



FINANCIAL REVIEW

Dr Doom prescribes some Asian tonic

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Marc Faber isn't about to relinquish his nickname of Dr Doom but he's in Australia this week to help launch a new Asian equity fund for the Treasury Group and has managed to find some positive "buys" for local investors, notably Asian stocks, real estate and commodities.

Indeed, never one to pull punches on investment recommendations, Faber told a group of local investors: sell your home in Australia and buy Asian equities and real estate.

His other observations for Australia included the opportunities for tourism from China and the fact that agricultural commodities are about the only prices which have not gone up in the current rises.

For share investors, his message is that asset allocation decisions should reflect the reality of the opportunities and growth in Asia, in contrast to the total 13 to 14 per cent share of total world stockmarkets at present represented by the whole of Asia (including Australia), and he is especially bullish on the Japanese stockmarket.

He certainly doesn't recommend investment in the United States market, arguing that it would be suicide to buy 30-year US treasuries, as he muses on the chances of a deflationary depression in America.

On the flip side to a likely falling US dollar, he favours investment in gold - "look for inexpensive assets" - and Australian stocks - "commodity prices won't go down".

Faber says deflation isn't necessarily bad - he cites cases in China and the US in the 19th century - but he says it becomes dangerous when combined with high debt levels, as in the US. Bad loans could explode and the US system could break down, leading to a "terrific recession".

He argues that the Federal Reserve and its incoming chairman, Ben Bernanke, have no alternative in the long run but to print US dollars and distinguished between price inflation and asset inflation.

Asset inflation is more dangerous because it has encouraged

Americans to borrow more. This is because people are now looking on increases in the asset value of their homes as a permanent state, removing the need to save.

Faber says there is "no question that the US dollar would be weaker". He argues that it is more likely that its decline would be against gold rather than other world currencies.

Because of the very low income per head in China and India (around 3per cent and 1.5per cent respectively of US income per head), he says there is no prospect that even massive revaluations of the Chinese currency could alter the trade deficit the US runs with Asia because of low Asian wages.

He argues that the pattern of rising wage levels seen in Japan from the 1960s onwards happened because Japan had a labour shortage, whereas China can rely on new sources of labour from the countryside.

Rather, he sees real estate as one of the big investment themes under the influence of large-scale urbanisation in China. In major changes in the world's economic geography, it will be important to invest in countries and sectors of the economy that enjoy comparative advantages, he says.

Faber also argues that tourism will be one of the most promising growth industries for countries outside Asia. The Chinese numbers are likely to rise from a 2004 base of 24million tourists (up from 10.5million in 2000). He says airline travel is beginning to rise in India and this will inevitably lead to people adopting the idea of a second home in resort areas as Asia develops its own Palm Beaches.

In most cases, local Asian industry is likely to benefit from the coming boom in consumption items in China and the rest of Asia. Faber notes that within a few years the average price of a car in China has come down from around \$US20,000 (\$27,000) to \$3700, which means that 20 million to 50million families (rather than a mere 1million) can now afford a car. The same trend applies to household and personal appliances.

In support of his views on commodities, he argues that China needs resources to grow, especially oil. Commodity prices will fluctuate with Chinese demand but, as they rise, so too will international tensions. "If you want to hedge, you have to be long commodities," Faber says.

In 2003, China was already ranked as the largest user of world mineral production in at least 11 major commodities. Faber forecasts that consumption per head of such commodities as oil, aluminium and copper in nations such as China, India and Vietnam will continue to rise under the influence of rapid capital spending and industrial growth.

He predicts a continued rise in demand for crude oil - this has doubled between 1986 and 2005 - and contrasts the likely doubling again with levelling world oil production.

Though crude oil prices probably overshot recently, Faber says, "the risk in oil prices is on the upside". This applies to uranium too, he says.

On the other hand, farm product prices, relative to energy prices, are at their lowest level in more than 200 years after a savage decline in relative terms since the peak in 1973.

Faber argues that commodity prices tend to move in cycles over very long periods (45 to 60 years). Producer price indices might be showing signs of bottoming after the last upturn starting around 1963.

His shorthand guide to the effect of commodity prices is that if they rise, this is negative for share prices, against the positive effect from falling commodity prices, which cause interest rates to fall and share prices to rise.

Faber is keen on the Tokyo stockmarket, noting that it appeared to bottom in April 2003. At present, he says, Asian institutions are "loaded with bonds" and much of the rise in the stockmarket has been from buying by foreign investors.

But, he says, if there is a whiff of inflation in Japan, all the money that is parked elsewhere will flow back into equities and real estate. He forecasts the recent outperformance of the Japanese stockmarket to continue for another five years or so.

Faber is an adviser to the Treasury Group's Treasury Asian Asset Management's new Asia fund and will earn his money from part of the 10 per cent performance fee on the fund's outperformance of the MSCI Asian index, ex-Japan.

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