have started to do in Europe?

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The fact is that, for the past three years, banks/institutions have purchased billions of bonds, bills and notes without interest coverage on the reasoning that economic recovery would skate deficits on side. Now the idea of economic recovery, at least recovery for those most in need, is starting to look like a mirage. The oasis is only in policy makers' dreams. In Canada problems loom for weaker oil sands participants, the uranium patch looks futureless and the blackberry patch has been ravaged. There appears to have been serious over-valuation of some forest assets in China and parts of the gold patch may fall well short of expectations.

Will investors continue to see the loonie as a resource paradise? The province of Ontario (40% of Canada's GNP) conducts its affairs on the Greek model. Are its billions of debt suitable investments for anybody? What will happen when the music stops? Probably the federal government will guarantee it, but that would be more bad news for the loonie. In fact, the practice of "A" credits guaranteeing "D" credits (such as the US government and Fannie Mae) is now global and can only hasten the decline of A to D.

Scratch the surface and you probably have dozens of governments with poorly disclosed black holes like Enron and Barings. And, almost without exception, they are more interested in camouflaging problems than in solving them. Stocks may be stressful, but the whole world of bank finances, government finances and currencies in general is toxic. In a "top ten" (top down from most likely to blow up soonest) we suggest: 1. Greece. 2. and 3. Spain and Portugal. 4. Ireland. 5. Belgium and/or Euroland. They live off each other (see clip). 6. Several big States in the US. 7. Ontario/Canada. 8. The UK, which has very poor numbers as well as Scotland. 9. The IMF. 10. The US and its greenback.

Having the greenback as (effectively) the world's only reserve currency immunizes the US from many of its follies. Right or wrong, the greenback will likely live on well beyond its shelf life, sustained as well by blow-ups elsewhere.

In Canada we are going to have a race between a slipping economy and a slipping loonie. As always, we conclude that good stocks are better than bad money.

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Cameron attacks 'gilded cage'

By George Parker
in Brussels

David Cameron has attacked the "gilded cage" mentality of the Brussels elite, after being handed a glossy brochure describing a €240m new European building at the start of a discussion about the Greek debt crisis.

The British prime minister was handed the 16-page brochure on Thursday night before European leaders began a summit discussion on the economic crisis, which is forcing austerity on citizens across the continent.

The building – which will encase what appears to be a giant glass egg – will provide a permanent home to the European Union president, a post now held by Herman Van Rompuy. When the project was conceived in 2004, Tony Blair was eyeing the job.

Mr Cameron was quick to attack the apparent insensitivity of Mr Van Rompuy's staff circulating the brochure – which describes features including "humane gathering places" – at a time of financial crisis.

The prime minister said EU leaders had to demonstrate to disillusioned citizens that they "got it" and that they had to move away from the impression they were living in "a gilded cage".

Although the project is already far advanced, Mr Cameron urged the EU's Council to show restraint and keep costs down.

Sir Jon Cunliffe, the Treasury man poised to become Britain's new EU ambassador, will be told to keep an eye on it.

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