TROUBLE IN THE U.S. STORE

We are in trouble.

In fact, the entire world is in trouble, thanks, to a very great extent, by the divisiveness, brought about by the US-perceived requirement for an Iraqi war.

As will, most likely, become apparent in the weeks ahead – assuming that the Regime of President Saddam Hussein of Iraq does not capitulate and/or the invading armies of the United States (US) and the United Kingdom (UK) are able to claim victory over this *'evil'* dictator – the US may, already, be enjoying a shallow economic dive, which could lead to another recession as the economic dive becomes more pronounced.

Well-heeled investors are looking for a safe haven for cash: That is easier said than done.

The trick, today, is not to maximise profits, but to secure capital from the ravishes, which are bound to follow in the wake of the war.

President George W. Bush of the US, unilaterally, declared war on Iraq on Thursday, March 20, while Prime Minister Tony Blair of Great Britain backed him with about 45,000 British troops, giving the coalition forces about 280,000 troops in all.

Taxpayers of the US and the UK are paying the price for this army, admittedly, the most powerful and formidable fighting force, ever assembled, taking into account the back-up aeroplanes and warships.

Whether or not the determinations of President George W. Bush with regard to the Regime of Saddam Hussein is correct is one matter (no weapons of mass destruction have been discovered to date), but the divisions, within the United Nations (UN) when the US President declared war on Iraq, were only too apparent.

One of the worst things, politically imaginable, would be for there to be deep divisions within UN because such divisiveness in this world body would undermine, forever, its effectiveness and efficaciousness.

The UN has a great deal of power, political and military; its mandate, from its very founding in 1945, following the cessation of World War II, which killed more than 50 million people, worldwide, is to maintain international peace, the security of all peoples of the world, and to stimulate international economic development.

In short, it must prevent wars; it was not established to initiate international tension, leading to one country, fighting another.

But President George W. Bush decided to fly in the face of the UN Security Council's consensus and, today, it is said that the US is backed up by more than 48 other countries, most of which are members of the UN!

It is accepted that those countries that have joined the US Government's war plan, one way or another, with the exception, most likely, of the UK, have done so for economic and/or political reasons, and, most likely, those governments that have thrown in their proverbial hats in support of President George W. Bush were/are devoid of any strong feelings toward the Iraqi Government of President Saddam Hussein, other than Iraqi oil, of course.

As the maxim goes: Money talks; bullshit walks.

There are, today, fears that the world order is headed for unilateralism, as opposed to multilateralism – multilateralism, being part and parcel of the mandate of the UN.

The original concept of the UN was that a consensus of its members would determine future actions, or non-actions, as the world's policeman would seek to maintain good international order.

President George W. Bush's decision not to abide by the determinations of the UN, which wanted more time in order to try to find a political solution to the Iraqi problem, even though the governments of the People's Republic of China, Russia, Germany and France strongly counselled the Texan not to take unilateral action against Iraq, is, to many people, indicative of a young and immature schoolboy, pouting, following his parents, confiscating his favourite toy.

Without question, Gorgias (5^{th} Century B.C.) would have applauded the actions of US President George W. Bush since this Sicilian-born sophist is credited with the maxim: *'Might is Right'*.

The US President's actions have sharply divided the world's former alliance, the worst such division since the end of World War II, one could say.

Coming to the rescue, one would hope, at least, is that economic considerations will prevail, causing the world to band together, once more.

One saw this when more than 33 more nations, suddenly joined the US, following a US-led attack on Iraq on Thursday, March 20, 2003.

While the US is, definitely, at the peak of its imperialistic, military and hegemonic power, one is reminded of the history of the Roman Empire and the reasons for its ultimate decay and, eventual, destruction.

Rome never recovered.

That the US will prevail against the forces of the Regime of President Saddam Hussein of Iraq is undisputed, but, for the world, the pre-emptive attack by the US into Iraq is, without question, the start of a new era in world politics.

This is only too apparent and needs no elaboration.

The Iraqi war is, also, the most accountable international conflict in history, with hundreds of the world's media, watching every move of the coalition forces on the battlefield and in the thick of the fighting, and with hundreds of millions of people, watching it, day by day, on television sets.

The objective reporting of the hundreds of journalists in Iraq, Kuwait, Qatar and other countries of the Middle East puts the coalition forces on notice that the world is watching their every move.

That the US Government may prove to be correct in its determination in respect of the Regime of President Saddam Hussein may not be the only important issue of today: Because there is another important issue, too: Whether or not the UN will have the power to prevent conflicts in the future.

President George W. Bush feels that he is walking the high ground of morality, which may prove, in the fullness of time, to be correct if weapons of mass destruction are discovered.

Nevertheless, he broke the rules of the UN, rules that the US Government had sworn to uphold: The US Government may not have had the backing of law when it invaded Iraq.

Be that as it may, the US has the largest fighting force in the world and President George W. Bush is well aware of that.

Which country is going to wage war against it because it broke the UN rules?

However, there is, still, North Korea with which the US will have to contend.

First Afghanistan, then Iraq, and then North Korea?

North Korea, with between one million men and women and 5 million men and women, under arms (nobody is quite certain how many of the 25 million human population of the country may be considered as part of the regular army or irregular army), is a very different kettle of fish to Iraq, with its 400,000-man army.

And North Korea, without question, is ruled by a man, who appears to be very short of some gray matter.

That must be the case because, who else would suggest that he would not hesitate to order a pre-emptive attack on the Capital City of Japan, using nuclear weaponry, in order to kill US troops.

There will be much more trouble from this international pariah.

What To Do?

Extreme pessimism in the international investor appears to be justified at this time.

The US may be at the peak of its military power, but all power, by definition, is limited.

Unlike the ocean, where buckets of salt water may be gathered, ad infinitum, power is finite; and, great power is, by its very nature, subject to deterioration in the course of time.

Even President George W. Bush will, in time, come to that realisation, if he is not aware of it, today, and he, too, will be forced to discard unilateral actions in favour of multilateral actions.

As he matures, no doubt this brash Texan will come to understand, also, that no man is an island, and, in the modern world, no single country can stand alone for long.

With each passing day, the cost of the Iraqi war is straining the US economy.

That which affects the US economy, affects the world.

The cost of the war, for just a 6-month period, is now put at not less than $US105 billion ($US30 billion already included into the new US Budget for the 2003 Fiscal Year, plus an Emergency (known, euphemistically, as *'Supplementary'*) Budget of another $US75 billion.

(**TARGET** maintains that, at the end of the day, on the basis of a 6-month war and at least a 3-year reconstruction period for Iraq, the cost to the US, alone, will approach $US1 trillion)

Consumer Confidence, as measured by The Conference Board, dipped an additional 2.30 points in March, to 62.50 points (period ended March 18).

That is the lowest level since about October 1993.

For the previous 10 months, Consumer Confidence had fallen for 9 of those months.

But the March calculations were made prior to the outbreak of the Iraqi war so that one may surmise that the gauge of Consumer Confidence will (or may have, already) fall further.

According to The Conference Board, it is expected that there will be another 47-percent decline, from 62.50 points, in Consumer Confidence over the next 12 months.

It appears that the deterioration in Consumer Confidence is fully justified, all things considered.

The importance of Consumer Confidence cannot be underscored because it is a fairly good indicator of US consumers' forthcoming spending habits; and, its tracking permits manufacturers and importers an insight as to that which US consumers may be buying ... or may not be buying.

It would be silly, in the extreme, not to rule out a recession in both the **E**uropean **U**nion (EU) and the US, one cascading down to another.

Asia will feel the brunt of such an economic recession, first, no doubt: Asia is a main supplier of goods to the US and the EU.

Even if the US could declare victory against the present Regime of Iraq before the end of April – which would be a pipe dream – an economic recession, worldwide, may still be unavoidable.

The price of oil, as at last Friday, had risen by about 13 percent within the previous 5 days, leading up to and including March 28, to more than $US30 per barrel. (Please see last Monday's stock market roundup for the previous week: TARGET Intelligence Report, Volume V, Number 61).

The price of oil is known to represent about 60 percent of the operating costs of most airlines.

And airlines are crashing, one after another, with very few of them, today, able to operate in the black.

Things will get much more bleak with the passing of every day, as far as international airlines are concerned.

Air Canada, for instance, is staring at bankruptcy, to be sure, with debts of about $C30 billion and with the airline, the largest in Canada, continuing to operate in the red.

A number of Canadian lawmakers have gone on record as saying that they do not want to try to save the ailing airline with public funds; and, they would strongly object to such a move in the event that Prime Minister Jean Chrétien suggests it.

Air Canada has a reputation that is not, exactly, that which inspires confidence in its future of this airline.

Back in the US, the labour market is being constrained due, in large part, to the fighting in Iraq.

The number of workers that have been called up to active service in the US Army, Navy and Air Force, or who have volunteered to don the uniform of the US militia, is, now, known to be about 200,000 men.

This leaves a bit of gap in the labour market in what may appear to be, on the surface, an improving labour situation.

However, this is a mirage, only: One should not believe all that one thinks that one sees from afar.

As at March 22, 2003, the number of Initial Claims for Unemployment Insurance in the US was about 402,000 Claims, seasonally adjusted.

That figure appeared to be an improvement over the week, ended March 15, 2003, when the figure was about 427,000 Claims.

The 4-week Moving Average stood at about 423,000 Claims, up to and including March 22, which appeared to compare favourably with the previous week when the figure was put at about 427,000 Claims.

Again, however, **TARGET** would remind subscribers that the March 22 figure was just 2 days after war was declared.

Employers in the US are unlikely, today, to splurge, hiring more staff, in view of the uncertain situation with regard to the war.

Daily, one hears of huge, multinational companies, sacking staff.

This will continue, no doubt.

While spending on defence will continue to increase in the US, giving limited employment to a wide range of workers, this will be insufficient to cause a turnabout situation in the largest single economy of the world.

It is highly unlikely, now, that the economic incentive programmes of US President George W. Bush will re-invigorate the flagging economy.

The US Federal Reserve Board continues to leave short-term interest rates at a 40-year low, but that is proving to be of no practical value since consumers in the US shun the idea of opening up their purses, even one crack.

Motor-car sales continue to droop in spite of the 3 big – General Motors, Ford and DaimlerChrysler – offering exceptionally attractive terms to prospective US purchasers: No down payment on the purchase of a new motor car; zero interest rate over the term of the hire-purchase contract; cash rebates, etc, etc, etc.

The EU's Central Bank

TARGET expects that the European Central Bank (ECB) will cut its interest rates, too, over the next few months.

But that would be equivalent to a panacea, only.

What many, if not most, multinationals are looking to do, today, is to cut costs, repay or reduce debt, and downsize operations because these multinationals fear that the immediate future will be even worse than the immediate past.

This is bound to exacerbate an already difficult situation in the EU.

For a worker, who finds himself without a monthly pay cheque and without any prospects of obtaining alternative employment, the family *'jewels'* will have to be liquidated.

The housing markets of the US and the EU will suffer, first, because, even with the present low mortgage rates, where there is no income, there is no way for families to honour their financial commitments to creditor banks, etc.

The EU housing market will continue to suffer, but the US housing market will suffer even more due to the housing boom of the past few years.

All in all, the prospects for this year, in the US and the EU, look grim.

For the US, alone, it is being estimated that overall growth in the economy will be not more than 2.50 percent, Year-on-Year.

For the EU, many countries will fall into recession: Germany is on the brink, today.

Turning to gold as a hedge is, probably, pretty much a waste of time although, in the past, gold has been an effective hedge against decaying, erstwhile, *'hard'* currencies.

But times are changing.

It is a well-worn maxim that the price of a commodity, such as gold, in order to be an effective hedge against a flagging US dollar, must rise in direct contrast to the extent of the fall in the value of the US dollar, vis-à-vis other *'hard'* currencies.

Put another way, the price of gold would have to rise, if it is to be an effective hedge against a depreciating US dollar, proportional to the decline in the international buying power of the US dollar.

According to UBS Private Banking:

> *'Hedging* (the US) *Dollar as well as other currency risks is best done with currency options, futures and forwards rather than with gold. Alternatively, investors can directly reduce exposure to Dollar risk by selling Dollar-denominated assets, especially fixed income instruments which are highly correlated with exchange rate movements.'*

As for investing in equity markets, in any part of the world, in view of the admissions of many companies of late, and in view of the international situation, which could change, one way or another, any day, that, too, seems to be a complete waste of time.

In which company and in which part of the world may one have confidence that (a) management is not crooked (b) profits will rise, or have the potential to rise, or (c) Provisions will not have to be made for previous investments in telecommunication companies, banks, retailing, etc, or records have not been falsified?

The third largest company of South Korea, SK Group, with annual revenues of more than $US40.80 billion in its 2001 Financial Year, is, today, in serious trouble.

Not less than 10 of its leading executives, including Chairman Son Kil Seung, are up on accounting fraud charges and illegal stock transactions.

The company was put into Receivership on March 19, 2003 after it was accused of falsifying earnings by more than $US1.25 billion in 2001.

PCCW Ltd (Code: 8, Main Board, The Stock Exchange of Hongkong Ltd) has had to make Provisions of at least $HK8 billion in its investment in a telecommunications, joint-venture in Australia.

PCCW, a Li Ka Shing company, is the largest, fixed-line telecommunications company in the Hongkong Special Administrative Region (HKSAR) of the People's Republic of China (PRC).

The company, for some years, has enjoyed negative net worth.

PCCW is likely to be forced to write off, completely, its $HK13-billion-plus investment in Reach Ltd of Australia.

Mr Li Ka Shing, said to be (or has been) one of the richest men in the world, today, cannot fart against thunder, to be sure.

PCCW is but one such company that is facing very difficult times; there are thousands of such companies, around the world, all staring at what appear to be insurmountable difficulties.

The mighty will continue to fall from grace.

There is bound to be a shakeout of many companies, around the world, over the next half a year or so.

As the dust settles, opportunities for investors will be made manifest.

Cash will be king until that time comes.

In the meantime, it would appear that the best action for an international investor is to try to keep his powder dry by looking for currency-linked investments, or straddling *'hard'* currencies.

(The US dollar will, in **TARGET**'s opinion, continue to be the international currency of choice, with the euro, coming in in second place, although, against certain currencies, including the euro, the US dollar could lose a bit of its shine, depending on the length and breadth of the Iraqi war.)

At the appropriate time, it would appear that liquidating currency-linked investment positions and/or cashing in Certificates of Deposit, or other such instruments, would place investors in a position to be able to buy into the Common Stock or the Preferred Stock of solid corporations, which have proven records and which have withstood the ravishes of the past few years – at bargain-basement prices.

But the timing of such investments is crucial.

There are likely to be quite a number of false starts between now and then.

Stock markets will be extremely volatile over the next few months, with indices, rising or falling, spectacularly, on news of gains or losses by coalition forces in Iraq.

One would be advised not to be caught up in any short-term euphoria, which may have been fanned by vested interests in corporations, whose shares are quoted on recognised equity markets, or in the stockbroking fraternity of the US and Europe.

How many times, over the past few years, has one heard a broker, talking from the trading floor of The New York Stock Exchange or The London Stock Exchange, or from his plush office, saying that the time is ripe to invest – while the opportunity exits to get in on the cheap.

One would be advised, also, not to be a party to such mental orgasms, titillated by such people, who make their living from churning investor accounts.

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