

>: Your Guide to Making Money During Stagflation or Recession

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We're down about 150 points from the last trading day of 2007. Not the welcome into 2008 that any one of us would have liked.

So what's going on?

The biggest fear gripping the market currently is that the old 1970's bogeyman called Stagflation might make a comeback. Stagflation is a slowing of economic growth that is accompanied by increasing inflation (driven by commodity price increases). It doesn't happen very often, because inflation is usually driven by economic growth.

In this cycle, commodity prices are rising and the economy is growing. *Just not our economy!*

The developing world is experiencing stellar growth rates, along with a surge in the value of their respective currencies. So the commodity price increases that they are experiencing are mitigated by rising personal incomes, rapidly increasing economic growth rates and a declining US Dollar, which is cushioning the blow of commodity inflation. (*This is because virtually all commodities are priced in US Dollars regardless of where your home country actually is*)

Stagflation is also accompanied by higher than average unemployment. So far we haven't seen that part of the puzzle unfold. In fact, current unemployment rates (4.7%) are indicative of full employment. But you must remember that employment is a lagging indicator, not a leading indicator. If you've been keeping a close eye on the weekly job data, then you are seeing some troubling trends emerge.

Initial jobless claims on a week by week basis are too volatile to take seriously. But most pros look at them on a four week average basis. When initial claims approach 350,000 over a sustained period, that can mean trouble ahead. As of this week's reading, we are at about 345,000.

But what really rattled the Street this week was continued claims. Continued claims came in 46,000 higher, meaning people are having a tougher time finding a job. In fact, continued claims haven't been this high (2.76 million) since the labor dislocations caused by Hurricane Katrina.

Even with all of that, our unemployment rate is still very low, and wages are increasing at about a 3.6% clip. The problem, though, is that headline inflation (*that's the inflation number that includes food and energy*) is growing at a faster rate than wage growth.

So we could actually see full employment and higher wages, but still see slow or even negative economic growth in the United States!

I want you to remember that, should we go into a recession, they last on average about 10 months ... and it takes 6 months to positively identify one. The market will begin to discount the recovery almost from the moment that the economists declare that we are in a recession. So if it does happen, it's not an event that lasts for an extended period of time.

So what's the solution?

Short term, you must start diversifying away from the US economy. You've got to look at foreign stocks, foreign bonds and US companies that get the bulk of their earnings from outside of the United States. This will allow you to still make great returns should the US economy tip into recession.

Long term, recessions and economic slowdowns provide superb wealth building opportunities. During slowdowns, the financial stocks will underperform, and will offer up some extreme bargains just like they did in 1991 and the late 1970's.

Also during recessions, commercial real estate, residential real estate, private businesses, industrial equipment, manufacturing equipment, vehicles etc? become very, very cheap.

Cash is king during a recession.

One of the biggest mistakes I made as a young man in 1991 was not taking my considerable income and plowing a portion of it back into New York City real estate. From 1991 through 1994, Manhattan real estate could have been had for a song.

Don't cry for me, though, I did very well with my stocks and bonds -- but they didn't have the leverage opportunity that real estate has. When you buy real estate cheap, and as the credit cycle begins to turn and the banks start loosening credit standards again, you can leverage up your real estate holdings by 10 and sometimes even 20 to 1.

When you apply that kind of leverage to acquire more property early in the real estate recovery cycle, you put yourself in the position to make tens of millions of dollars.

Remember the golden rule: he who has the gold makes the rules.

During a recession you can hammer people on price. When buying real estate during an economic slowdown, you know you've offered the right price on a property when it's so low and so one sided (*one sided to your benefit of course*) that you are embarrassed to show the offer.

But that's how you make big money from recessions. You are looking to acquire revenue generating assets at distressed prices, PERIOD. For the long term player -- I'm talking 5-7 year time horizons -- recessions offer a truly breath taking opportunity to develop some serious wealth.



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