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# SWH CAPITAL

## Financial Outlook

# A year on...the story continues

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- Little change in policy response
  - Exceptional monetary policies: ZIRP and QE
  - Deficit spending
- Consequences
  - Central Bank Balance Sheets expanding
  - Debt levels increasing
- Growth looks fragile
- Is this sustainable? What are the risks?
- Energy innovation is critical

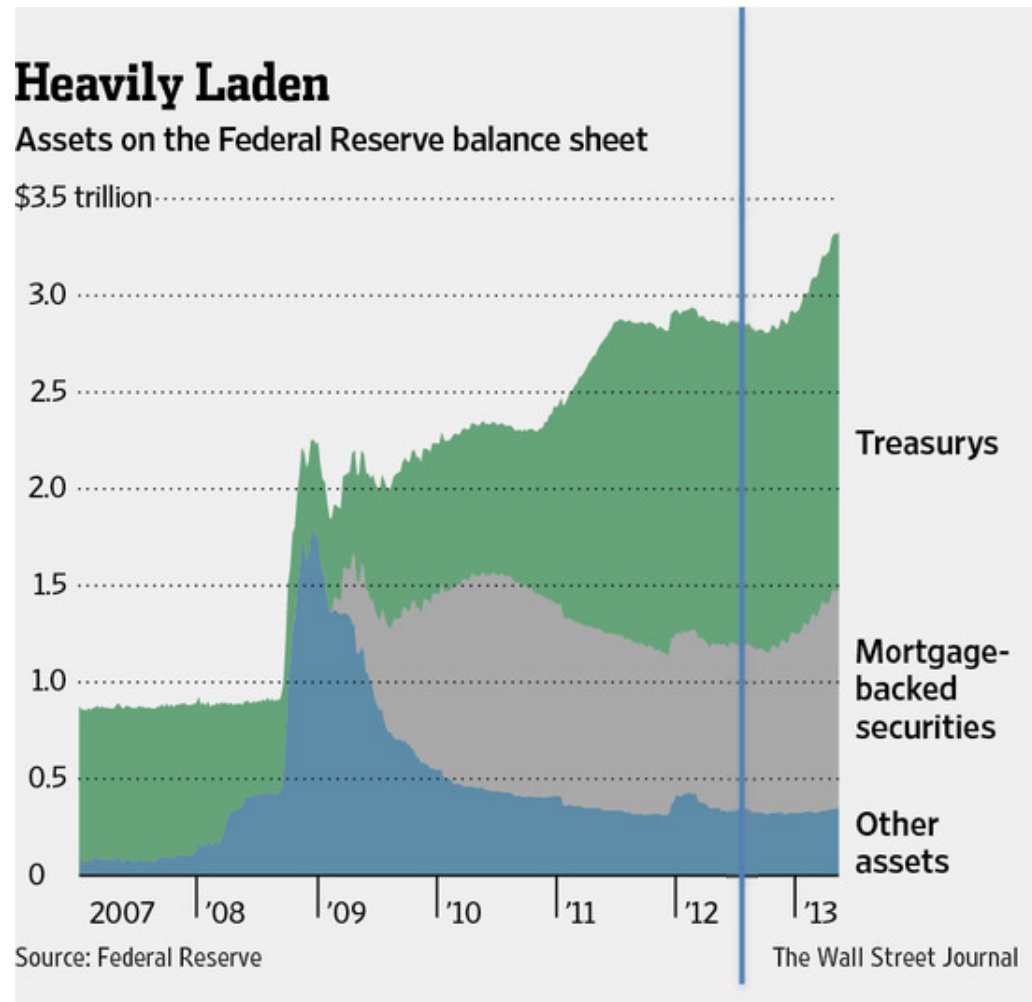
# Deficit spending and debt levels...

General government gross financial liabilities as a percentage of GDP

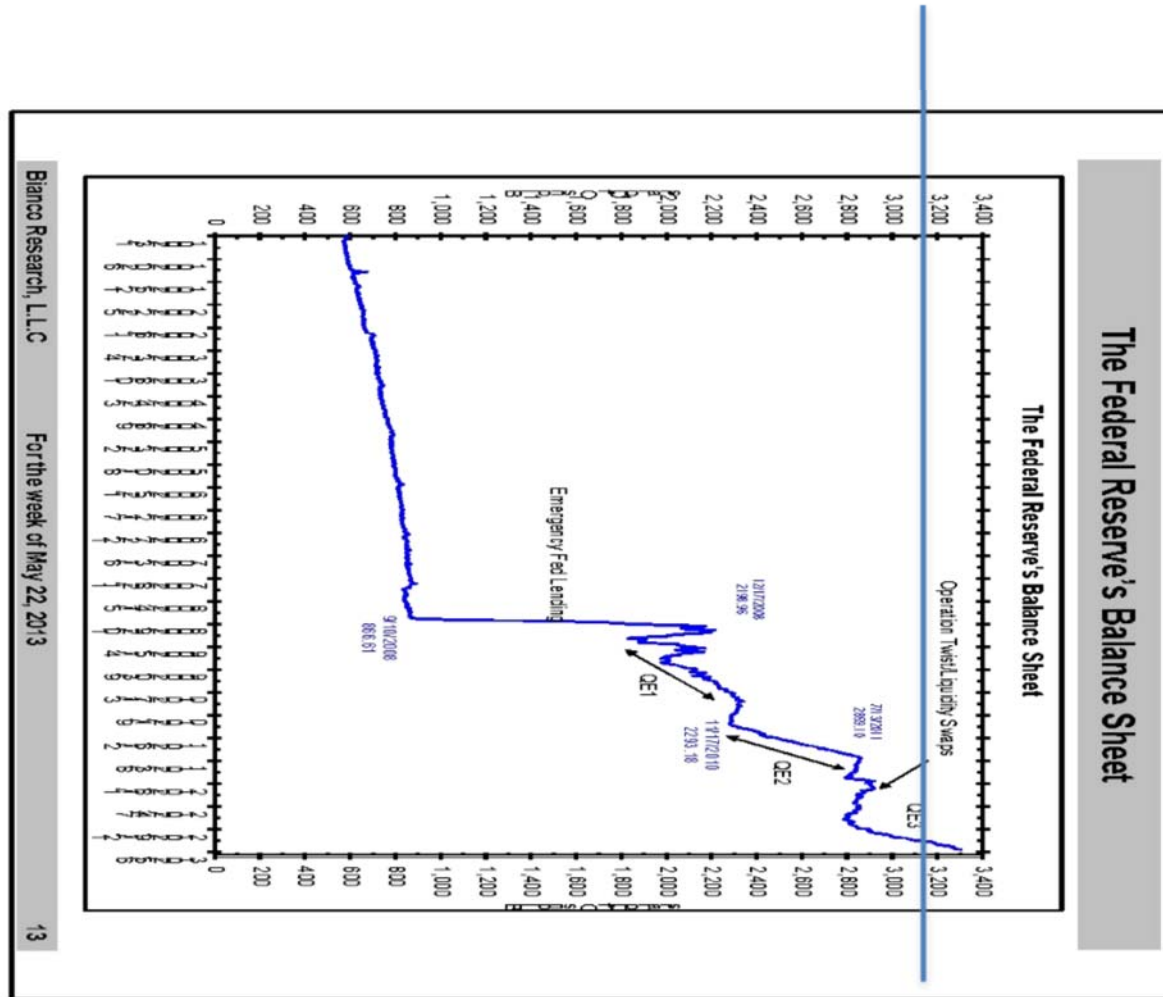
Source: OECD.

<b>Gov. Deb as % of GDP</b>	<b>2007</b>	<b>2013</b>	
Japan	167.0	226.8	36%
Greece	115.0	183.9	60%
Italy	112.1	126.6	13%
Iceland	53.3	126.2	137%
Portugal	75.4	123.7	64%
United States	62.1	108.5	75%
France	73.0	104.1	43%
United Kingdom	47.2	102.3	117%
<b>Euro area (15 countries)</b>	<b>71.8</b>	<b>98.2</b>	<b>37%</b>
Canada	66.5	96.6	45%
Germany	65.6	86.4	32%
Spain	42.3	79.0	86%
<b>OECD-Total</b>	<b>73.3</b>	<b>108.4</b>	<b>48%</b>

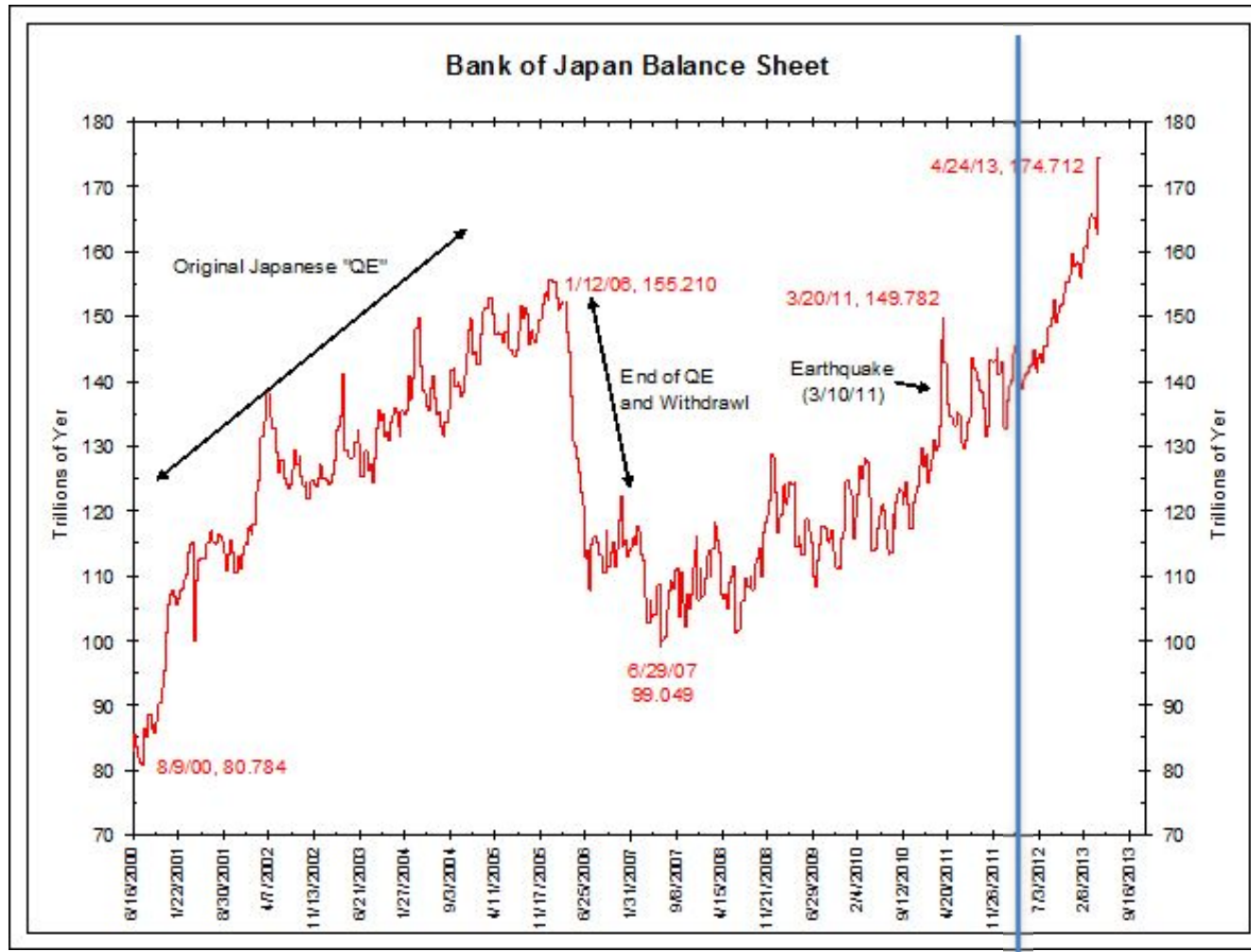
# A year on...Fed balance sheet



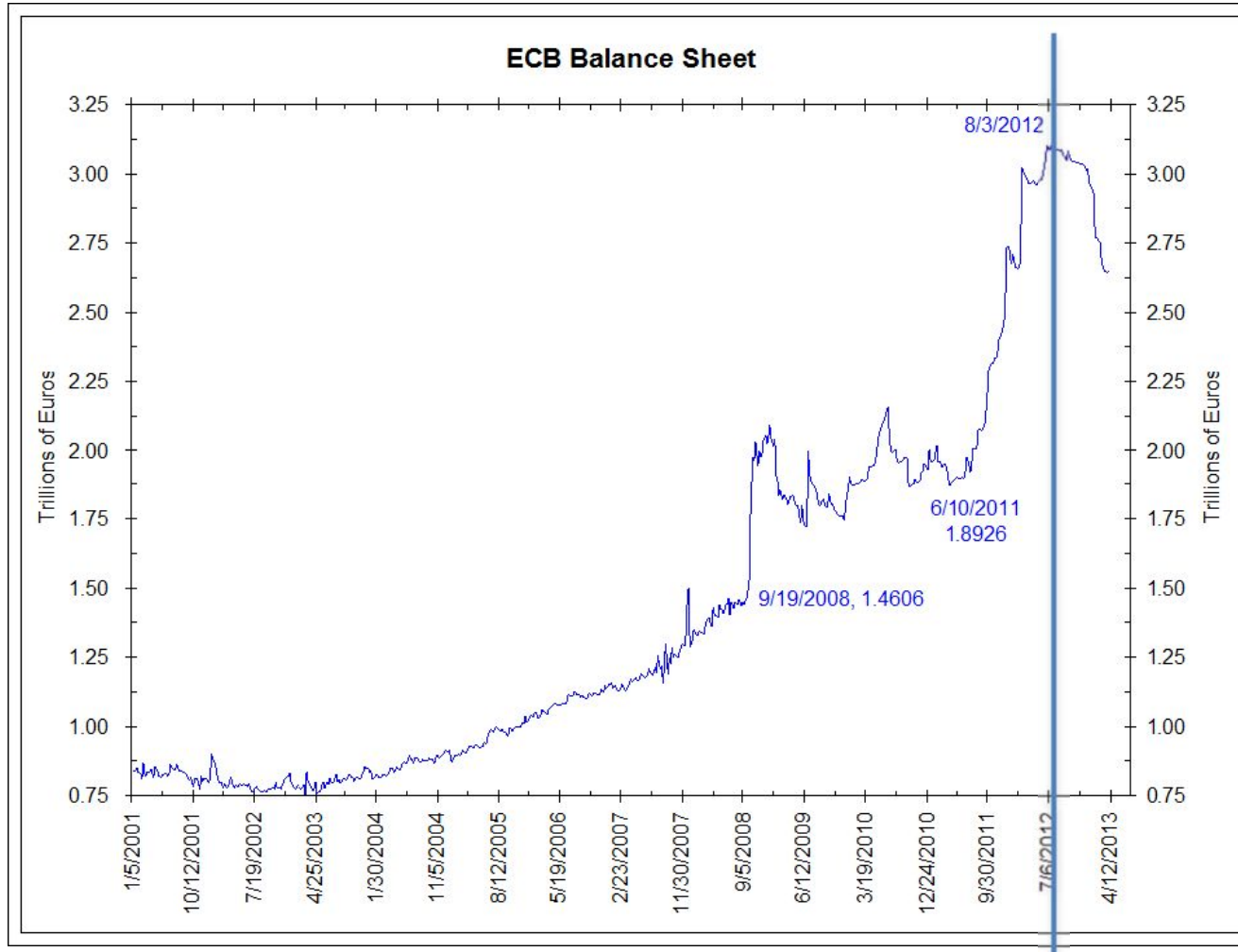
# Fed buying \$45Bn of MBS and \$40Bn of Treasuries per month



# BOJ now buying substantial more JGBs



# ECB Balance Sheet



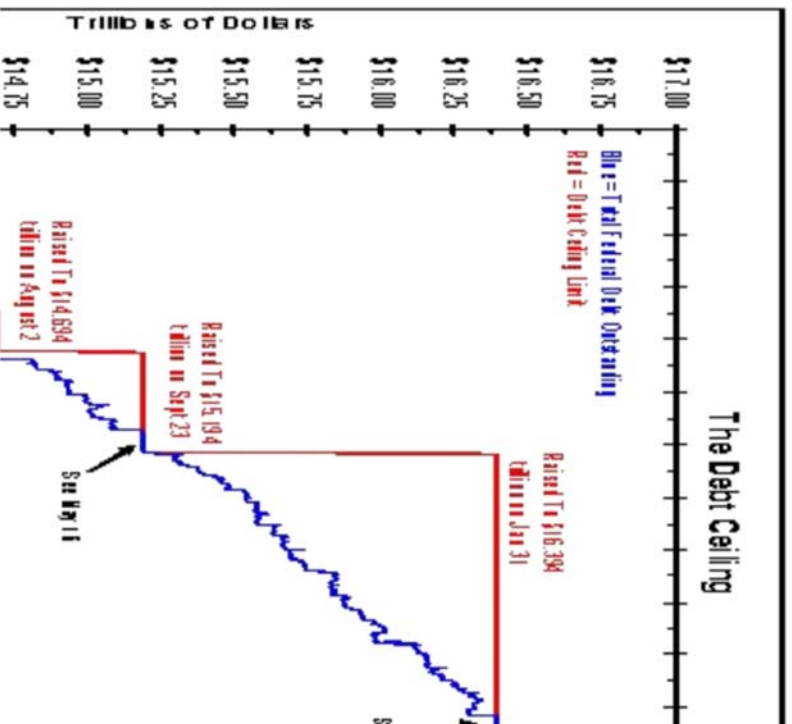
# US Debt Ceiling

## The Debt Ceiling Returns

### 2) - U.S. to Hit Debt

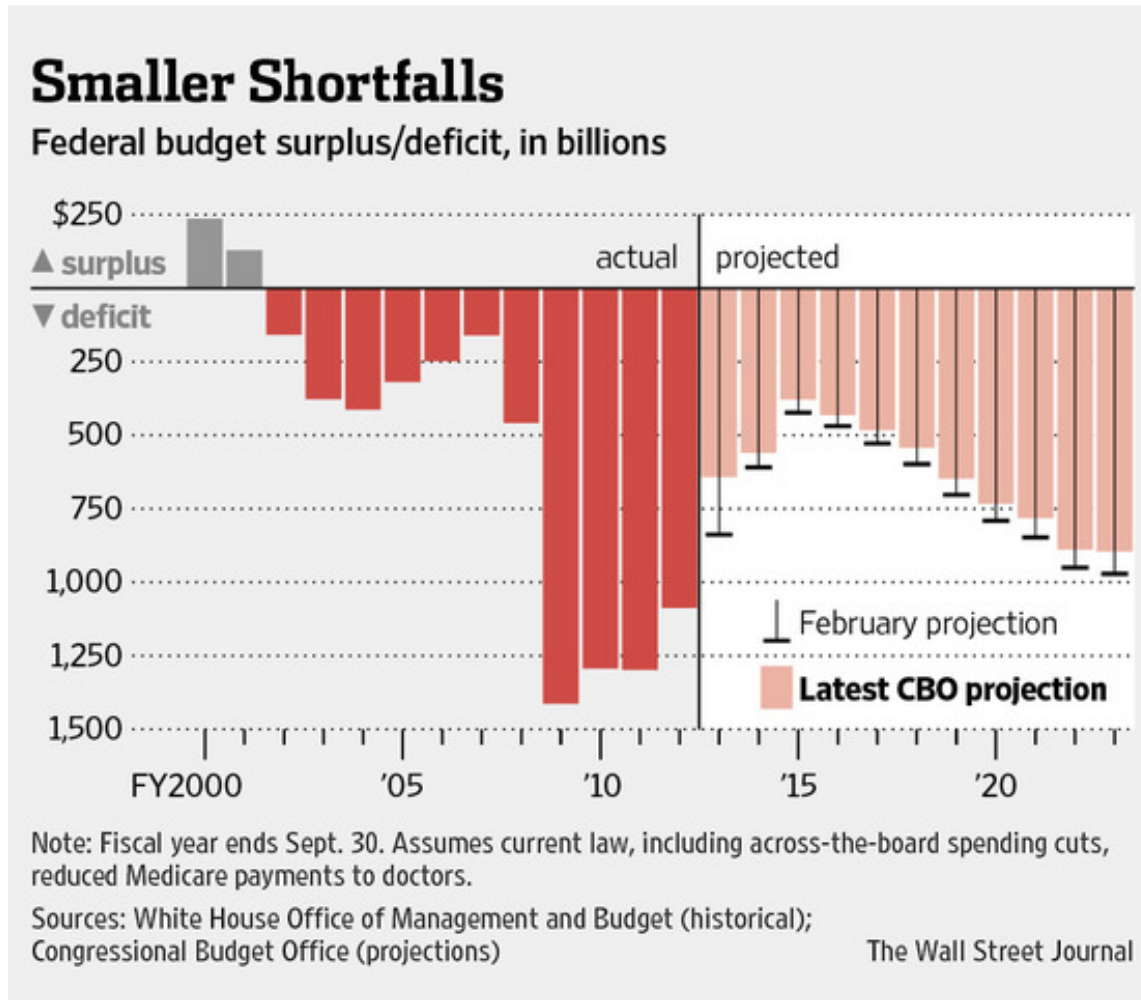
#### 1 Room

p against the federal  
 series of emergency  
 ng all of the nation's  
 , Treasury Secretary  
 artheless, Congress  
 to protect America's  
 entially catastrophic  
 till it is too late," Mr.  
 and Senate leaders.  
 o suspend the debt  
 e White House and  
 y and tax plans. But  
 on May 19 the debt  
 ious level, plus the  
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 Treasury will be up  
 ew said the Treasury

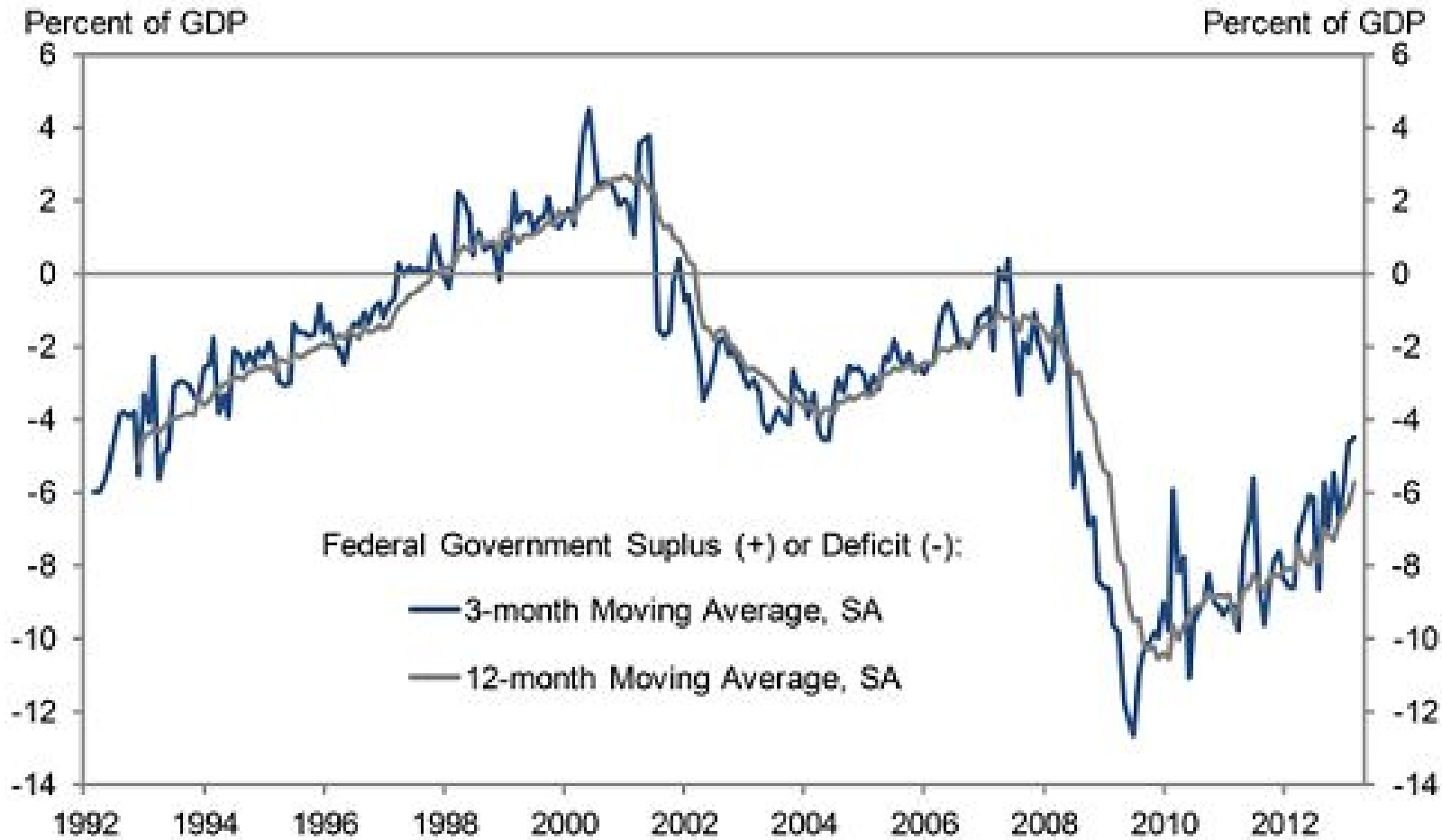




# US deficits have stabilised...

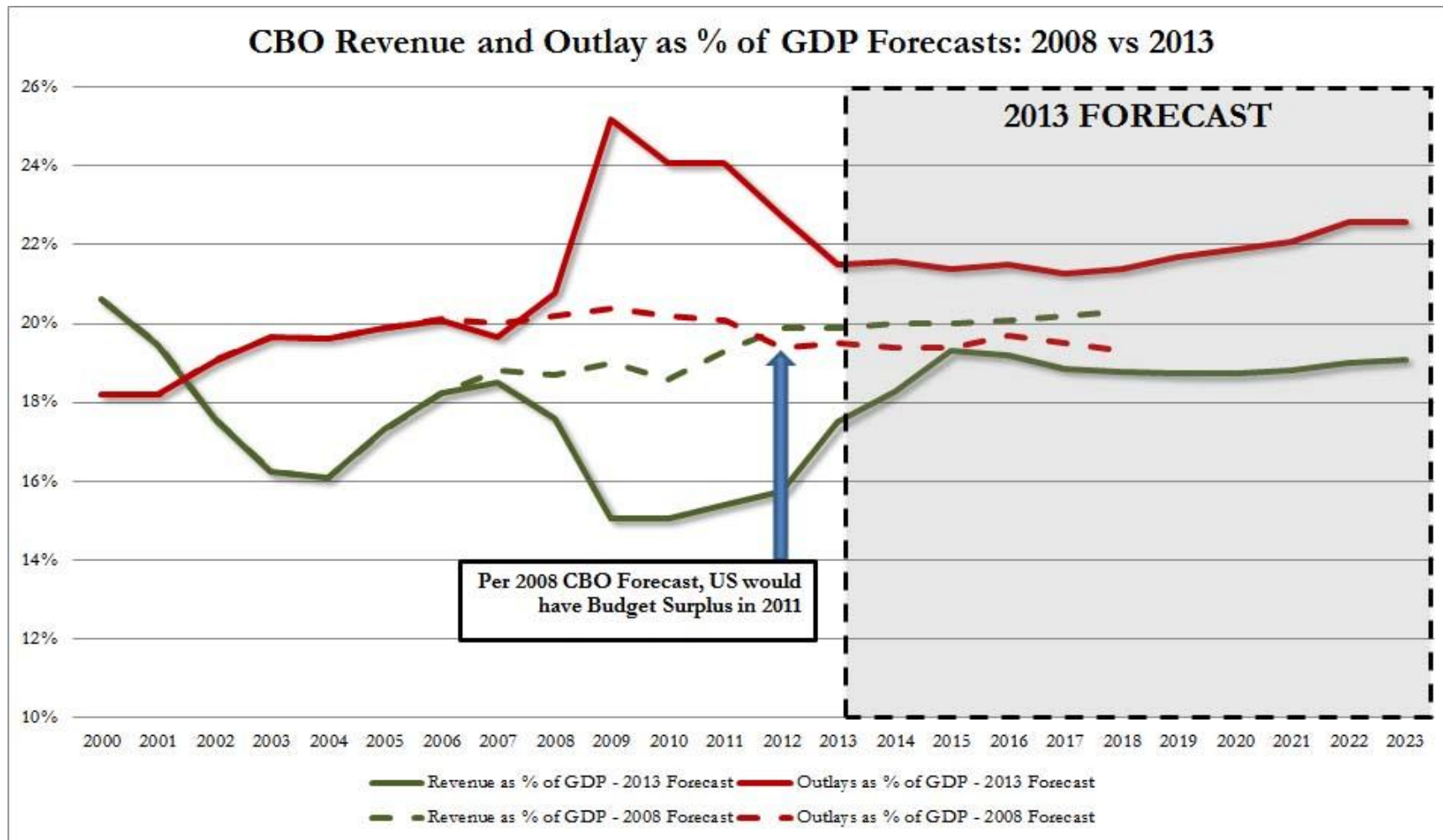


# US deficits...

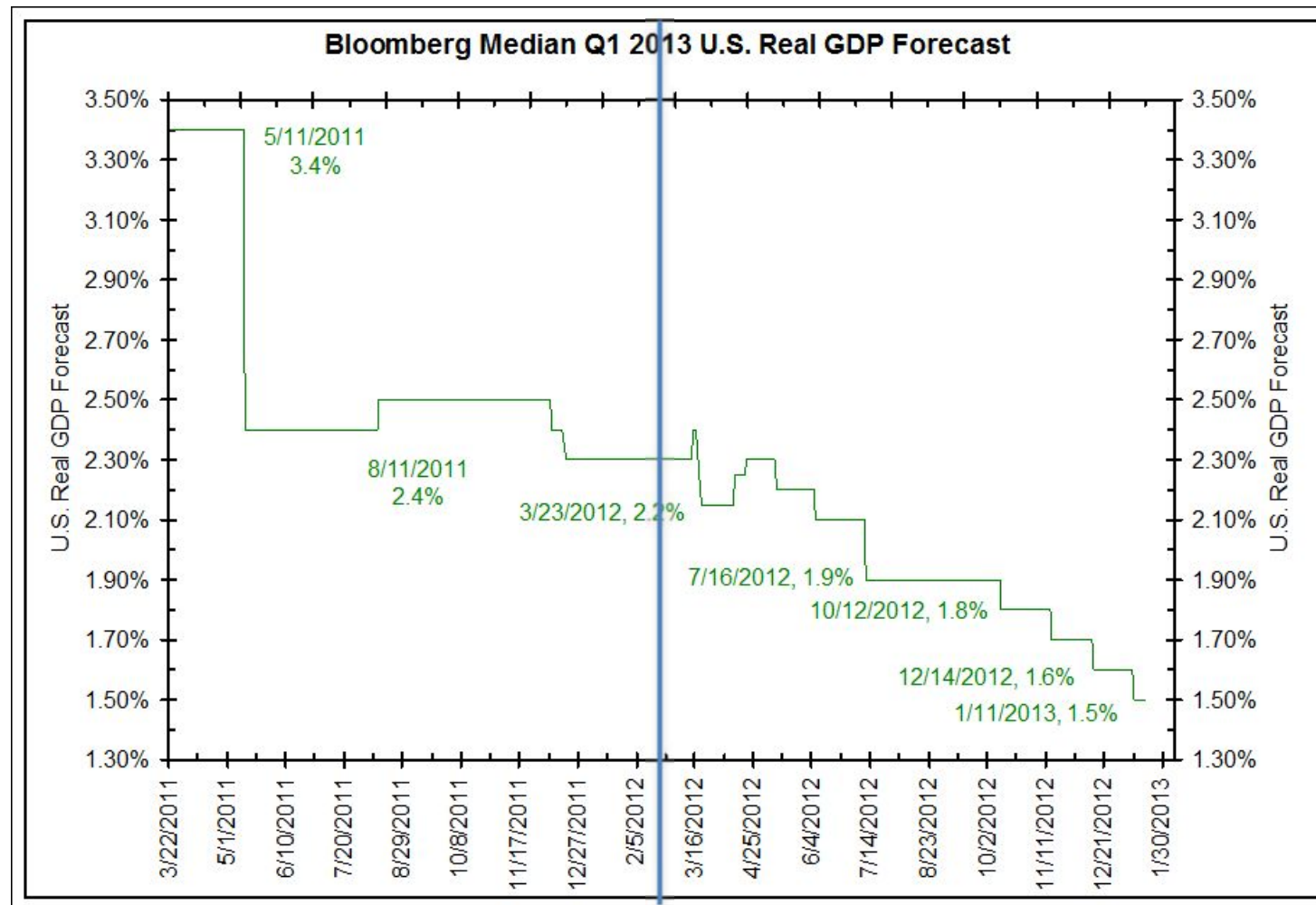


Sources: Goldman Sachs, Treasury Dept., Macroeconomic Advisers

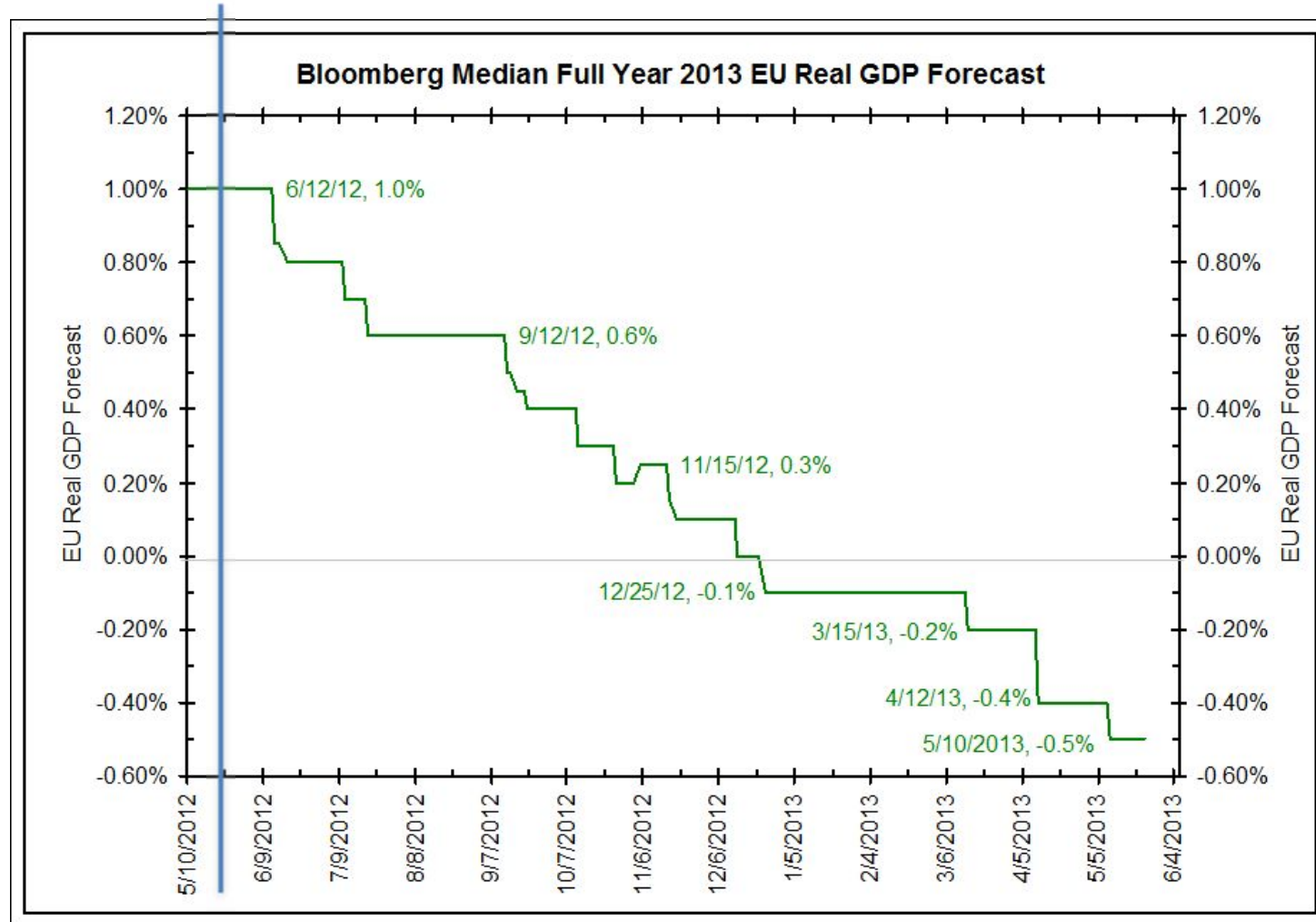
# Are CBO figures too optimistic...?



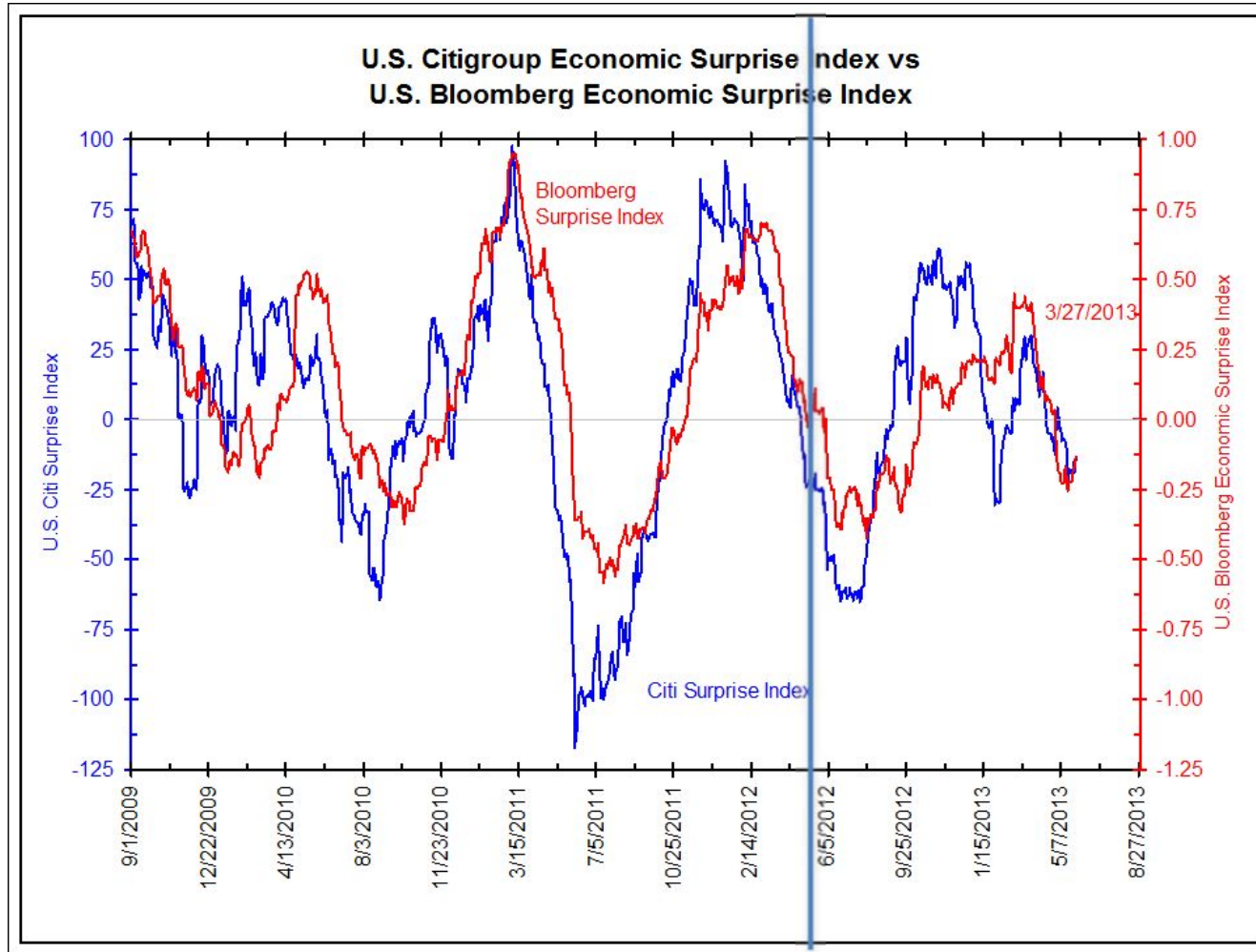
# Are growth expectations falling?...US



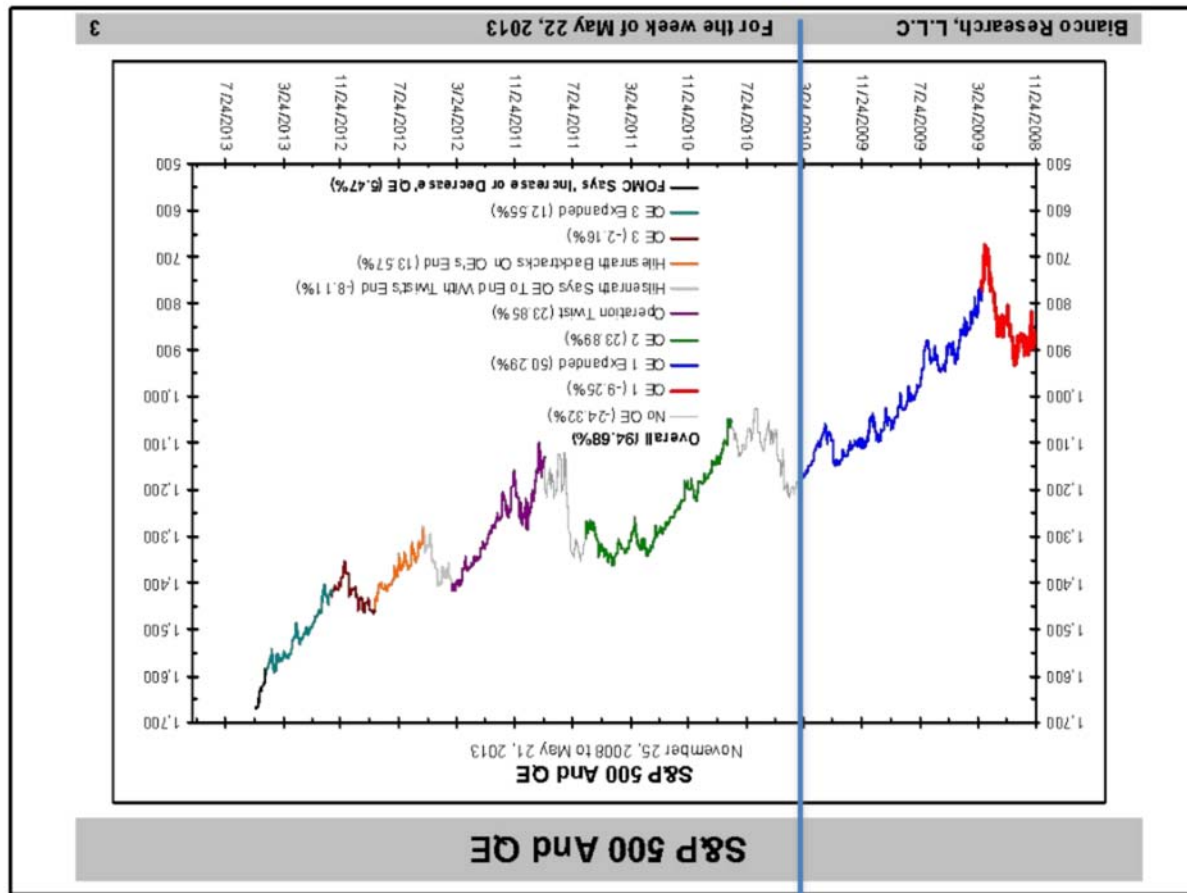
# Growth expectations are falling?...EU



# Economic surprise index



# Equity markets makes new highs...

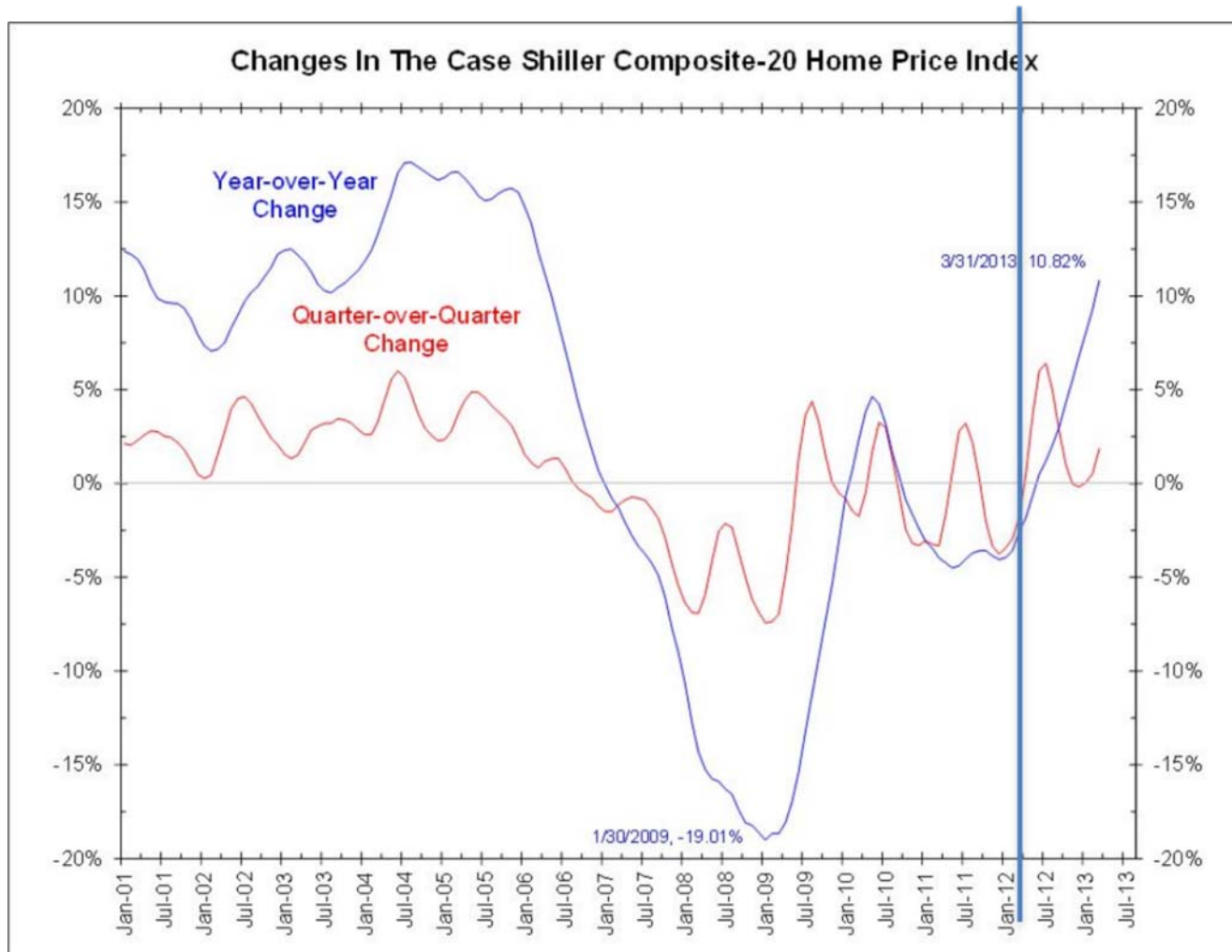


TEAC 2013

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# And house prices...





# What can we expect now?

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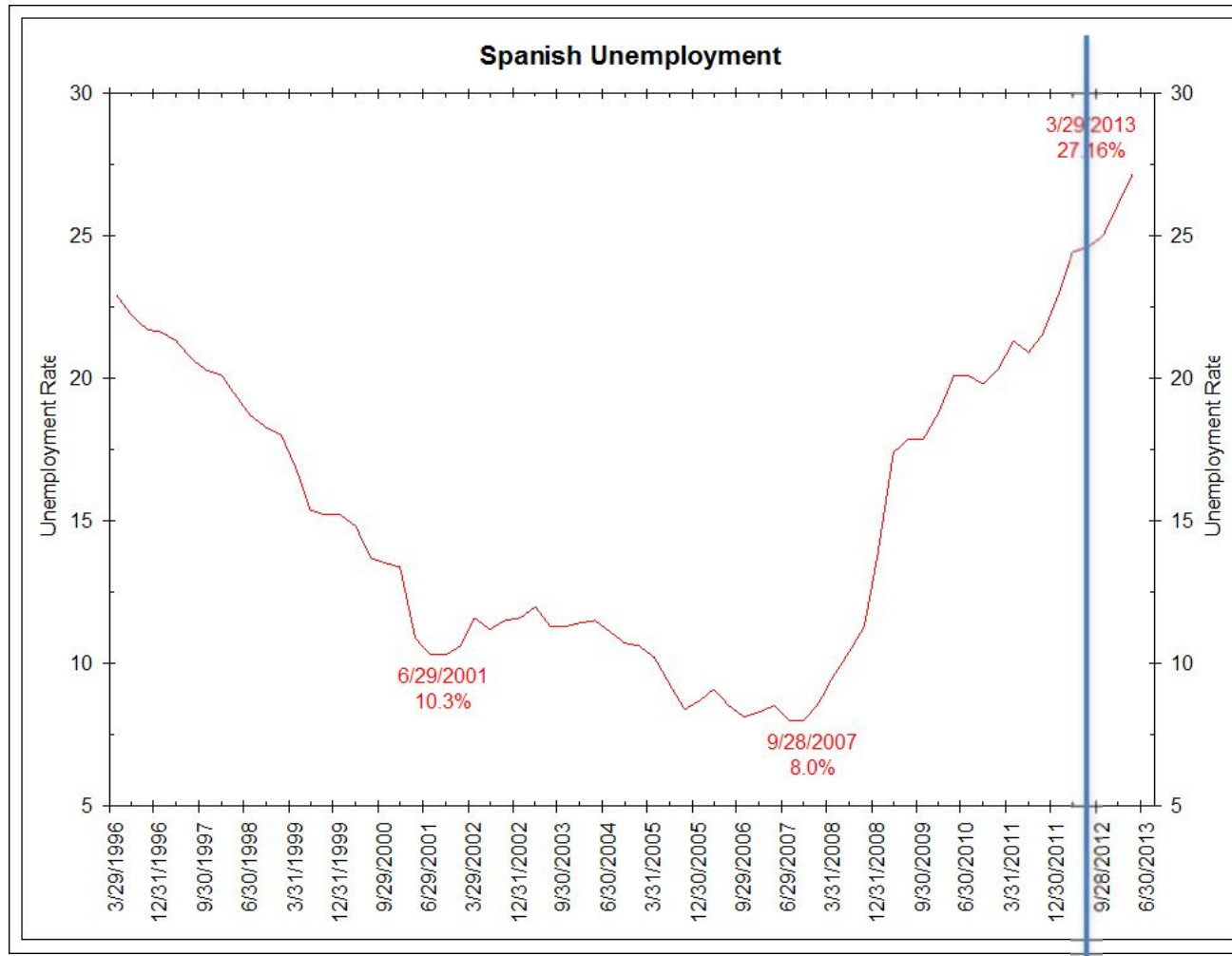


# Risks

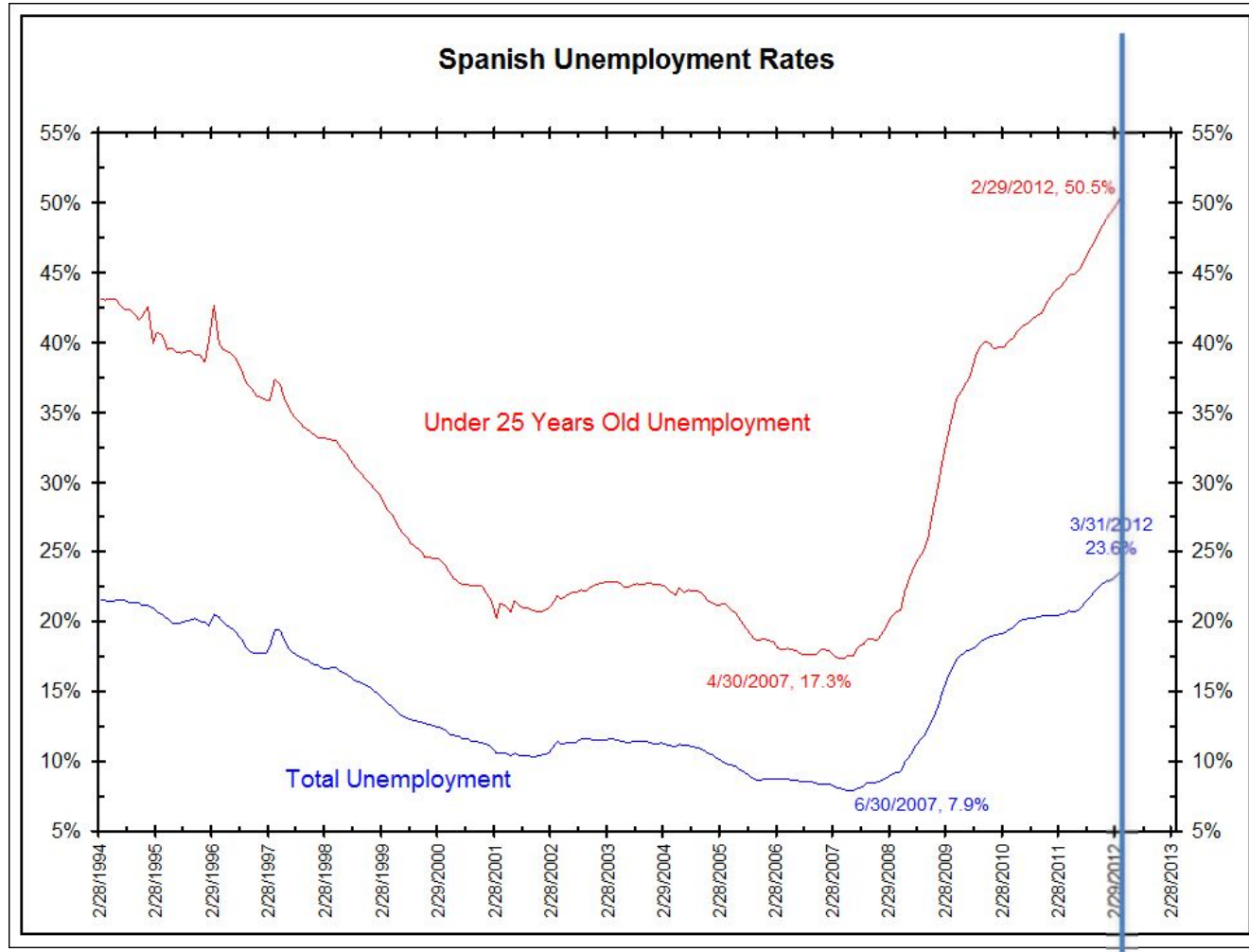
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- Policy error
  - Inflationary outcomes
  - Deflation outcomes
- Political
  - Monetary policy used as a substitute to difficult structural reforms
  - Employment
- Euro
  - Economic chaos and policy uncertainty
- China
  - Sustainable growth?
- No growth
  - Leads to declining ability to service private and public debt
- Japan
  - At \$4.4Tn the third largest economy (with an acute energy problem)
  - At Y1Qn the second largest bond market (Italy is the third largest)

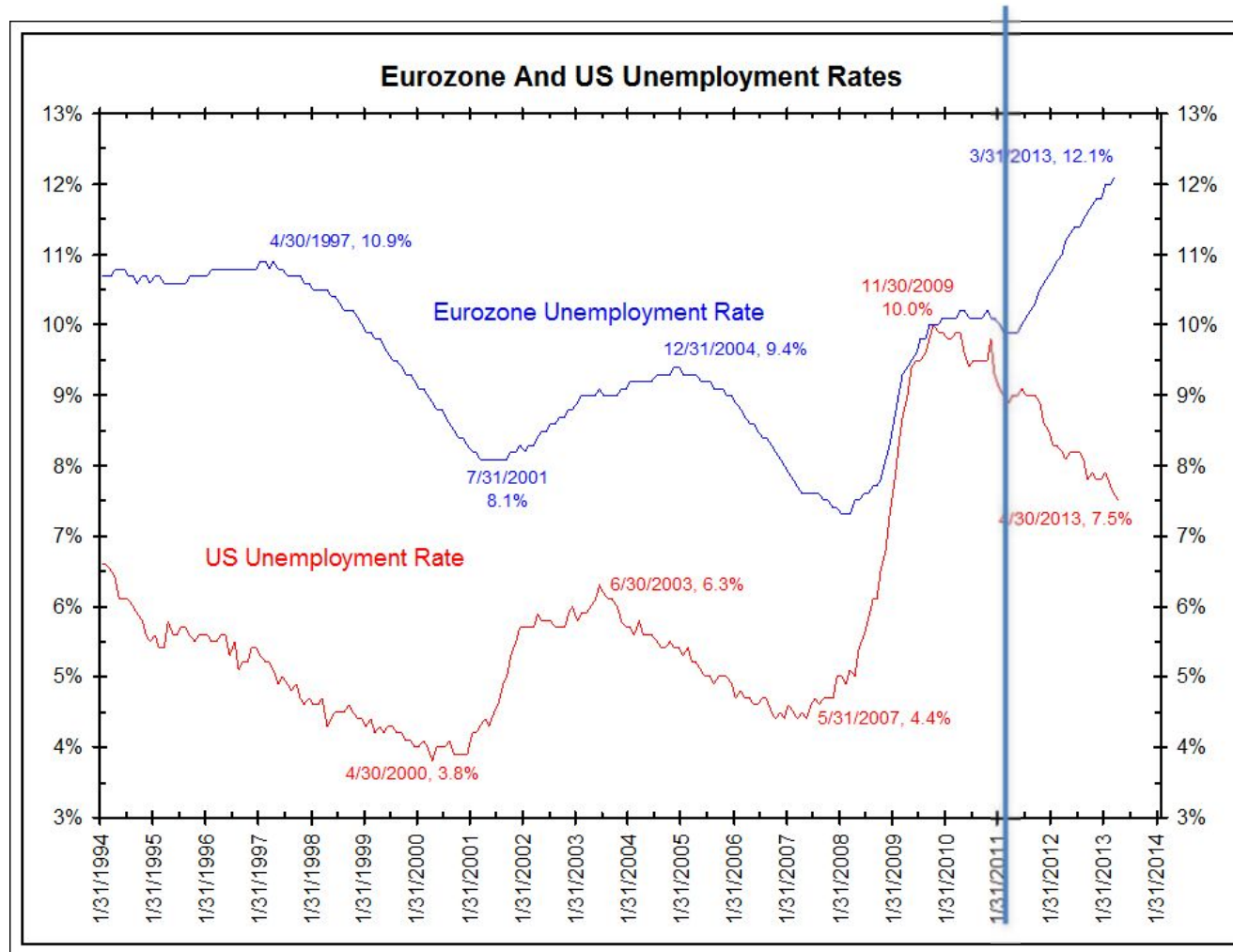
# Political risk in Spain



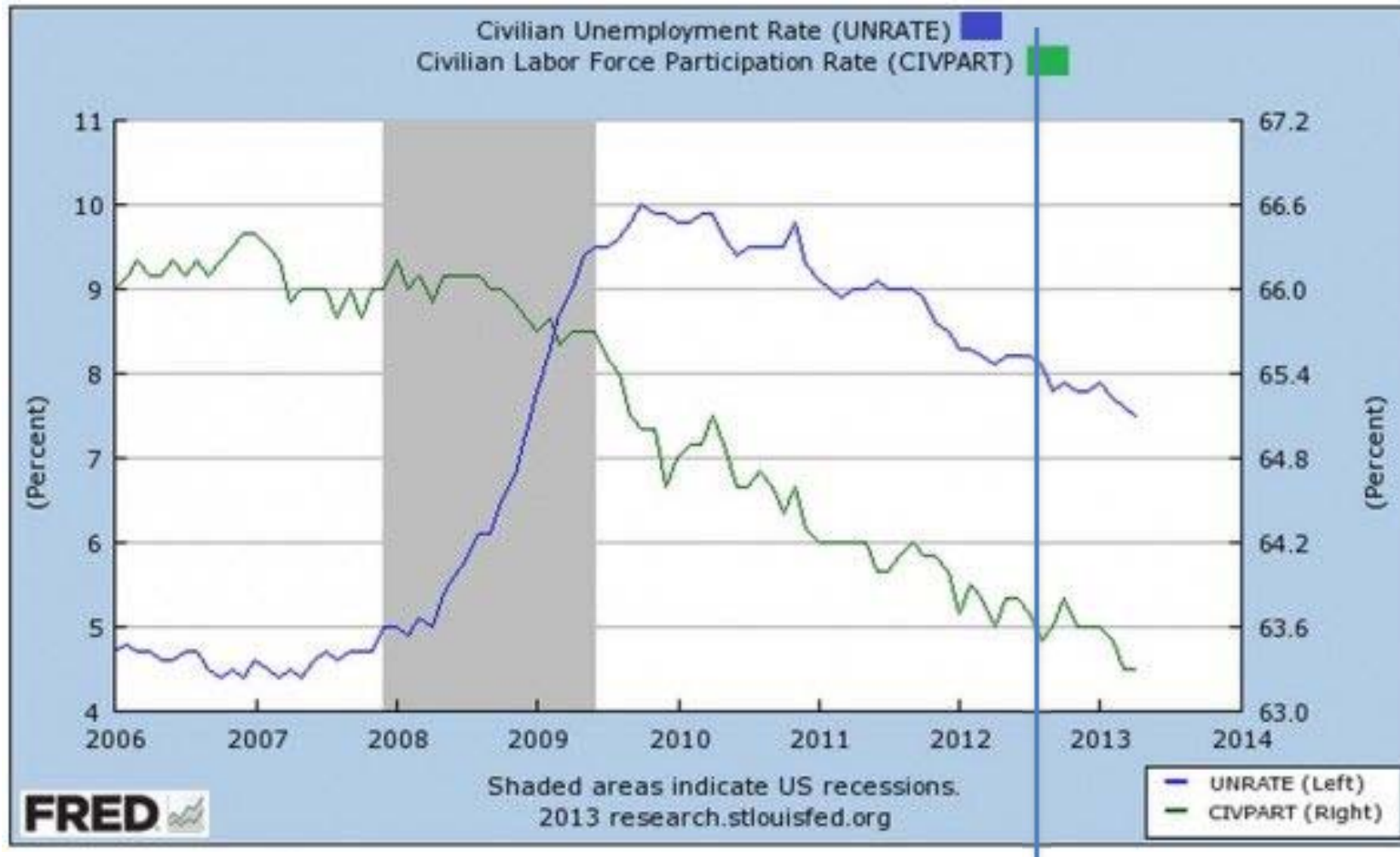
# Situation far worse for the under 25's



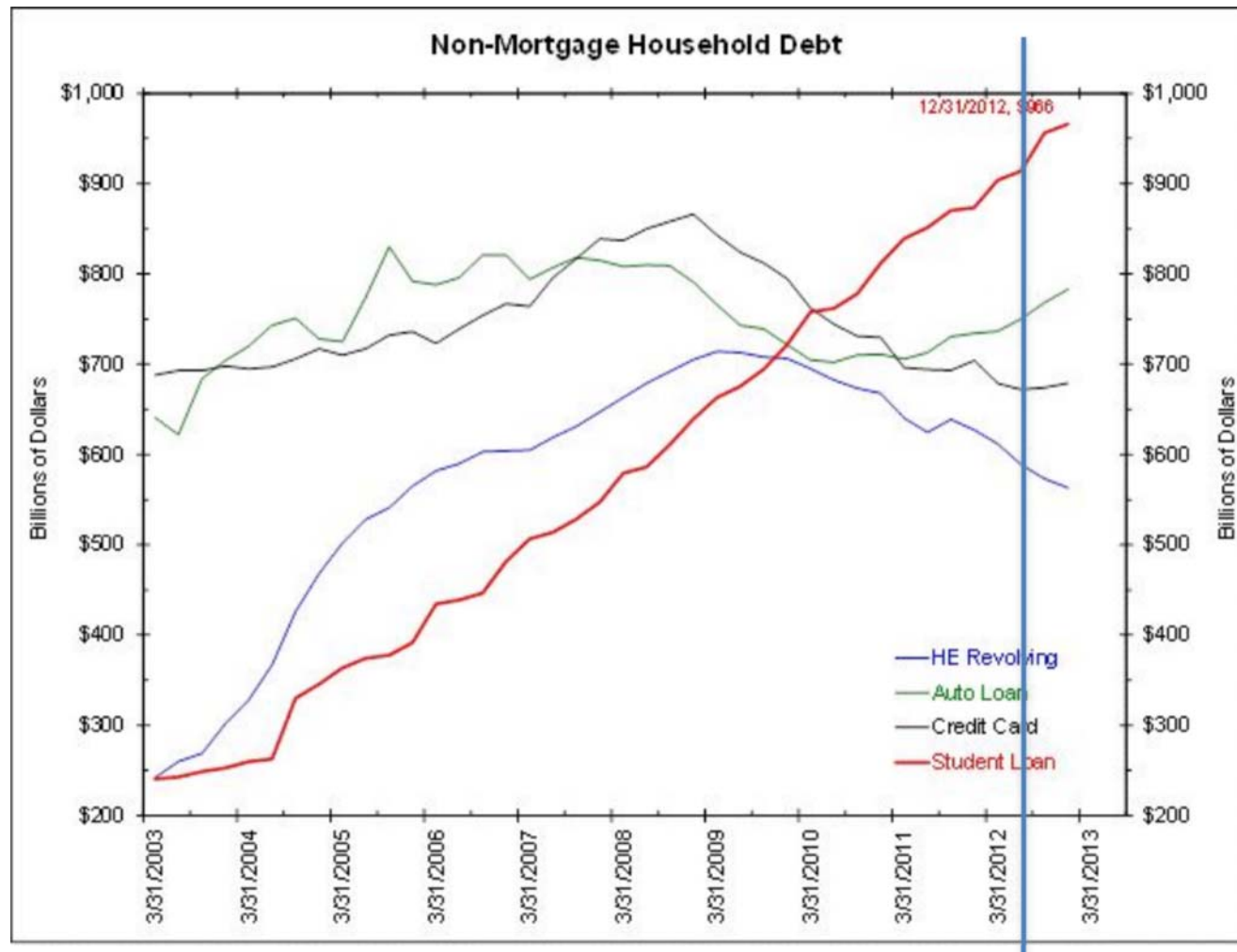
# Employment is mixed...



# US Employment...an improvement?



# In the US many are going back to school...





# Japan's experiment

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- How do you deal with a burst bubble?
  - One answer: 20 years of fiscal and monetary stimulus
  - Outcome:
    - Unsustainable levels of debt: 245% of GDP by 2013 Y/E or \$10Tn
    - Y1Qn is 21X central government revenues. A 100bps increase in yields will take a 25% slice out of government revenues.
    - Chronic deflation and little to no growth
- The Dec 2012 Abe paradigm shift
- Abe's reflationary experiment
  - Mar 2013 BoJ announced QE 10(?).
  - Target 2% inflation and job growth.
  - "Do what is necessary"
  - BoJ to buy Y140T JGBs by Y/E 2014. BoJ BS to increase from Y130Tn to Y270Tn.
    - Approx. \$70Bn of QE per month in an economy that is 28% the size of the US
    - Equiv. to a \$280Bn per month Fed program
    - This is a grand monetary experiment
    - Risks? Currency crisis? Hyperinflation?



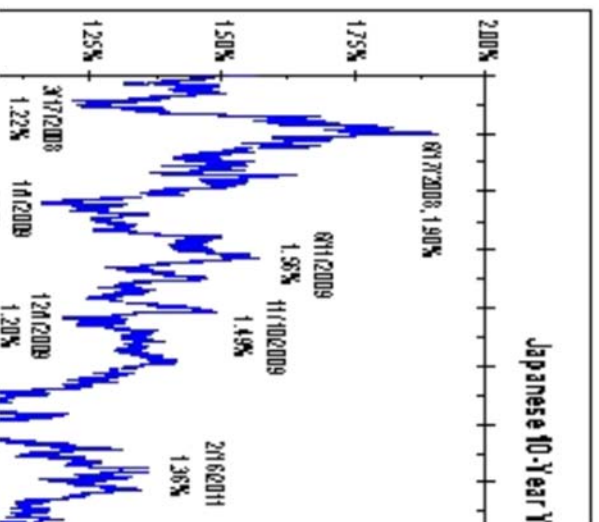
# How is the experiment doing?

## Is A Japan Crisis Coming?

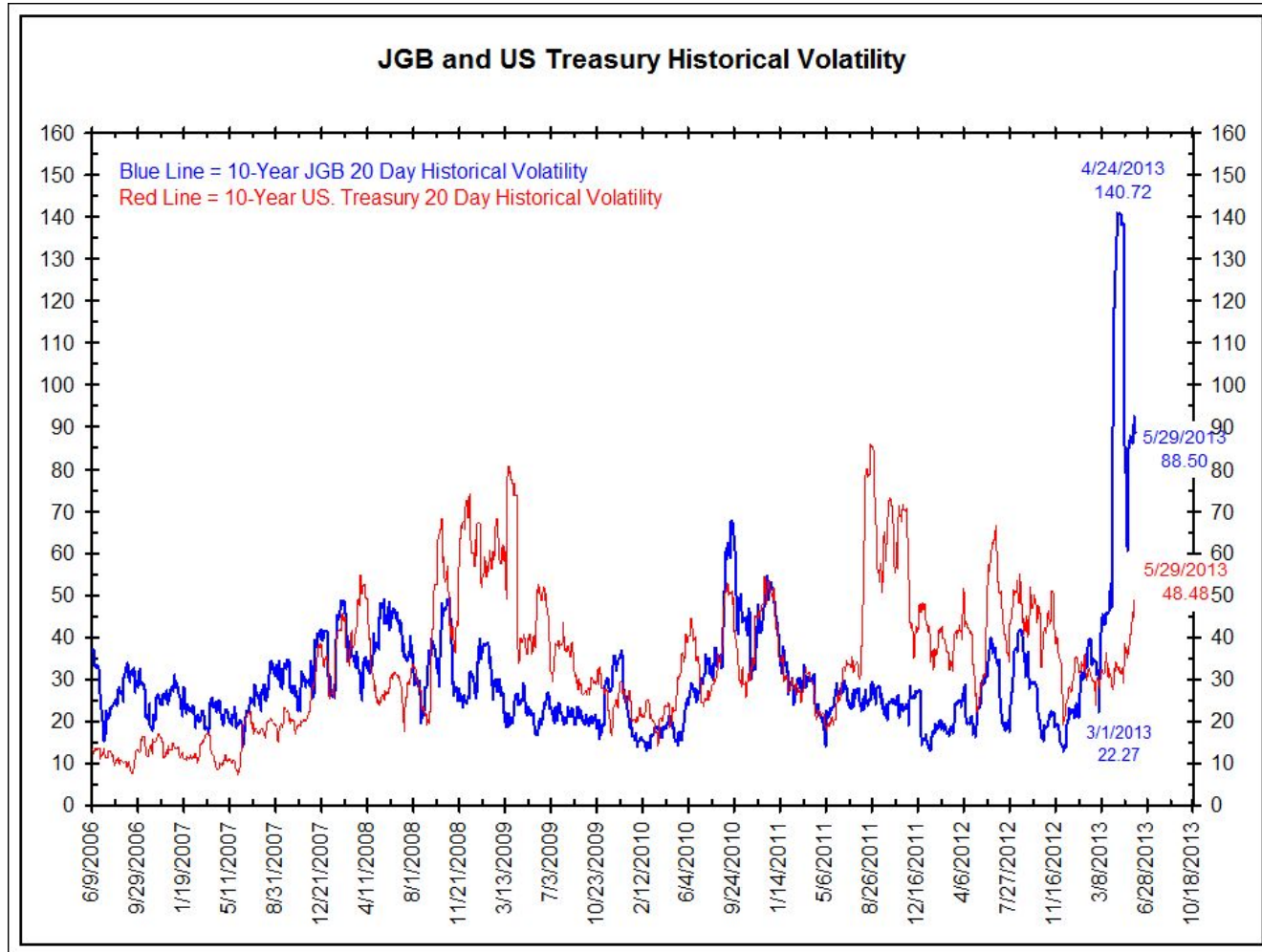
### ! Bass bets on full-blown Japan

ig, and so may everyone else, as founder of Dallas-based Hayman a full blown financial crisis in the y, Japan. While the hedge-fund o short the yen and buy Japanese port boom, Mr Bass sees in om Japan's new prime minister is that he has been predicting for

y against Japan, we believe this 2Es credibility. As we wrote last



# Bond markets are taking note...



# The importance of energy markets...

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- Easily assessable energy allows societies to organize and develop
  - Water buffalo better than human hard labor, the carthorse better still
  - Coal and the steam engine a step change
  - Oil and the internal combustion engine another step change
- Energy markets are enormously. They are critical to growth of our economies and our societies.
  - Energy costs drive costs across the economy, oil costs drive booms and busts
  - Energy drives all industrial production
- We spent a lot on energy. It is used to organize our lives
  - \$3.3T of oil consumed globally, approx. 90 mn barrels a day. That is just oil.
    - Global GDP is \$79T
    - Exxon spends \$100mn a day on oil and NG exploration. \$37bn by 2016.

# Accessible energy...

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- Accessible energy at a fraction of current costs will revolutionize industrial production
- Everything is linked to energy cost and availability
  - Cost of Transport fuels
  - Costs of mining, milling and refining base metals: copper, iron, nickel, zinc
  - Cement and steel
  - Ethylene
  - Transport and cost of shipping
- An energy revolution will result in a step change in global growth
- Without an energy revolution
  - Our debt risks being unserviceable
  - Our societies risk falling into disorder
- Are we innovating?

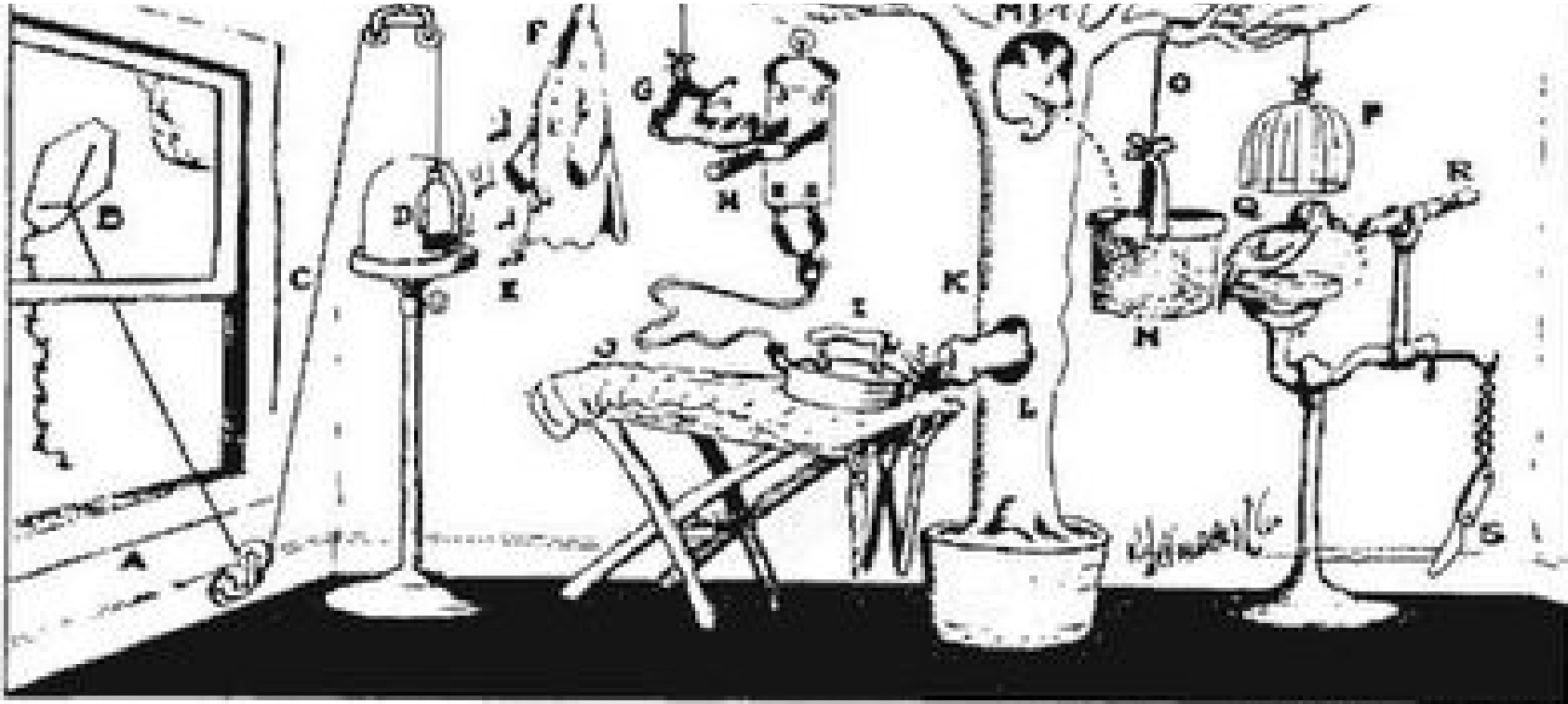
# Today's innovation...

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- Social networking
  - Tumblr. No revenues. Bought by Yahoo for \$1.1Bn
  - Facebook. At IPO 1Bn revenues, \$104Bn valuation
- Alternative Energy
  - Too expensive
  - Severely capacity constrained and not cost effective power...“filling the swimming pool with an golden teaspoon”
- Natural Gas in not accessible energy
  - GTL: Fischer-Tropsch process discovered in 1930's. Energy intensive
  - LNG: 25% of energy used to liquefy/re-liquefy. Energy intensive
- This is not energy innovation. This is energy tinkering and “tweeting” about it
- We need step change energy innovation, we need accessible energy.
- We need a new steam engine

# INNOVATE...INNOVOTE...INNOVATE

## And quickly. The debt clock is ticking...



Open window (A) and fly kite (B). String (C) lifts small door (D) allowing moths (E) to escape and eat red flannel shirt (F). As weight of shirt becomes less, shoe (G) steps on switch (H) which heats electric iron (I) and burns hole in pants (J). Smoke (K) enters hole in tree (L), smoking out opossum (M) which jumps into basket (N), pulling rope (O) and lifting cage (P), allowing woodpecker (Q) to chew wood from pencil (R), exposing lead. Emergency knife (S) is always handy in case opossum or

# Thank you

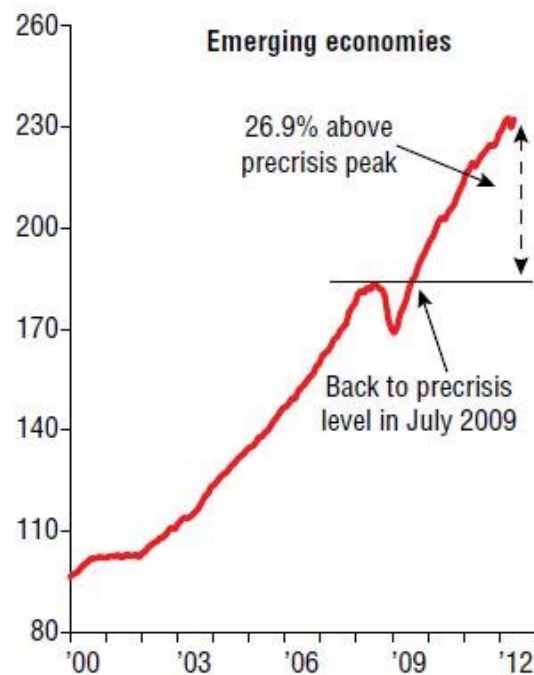
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# The weight of debt...

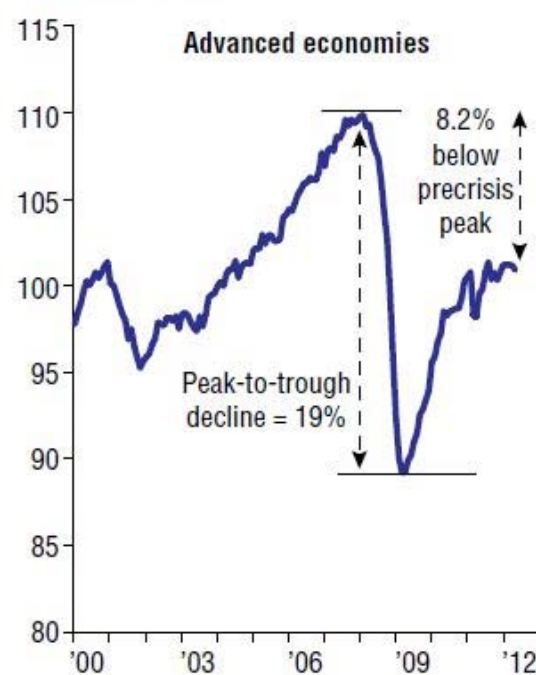
**Chart  
1**

Industrial Production Rebounds in Emerging Economies,  
Lags in Advanced Economies

Index, 2000 = 100



Index, 2000 = 100



SOURCE: Netherlands Bureau for Economic Policy Analysis/Haver Analytics.