

Société Générale tells clients how to prepare for 'global collapse'

Société Générale has advised clients to be ready for a possible "global economic collapse" over the next two years, mapping a strategy of defensive investments to avoid wealth destruction.

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Explosion of debt: Japan's public debt could reach as much as 270pc of GDP in the next two years. A bullet train is pictured speeding past Mount Fuji in Fuji city, west of Tokyo Photo: Reuters

In a report entitled "Worst-case debt scenario", the bank's asset team said state rescue packages over the last year have merely transferred private liabilities onto sagging sovereign shoulders, creating a fresh set of problems.

Overall **debt is still far too high in almost all rich economies** as a share of GDP (350pc in the US), whether public or private. It must be reduced by the hard slog of "deleveraging", for years.

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"As yet, nobody can say with any certainty whether we have in fact escaped the prospect of a global economic collapse," said the 68-page report, headed by asset chief Daniel Fermon. It is an exploration of the dangers, not a forecast.

Under the French bank's "Bear Case" scenario, the dollar would slide further and global equities would retest the March lows. Property prices would tumble again. Oil would fall back to \$50 in 2010.

Governments have already shot their fiscal bolts. Even without fresh spending, public debt would explode within two years to 105pc of GDP in the UK, 125pc in the US and the eurozone, and 270pc in Japan. Worldwide state debt would reach \$45 trillion, up two-and-a-half times in a decade.

(UK figures look low because debt started from a low base. Mr Ferman said the UK would converge with Europe at 130pc of GDP by 2015 under the bear case).

The underlying debt burden is greater than it was after the Second World War, when nominal levels looked similar. Ageing populations will make it harder to erode debt through growth. "High public debt looks entirely unsustainable in the long run. We have almost reached a point of no return for government debt," it said.

Inflating debt away might be seen by some governments as a lesser of evils.

If so, gold would go "up, and up, and up" as the only safe haven from fiat paper money. Private debt is also crippling. Even if the US savings rate stabilises at 7pc, and all of it is used to pay down debt, it will still take nine years for households to reduce debt/income ratios to the safe levels of the 1980s.

The bank said the current crisis displays "compelling similarities" with Japan during its Lost Decade (or two), with a big difference: Japan was able to stay afloat by exporting into a robust global economy and by letting the yen fall. It is not possible for half the world to pursue this strategy at the same time.

SocGen advises bears to sell the dollar and to "short" cyclical equities such as technology, auto, and travel to avoid being caught in the "inherent deflationary spiral". Emerging markets would not be spared. Paradoxically, they are more leveraged to the US growth than Wall Street itself. Farm commodities would hold up well, led by sugar.

Mr Fermon said junk bonds would lose 31pc of their value in 2010 alone. However, sovereign bonds would "generate turbo-charged returns" mimicking the secular slide in yields seen in Japan as the slump ground on. At one point Japan's 10-year yield dropped to 0.40pc. The Fed would hold down yields by purchasing more bonds. The European Central Bank would do less, for political reasons.

SocGen's case for buying sovereign bonds is controversial. A number of funds doubt whether the Japan scenario will be repeated, not least because Tokyo itself may be on the cusp of a debt compound crisis.

Mr Fermon said his report had electrified clients on both sides of the Atlantic. "Everybody wants to know what the impact will be. A lot of hedge funds and bankers are worried," he said.

<http://www.telegraph.co.uk/finance/economics/6599281/Societe-Generale-tells-clients-how-to-prepare-for-global-collapse.html>