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PROVIDING PEACE OF MIND

How Low Can You Go?

We have repeatedly stated that we believe interest rates will remain low and eventually go lower. This has been somewhat of a contrary view in that most people can list a litany of reasons why interest rates will rise. For example:

> Unemployment rates are hitting new lows every year.
> Low unemployment results in higher wages,
> which results in higher product prices,
> which results in inflation,
> which results in higher interest rates.

Ironically, even though decreasing unemployment has resulted in rising wages, it has not produced an inflationary environment.

The absence of inflation combined with a slowing global economy has kept a lid on interest rates.

- At this writing, the U.S. 10-year Treasury Bond has an interest rate of 2.64%.
- The German 10-year bond has an interest rate of 0.07%. (That's zero point zero seven percent!)
- The Japanese 10-year bond has an interest rate of -0.04% (you actually get a NEGATIVE return by investing in the Japanese 10-year bond!)

But the most compelling reason we think rates will trend lower is that Greece, the world's most prolific deadbeat, announced that it is selling 10-year bonds with an interest rate of 3.9%.

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No one should ever lend money to Greece. They have a several-hundred-years history of stiffing investors who bought their bonds. In our March 2010 Investment Commentary, we wrote:

> *There are several European nations that seem to have the problem of spending more than they are producing, which means they have to borrow money from other nations. . . . When a country falls into a recession, being a debtor nation becomes an even more troublesome issue. We made a passing reference last month to five countries that are a cause for concern: Portugal, Ireland, Italy, Greece, and Spain. They are also referred to as the PIIGS.*
>
> *The one getting most of the attention is Greece. . . . Greece likes to spend but apparently is not very efficient about collecting taxes from its citizens. So instead of getting more efficient about increasing its revenues, it has simply turned to the world to borrow, which is kind of like your unemployed cousin telling you he's having trouble scraping together enough money to take the family on a cruise, and could you spot him $10,000.*

In 2011, Greek bonds were trading with an interest rate of over **35%**. In 2015, they traded with an interest rate of around **15%**. In between those years, Greece defaulted on its bonds. How is it that Greece is now able to borrow at 3.9%?

Here's how:

1. With other bonds trading at 2.7% or less, investors are desperate to get a higher yield —apparently with little regard of getting a return "of" their money.
2. The European Central Bank (ECB) is buying bonds of all kinds in an attempt to help stimulate Greece's economy.
3. Investors have short memories. ("This time it's different.")

By the way, there are only four countries whose economies have had growth rates worse than Greece's in the past ten years:

Libya (civil war)
Yemen (civil war)
Equatorial Guinea (corrupt dictatorship)
Venezuela (see Everyone Has Nothing)

This is not a club you want to be a member of.

Obviously, things can improve from one year to the next (and have over the past few years in Greece), but it is expected that they will be wrestling with this debt for years to come.

We'll say it again: Interest rates will remain low and trend lower. Don't get too worried about your Adjustable-Rate Mortgage.

Speaking of Venezuela . . . Last month we gave Maduro (the president) less than 365 days to remain in power. He made it through February, but conditions have not improved and we still feel his tenure as leader is limited.

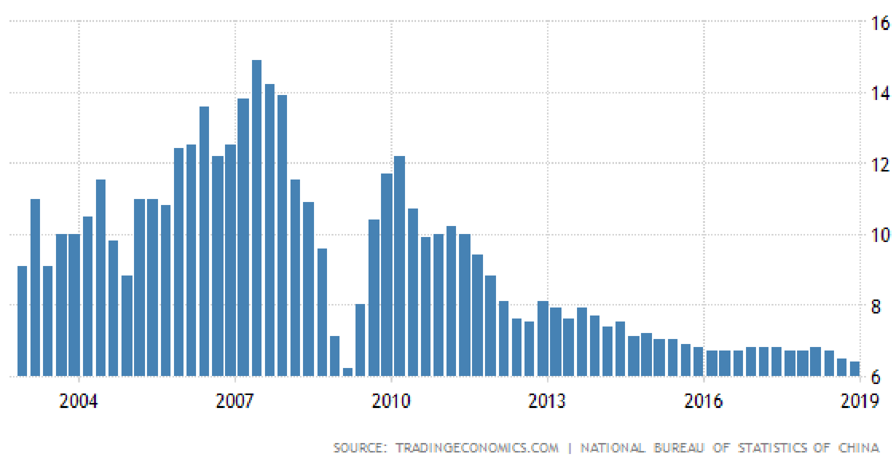
Britain's exit from the European Union (EU) is scheduled to occur on March 29, unless it is postponed/ delayed. (Don't be surprised when that happens.) The referendum to leave the EU was held almost three years ago and, with seventeen days to go, they still haven't figured out what leaving the EU means.

Quite frankly, most people haven't figured out what it means except that it won't be good economically. No one is sure just how bad it will be, but everyone pretty much agrees it won't be good, particularly for the United Kingdom.

However, it won't be difficult to revert back to using the British pound given that they never adopted the euro currency in the first place. This should have been the first red flag that Britain wasn't "all-in" this marriage from the get-go. (Is anyone paying attention to Sweden, which is still using the kroner and not the euro?)

The worrisome part of this is that Brexit will occur against a backdrop of a global economy that is significantly slowing down.

China, which used to be chugging along at 10% per year or more is now "hoping" to grow at 6%. And every year seems to bring an economy growing at a slower rate. The graph below illustrates the consistent and gradual decrease in China's GDP (Gross Domestic Product).



Turns out that, from an economic-growth perspective, maybe their "One Child Policy," instituted in 1979, was not such a great idea after all. A growing economy needs a growing workforce. If you aren't producing children or encouraging immigration, your workforce eventually doesn't keep up. China "relaxed" the One -Child Policy in 2013 and eliminated it in 2016, but it takes eighteen years and nine months to produce an adult.

It was inevitable that the Chinese growth-rate would decline. No economy can continue to grow over 10% forever. Given that China is the second-largest economy in the world, any slowdown there will be felt everywhere.

As for the largest economy in the world, the U.S. growth-rate has not been slowing like China's, but it is not on fire either. In 2018, U.S. GDP grew at 3.1%. We have yet to reach 4% after coming out of the Great Recession . . . and it is likely we see growth go negative before we see it hit 4% again.

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