ECONOMIC MYTHS OF THE 20th CENTURY

ECONOMIC MYTH NUMBER ONE

In the late 1960's the U.S. stock market and the U.S. dollar were thought to be the best investments in the world. These were two myths of major magnitude. Reality was that an economic boom created by the end of World War Two ended a 20 year cycle of major recession in the 1950's, which began in the 1930's. The end of World War Two began a seventeen year stock market boom. From 1949 to 1966 (17 years), the S & P 500 rose 415%. Almost every currency was pegged to the U.S. dollar. This created the myths that U.S. stocks were the best and that U.S. dollars were as good as gold.

At that time almost everyone was investing in Wall Street and the dollar. But they were wrong! The rising U.S. equity and dollar cycle had ended. A new cycle had begun. From 1966 to 1982 (16 years) the U.S. market and dollar faltered badly. The dollar fell to barely a fourth its value versus the German Mark, Swiss franc and Japanese yen. Wall Street was in turmoil and the S & P Index rose less than savings rates! The new reality is shown by the top twelev performing markets: Hong Kong, Japan, Singapore, Netherlands, Sweden, Belgium, Denmark, Norway, Switzerland, Austria, Germany and Finland.

The U.S. stock market did not even make the top ten in this new trend. $10,000 invested, which kept pace with the U.S. market turned to $83,700. Those who invested in Hong Kong instead, turned the same $10,000 into $1,052,570 and made $968,000 extra!

At this moment in time, shares are really hot in New York. The fundamental reality? Wall Street's boom is doomed! Since 1949 Wall Street has fitted remarkably well into 17 year patterns of three bull cycles followed by 16 year cycles of bust. In 1949 to 1966 the S & P 500 rose 415% over 17 years. Then from 1966 to 1982 the market suffered turmoil. Starting in 1982 the market rose (again in three waves) by 389% by the end of 1995. The market rose again in 1996 (the 16th year) to a total rise again of 415%.

The U.S. stock market could dive at any minute, yet millions of investors, especially those 50 and under (who have never seen a full cycle as investors), continue to pour billions into this overheated market. These could be wiped out, just as in the late 1960's and 1920's

ECONOMIC MYTH NUMBER TWO

Swiss Francs are the world' s strongest currency. Fundamental reality? Swiss francs can be economic death traps!

This myth may bother you considerably if you have piled your mattress money in Swiss francs, hinged your future on Swiss franc annuities or hold wads of Swiss cash. Before you ignore this warning completely, (just as investors ignored recommendations to invest in Hong Kong 20 years ago did), consider these facts:

Fundamentals in a country are what make a currency strong. The fundamentals of America' s great economic expansion from 1949 through the 1960' s (plus the Bretton Woods Agreement) made the dollar strong then. Switzerland' s economic prudence, efficiancy and isolation made the Swiss franc the bastion currency through the 1970' s and 1980' s.

Now the Swiss fundamentals have changed, because of EMU! The European Monetry Union started when a treaty was signed in Maastricht, The Netherlands , December 1991. This Maastricht Treaty was signed by Spain, Germany, Belgium, Britain, The Netherlands, Luxumbourge, Denmark, Italy and Portugal to create a single, new currency to replace their currencies. Sweden, Finland and Austria planned to join later. All the countries agreed to limit their current deficits to 3% of Gross Domestic Product, to cut government debt to 60% of GDP, plus keep inflation at a low level and maintain agreed interest rate parities.

In 1991 the countries pegged their currencies to not fluctuate more than 2-5%. Investors flocked to soft currencies such as the Swedish kroner and Italian lira because they paid much higher interest rates than German marks, Dutch guilders, etc. Investors said "Now the soft currencies are as good as the hard, why not earn extra interest?"

The problem was few governments kept their promises to lower debt and deficits. The entire agreement blew up! The Swedish kroner and Italian lira were seriously devalued. Millions of investors were ruined.

EMU was such a fiasco that Britain and Italy suspended their currency from the peg. An era of currency turmoil followed in 1993 and 1994 causing interest rates to fluctuate, ecomonies to slow and stock markets to crash. This fluctuation was the root of many economic disasters such as the bankruptcy of Orange County.

The Swiss had stayed out of EMU and the franc rose to its highest level versus the U.S. dollar, yen and German mark ever during this turmoil. This peak, fortified the myth that the Swiss franc was a totally safe currency. As a myth this idea grew more deadly by the hour!

EMU is an incredibly fundamental currency change which will affect the strength of the Swiss franc wether you, I Europe or the Swiss like it or not. The simple economic truth is that governments, no matter how much they wish, cannot wipe out centuries of economic and social development overnight. After the EMU treaty, a German will still be a German, an Italian an italian. Each will still be different in social and economic expectations, work ethics, savings patterns and spendiing habits.

The Masstricht Treaty utterly and totally failed, seriously weakening the EEC. Now the politicians have decided the cure is to have more! Even more countries set a timetable for shifting to one currency, the Euro, in 1999. The beginning of this shift is 1997.

Here's why EMU now will wreak such havoc on the Swiss franc: Many EMU governments (including Italy and Spain) claim to meet the requirments of entry, but don't really. A Financial Times article entitled " EMU, Lies, damned Lies and Statistics" summed this up, pointing out that each country has fudged ecomic figures rather than solve economic issues. Even if EMU governments could meet the treaty guidelines through an all out push, they can't keep up the guidelines over the years. Timing also could not be worse. Europe's economy has been slow. Unemployment is extremely high. Interest rates are at an all time low. Because of this economic crunch, governments have been spending more than usual. At this time, even Germany does not meet the EMU guidelines.

Here is why the Swiss franc can no longer be treated as bastions against all bad currencies. Switzerland has been hit by the slow European economy too. The franc was so strong after 1994's turmoil that Swiss industry had a hard time exporting, especially to Germany. Switzerland is economically in a mess. The economy has not grown for four years. Swiss tourism has been hit hard and Swiss banking has been clobbered by the holocaust investigation and by bad loans throughout Switzerland. This problem has grown to the point that the big three Swiss banks all reported losses in 1996. The unthinkable has happened, one of the big three even had its credit rating lowered!

To weaken the franc and rekindle the economy, the Swiss National Bank lowered interest rates to very low levels. Earnings on Swiss franc savings are below 1%!. Yet the Swiss GDP is still expected to fall in 1997.

Switzerland as a nation does not have adequate land to feed itself. The country has no energy resources at all. This tiny nation must export to earn enough foreign exchange to buy its food and energy. Switzerland must keep the Swiss franc pegged to the German Mark beacuse Germany buys almost half of Switzerland's imports!

Yet EMU almost guarantees the german mark will weaken. being the strongest currency in EMU, the German mark is almost certain to fall as it helps strengthen the rest of Europe's currencies (just as the dollar helped strengthen the yen and mark 20 years ago). If there is currency turmoil in 1997 and the Swiss franc begins to rise in value, expect a negitive interest rate to one again be imposed on the Swiss franc.

Don't get me wrong. The Swiss franc is not necessarily a bad currency. Nor is Switzerland a bad economy. Swiss banks are still incredibly strong. To reinforce this point let me assure you that I still keep much of my wealth in Swiss banks. But certainly not all and especially no longer much of it in Swiss francs.

Do not ignore this reality and fact. 17 years have changed fundamentals which made the swiss franc the number one bastion of safety. These changed fundamentals have turned the strength of Swiss francs from reality to myth. Now the franc is just another currency. Hold it along with others by all means, but realise it too can crash dangerously any time.

ECONOMIC MYTH NUMBER THREE

German and Japanese markets are where the action is. The fundamental reality? Great opportunities are gone in major stock markets. The next wave of incredible profit will be elsewhere.

The myth of Japan and Germany as super power economies was real 17 years ago. The U.S. stock myth was real 17 years before that. Reality now is Germany and Japan suffer like the U.S. from affluent, maturing populations who want more play, less work.

The worst sad truth is Japan and Germany learned too much from America about using debt to grow. They have been seduced by big government. Government spending in germany and Japan is involved in almost everything, from keeping crime off streets to pensions. Medicine, roads, mail, phones, electricity, airports, sewage, schools, mortgages, military, courts, banks, railroads, farming, and insurance, are all plugged into big government spending. Millions are employed and thousands of industries regulated, controlled, subsidised, financed or affected. The system has such force, such power, and so permeates society, like in the U.S. no politician can stop it. Japan is fast catching the U.S. as the largest creditor in the world and has a larger debt as a percentage of its GDP than the U.S. Either market can crash at any time which no one can predict. There is a great risk in major markets.

To make matters worse major markets have little real profit potential now. The U.S. and german markets are at all time high levels. Japanese shares, even though far below their top price, are still at ridiculous price earnings ratios. There is little chance we will see any of these markets rise strongly in the year ahead. There is a good chance they will fall. Why take a chance? Last year major markets seemed to perform well. Their good performance will look more like a myth when you look at the top ten stock market performances of 1996:

Russia: + 100.87% average one year growth.
East Europe: + 56.20%
Bangladesh: + 51.29%
Hungary: + 49.84%
Taiwan: + 35.14%
Malaysia: + 35.10%
Brazil: + 32.31%
China: + 31.27%
Luxembourg: + 31.13%
USA: + 19.33%
Germany: + 14.47%
Japan:- 5.80%

Not one major market was a top performer last year! More proof that getting extraordinary profits in major markets is myth not fact. Why risk investing in markets at all time highs when other markets have much better value and almost unlimited, upside profit potential?

Again don' t get me wrong, the facts above do not suggest that you suddenly run out and invest all your money in Russia' s or Bangladesh' s stock markets. Nor do they suggest you dump all of your Swiss francs. As a conservative investor, I try to see fundamentals as they change so I can maintain a safe and profitable portfolio. Being conservative today is different that being conservative was five, ten or fifteen years ago. In the 60' s, conservative investors put all their money in the U.S. dollar and U.S. shares. Unless they changed, then they lost as much as 50% of their wealth in global purchasing terms. Then 15 years ago, conservative investors diversified into Japanese and German shares and Swiss francs. Now the fundamentals have changed on this too.