- Although there are multiple takes on the global economic outlook, there is a single determining factor upon which that outlook hinges: **the world suffers from over-indebtedness and needs to cure its addiction to credit**. According to a recent McKinsey report, global debt has increased by $56tr since 2007, far outpacing economic growth. With very few exceptions, leverage has increased around the world: total global debt now amounts to 286% of global GDP, versus 269% on the eve of the great recession.
- There is a fixation with the level of indebtedness, but when assessing debt vulnerability, it is the rate of change that matters the most. On this scale, **China appears as one of the most vulnerable countries**. Its ratios of corporate and private debts to GDP have risen by an astonishing 70 percentage points between 2007 and 2014.
- On the upside, there is evidence that **the reflationary effect of lower oil prices is starting to work in energy-importing countries**. In particular, consumers in the Eurozone (EZ) are spending more, not deferring purchases, as would be expected in deflationary conditions. The EZ is technically in deflation, but the dreaded deflationary mind-set has not yet kicked in.
- Central banks in the Eurozone (EZ), Switzerland, Sweden and Denmark have just moved to negative interest rates; thus casting **investors into a world of negative yields** already amounting to $2tr (comprised of both sovereign and corporate bonds, like Nestlé or Shell). As much of the world flirts with either lowflation or deflation, **this situation will endure,** with two main consequences: (1) It pushes many investors into risky assets; (2) It makes the life of insurance companies and pensions funds a misery - no longer able to match returns (often expected at 8%!) and liabilities.
- Technology and human capital are acclaimed as two silver bullets - the holy grail duo of innovation and education that will soon deliver much higher productivity. Although vital, alone these are insufficient motors for rapid growth, for which a third but more elusive factor is needed: social capital (trust). This critical ingredient is sorely lacking. Different surveys show that **trust** in institutions (all of them!) **is evaporating and at an all-time low**. The overall sentiment of distrust is further exacerbated by rising inequalities. The consequence: **at a time of deficient social capital, the digital revolution might not deliver as much growth as is commonly hoped.**
- Almost all the world's most advanced economies are democracies; but **liberal democracies are now in trouble**. Dogged by a general malaise and elector disillusionment, they seem dysfunctional and unequal to the dramatic "efficacy" challenge: unable to deliver the goods and to renew the social contract. **Their challenge is not one of leadership but rather governability.** The situation is not much better in "illiberal" and "low-quality" democracies. In countries like Russia, Turkey, Thailand, or Bangladesh, democracy is receding and the rule of law being eroded. The challenge they pose to investors is less about governability than **unpredictability.**
- The agreed 4-month extension on Greece's bailout doesn't bring the curtain down on the Greek tragedy. It merely postpones thorny negotiations between Greece and its partners. Within the EZ itself, **infighting between the partisans of the "amputated leg theory"** (who want Greece out before it "infects" the rest of the EZ) **and those of the "domino theory"** (who fear that a Grexit would entail a cascading effect) **will fester**. Many hurdles remain and much could go wrong. What are the main risks? (1) A sharp deterioration of the Greek economy that would render the pursuit of an agreement impossible; (2) Dissensions within the governing coalition or an implosion of Syriza itself.
- If any more proof was needed that **technology is turning the whole world of business upside-down**, look no further than the automotive industry. As "**software is eating the world**" (an expression coined by Mark Andreessen), a tech company can now mutate into a car company, which is why Apple and Google have decided to enter the market. Since electronics have "invaded" the car – representing 40% of its cost -, owning technology and licensing software will prove more beneficial than manufacturing *per se*.
- The investigation into tax evasion at HSBC's Swiss subsidiary has turned into an enquiry about its global CEO's own finances. The public debate is no longer about past illegal practices, but rather what is rightly or wrongly perceived as "legal" corruption, and the much more tricky notion of "violation of public trust". One thing is certain: **the move to transparency, and the global crackdown on "legal" tax evasion, for individuals and companies alike, is bound to intensify**, with dramatic implications on things formerly taken for granted, such as the validity of the non-domiciled resident status in the UK.
- With respect to transparency, a spate of recent affairs shows that **the sacrosanct notion of privacy exists no more**. In less then a week, the media revealed that: (1) US and UK intelligence had stolen encryption keys from Gemalto - one of the world's leading SIM card manufacturers; (2) Kaspersky had found preinstalled malwares on most hard drives; (3) Lenovo computers had been shipped with preinstalled malware … **This is what a post-Snowden world looks like**…
- Our list of major "must-watch" issues for investors and decision-makers: (1) **growth deceleration in China** - the biggest economic risk of 2015 - and its inevitable knock-on effect (2) **deflationary pressures and rising political risk in the Eurozone** (with a focus on Greece); (3) a **possible "distress loop" in the market for EM hard currency corporate bonds** – which now amounts to about $2tr**;** (4) global geo-political turmoil, with a focus on Ukraine / Russia. For real-time or in-depth analysis on any of these, and if you are interested in prediction markets to better forecast some of the risks, please contact us.
- It's ironic to sell a predictive macro newsletter by confessing: "I don't know", but we don't intend to make it up as we go along! For a surprising number of issues covered in the Barometer, **the outcome is just unknowable**. Whether Greece will default or not; whether China will experience a hard or soft-landing, and so on… The outcome of these issues of bewildering complexity, determined by so many different parameters conflating with each other, **simply exceeds our cognitive abilities** to predict with confidence. Most experts and opinion-makers exhibit "confidence authority" when in reality they simply "can't know". It's a trap in to which we do not want to fall. **We prefer to harness the power of technology by leveraging the wisdom of an "enlightened" crowd using prediction markets.**