

“On the Edge Of A Precipice” – A Challenging Decade Is Upon Us

Description

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While a decade is just an arbitrary measure of time, people often attribute certain emotional and cultural characteristics to it, such as the “roaring 20s” of the 20th century.



The 20s of the 21st century are promising to mark a defining period in world History, particularly for the West, as vital trends that have been developing for years are expected to accelerate and reach a tipping point. “Roaring” might not be the best description by the end of it.

Consider that at the very start of the decade the UK will no longer be part of the EU, itself a monumental change with deep social, economic and geopolitical consequences. The US and other major economies will face even more profound developments this decade.

The dominant context behind all this is what British historian C. Northcote Parkinson defined in the early 1960s as the great dynamo of History – the passing of the baton of global preeminence between East and West since historical records began.

Nobody knows what will happen 6 months from now, much less a decade, but recognizing the ascendancy of the East as a whole – and the evident decline of the West – can help pinpoint important trends and cycles that are likely to materialize in the near future. That ascendancy has started decades ago and will solidify in the short years ahead.

This is a humble “back of the envelope” attempt by the author to read some through important tea leaves, colored (as a disclaimer from the outset) by his rather pessimistic view of the prospects of his native West and by his admiration of the resilience of the East:

1. The productivity of debt in most major economies is already below 1, meaning that it takes several dollars in new debt to create a dollar of GDP. This is particularly the case with government debt, and consequently in order to sustain even meager economic growth debt loads as percentage of GDP will continue to grow strongly, following Japan's path;
2. This in turn means that interest rates can never be normalized, otherwise such debt loads would become immediately unsustainable. Financial repression will thus continue, likely even be expanded. Central banks will continue to monetize debts at unprecedented levels and even take on the role of steering industrial policy, a good example being the "green economy";
3. These actions by central banks have enabled Eurozone banks over the last decade to become liquid but not necessarily solvent, a situation exacerbated by negative interest rates and the flaws of and structural imbalances generated by the Euro. A quick look at the share price of Deutsche Bank, Germany's largest bank, clearly shows this;
4. Birth rates across the West will continue to fall further given a confluence of social and economic problems. Many Eastern countries are wrestling with this problem, but the way Western elites are dealing with it are transforming its cyclical nature into a structural one, with deep generational consequences;
5. Related to that, the pension crisis will come to the forefront, with more Baby Boomers retiring (where possible) into pension plans that for the most part are underfunded, in many cases severely, despite record high asset prices;
6. Modern agriculture has been very successful in delivering calories, basically by converting copious amounts of fossil fuels into food, but rather less so in delivering nutrients. This is because it exhausts top soil and organic matter, critical to produce nutrient-dense foods. As such the health crisis will become worse as a depleted nutrition acts as a catalyst to major diseases;
7. All these factors will add more pressure for governments to take action, meaning that all those contingent liabilities will finally start materializing in budgets over the course of the decade – with a vengeance;
8. This situation is particularly serious in the US, where it is very possible that the government will lose control of its budget deficit at some point (if it hasn't already), especially given zero political will and capability to address this. One look at the Congressional Budget Office decadal projections should raise alarm, especially as no recession is expected, but no party seems to care;
9. Mass migration into the Western world will continue unabated driven by massive demographic imbalances between developed and developing countries, and Western elites seeking to maintain control by "dividing and conquering" their societies and absorbing the spoils into supranational compacts that they control;
10. Another thing which is unlikely to change is the US' foreign entanglements. Like with immigration and the budget deficit, no party has the will to do anything about it. Three dynamics make highly likely the emergence of a new, bigger conflict where the US will once again become involved this decade: (i) the military being spread all over the planet, raising the chances of some fire exchange with someone, even by accident, (ii) enormous military spending, already larger than several major countries combined, that keeps on growing, and (iii) America's enemies becoming more entrenched and determined in their quest to develop capabilities to seriously challenge its dominance (like Iran developing medium-range nukes this decade, along with others);
11. Automation, the replacement of humans with machines, will accelerate and start replacing enough jobs to generate even more income inequality between workers and capital owners, already a sensitive topic thanks to the monetary and fiscal policy imbalances of the last decade;

12. It is therefore inevitable that populism will continue to increase, both on the right and the left of the political spectrum. The hollowing out of the moderate center, tied to a neo-liberal model that is seriously sputtering, will prompt a major political and social polarization in many Western societies not seen since the 1930s;
13. The trend towards globalization will be impaired, despite the best efforts of supranational organizations like the UN to maintain the status quo. Major exporting economies like Germany will be disproportionately impacted, creating more tensions inside an already frail EU;
14. The political landscape will massively change in the US. The fragmentation of political views and aspirations already means that a two party-system is incapable of dealing with differing objectives inside their respective electorates. However, the emergence of new parties is severely limited by lack of access to funding necessary to win at the federal level, which means that democracy will suffer;
15. This loss of democracy is even more likely given the profound demographic change taking place in the US, where immigrants tend to vote overwhelmingly for the Democratic Party. As a result Texas and other states will likely swing Blue by the end of the decade, meaning that Republicans will be locked out of power for a generation+. Once again California led the way for the rest of the country, with an entrenched Democrat super-majority there. As democracy recedes, societal and ethnic conflict will gradually become mainstream;
16. What this really means is the beginning of the end for the great American experiment this decade, as its traditional institutions – including its Constitution – can no longer properly function under such conditions. This is hugely consequential for the world in terms of prosperity and freedoms;
17. One feature of diverse societies is that they are inherently unstable, meaning there's a far greater need for a government to mediate the interests and conflicts between different groups. Politicians will increasingly tighten their grip on society, aided by technology that will become even more intrusive. Silicon Valley and Washington DC will thus become even more intertwined;
18. Societal fragmentation will not be limited to the US, far from it. French President François Hollande warned in 2016 (after he left office, of course) that his country would eventually break apart. This may become a de facto reality in the 2020s as multiple societal, demographic and economic factors converge in French society. In fact the new decade was inaugurated with dozens of cars set on fire in Paris. These factors will also impact other European countries in similar ways, including Sweden, Belgium, even Germany;
19. The EU will become increasingly authoritarian to prevent more BREXITs and keep that political project going. Any dissent of its main guiding policies, from the environment to immigration, is already being stamped out under the guise of "hate speech". It will only get worse from here. A draconian social credit system similar to what China is developing might be in place by the end of the decade. It seems inevitable that the political make-up of the EU and several of its members will be radically different by the end of the decade compared to today;
20. BREXIT might have been a fantastic idea given all that is happening in the EU, but the timing will prove to be off. First, we are close to a global recession, which absent very vigorous central bank action might become serious, thus curtailing any initial enthusiasm. Second, Boris Johnson will be pursuing free trade deals when the globalization tide is turning against him. Third, because in order to ensure the City of London's preeminent access to global capital markets he will have to offer a bargaining chip, and that is what's left of British industry – meaning the working class seats the Conservatives were able to impressively flip from Labour on the back of BREXIT. Perhaps the UK as well might not escape the coming fragmentation;

21. Working and middle classes across the West, including the UK and especially the US (if one looks objectively at the results of three years of “America First” policies under Donald Trump), will finally realize that they have no real political representation. The real political fault line is not between right and left, rich and poor, liberal and conservative, but rather globalism versus nationalism. There is no money in the latter, beyond extracting taxes to pay for that burgeoning government (that will inevitably oppress them) and elite pet projects, like solving “climate change” and the “migrant crisis”;
22. The West thrived when its working and middle classes thrived. These are the people who consume, who largely maintain the national traditions, who fight their wars. Financially and demographically they are in a very tough spot, with birth rates far below replacement levels and life expectancy plunging due to drugs and health problems. Half of Americans can’t cut a \$400 check for an emergency. As things stand this rot will likely accelerate as the decade progresses;
23. All this does not mean that it will be smooth sailing for the East, far from it, as those economies still depend a great deal on Western markets. Still, they have a highly motivated, educated and productive workforce, comparatively low debt levels (ex-Japan), high savings and very little contingent liabilities. They are also very safe to live in. Attracting top talent from the US and Europe, in addition to their own, should not be too difficult, further cementing their competitiveness. In a sense these economies are merely reverting to the global place they used to occupy before that baton swung to the West;
24. Russia is an interesting case as it was always between East and West, given its vast cultural, ethnic and geographical components. Thanks to incredible short-sightedness and (frankly speaking) stupidity from the NeoCons in Washington DC it will now embrace its Eastern future. The 2020s will consolidate the emergence of Eurasia as a super economic block towards the end of the century, independent from any US interference;
25. That sets up different scenarios for the coming fracturing of the EU by mid-century, if not sooner. Eastern European countries should gradually gravitate towards Eurasia, including Germany – the worst case scenario for US hegemony. The center West of Europe will become more culturally and demographically aligned with Africa, and so might pursue its future there. And Portugal and Spain, if they had any sense, should seek close ties with their cultural peers in Latin America and Africa;
26. Africa could be the one bright spot in the middle of all the turmoil elsewhere, especially given that it has a lot of development potential and a vast supply of all sorts of natural resources. China (i.e. the East) is spending vast sums to unlock this potential and is now the continent’s largest trading partner. Unfortunately, the constraints holding Africa back are all too familiar: corruption, loss of their most enterprising people to mass migration, weak institutions incapable of addressing the aspirations of its very young populations and increasing social and ethnic conflicts, exacerbated by a resurgence of political Islam – another quintessential Eastern ideology that gains force whenever the West declines. This decade will indicate which way it will eventually go the rest of the century;
27. Energy prices should remain very volatile, as demand is pressured by a weakening of the economic cycle and supply by a coming peak in US crude oil production this decade. The explosive situation across the Middle East, from Libya to Pakistan, will add much greater uncertainty as the decade unfolds. The West faced serious oil shocks in the 1970s as the US could no longer ramp up its production to counter supply embargoes from the Middle East; it is vulnerable to a repeat of that by the end of the decade. Sustained crude oil price rallies above \$100/bbl would very likely put a nail in the coffin of the financial house of cards concocted by

Western central banks;

28. Commodities markets in general should perform better on a relative basis this decade, especially when compared to US stock markets, which have been on an absolute tear since the end of the financial crisis in 2009. The longest bull market in the context of the weakest capital expenditures cycle since WW2 suggests that significant productive capacity might be taken offline at some point this decade. Mean reversion is a real thing in capital markets;
29. Aging farming populations worldwide, quite severe in some cases, will finally put significant pressure on food supplies by mid-decade, if not sooner. And the young, so far, are not replacing them. As a result, record food supplies globally at the start of the decade may turn into food deficits by the end, especially given strong population growth projections (including in the West via mass migration);
30. And the US dollar? Its cycles typically last around a decade, and if that is the case we might be nearing the end of its bull run, certainly this decade. Adding to this cyclical outlook is the fundamental deterioration of the US fiscal position outlined above. That deficit will have to be financed somehow, and some pretty juicy yields might have to be offered especially if the dollar starts weakening. While it may still remain the world's reserve currency given lack of competitors, cryptocurrencies might increasingly offer an alternative. StableCoins, a variant, in particular offer governments a monetary alternative to generate growth within the constraints of the Euro, for instance;
31. Gold should remain part of any investor's portfolio (in physical form), although nobody can say for sure whether prices will be higher in dollar terms by the end of the decade. Trillions of dollars in debt issued in the last decade will become due and together with weak economic growth the risk of a deflationary shock remains significant;
32. The wildcard in predicting financial outcomes is as Western societies profoundly change so will the rules of the investment game. It's not inconceivable that capital controls will be in place before the end of the decade. The more Europe and the US sink into deep fiscal and economic issues, the bigger that wildcard will be;
33. Investors' focus will gradually shift from speculation to wealth preservation, given the dearth of fairly valued opportunities at the start of the decade and a far more uncertain global environment.

Summing up, **this decade will very likely be remembered for the end of the world order that had been in place since WW2.**

Yes, there is a positive drift on societies across the world emanating from relentless technological progress, but it is highly unlikely that this will do anything to stop the profound demographic, financial and cultural changes that have accelerated this past decade.

Adam Smith noted that a nation can take a lot of ruin. For decades Westerners have been doing their best to figure out how much. Not only that, but a progressive cultural revolution starting in the 1960s has upended all Western traditional values and morals, and so the present generations are ill-prepared to cope with the massive challenges that lie ahead.

If there is a silver lining in all this is that young people are starting to acknowledge the failure and dead-end of the current economic, moral and governance models, and are gradually returning to tradition, family life and communities. Localism, as opposed to globalism, will gain traction.

Building resilience should be the motto of the coming decade.

And with that, wish you a very hopeful, positive and healthy 2020.