IceCap
Asset Management Ltd.

Our view on global investment markets:

June 2017 – "The Beautician"

Keith Dicker, CFA
President & Chief Investment Officer
keithdicker@IceCapAssetManagement.com
www.IceCapAssetManagement.com
Twitter: @IceCapGlobal
Tel: 902-492-8495

Eye of the Beholder

In 1888, Martha Matilda Harper became the world's first professional beautician. In addition to inventing the first reclining shampoo chair, Ms. Harper became famous for opening the first ever, stand alone beauty salon.

Next up to dominate the industry was Elizabeth Arden. Her success was founded upon expanding the salon concept to 1000s of stores around the world, and for the distribution of her self made products, most notably lipstick.

Today's top beautician is breaking the mold. His product and distribution are light years ahead of anything dreamed of by both Harper and Arden, and best of all he truly believes if he applies just the right amount of foundation, concealer and lipstick (especially lipstick), then he can make anything beautiful and attractive.

Up to this point, his business has been a self-declared, resounding success. His salon is in Frankfurt, Germany. His company has gathered over $5 billion in assets, and his clients total over 340 million people.

Yet recently, more and more people are realising that all isn't as beautiful as meant to be. Cracks are building in the foundation, mascaras are running long, and worst of all, the lipstick has been smeared.

Mario Draghi's days as both Beautician and President of the European Central Bank are starting to show their wear. While the headline news celebrates the outcome of France's election, Europe's governments and banks remain burdened in a financial struggle that even the very best lipstick cannot hide.

Two things are for certain.

One, underneath all the financial make-up applied by Mario Draghi remains a fractured, unworkable Eurozone system.

Two, the majority of investors around the world are not prepared to see what is truly behind Draghi's scheme to delay the inevitable.

Canada Top of the World

This Toronto icon rises above the clouds; it rises above its west coast rival , and is also towers above any of its rival's south of the border.

Yes, the CN Tower dwarfs its competition and 40 years after completion it continues to rank amongst the tallest in the world.

Yet within its own city, the CN Tower has taken a back seat to another towering, momentum building mass – *the housing market*.

Whereas many housing markets were stopped cold turkey in 2008, Torontonians merely paused for a refreshment, and then quickly jumped on the back of the world's zero and negative interest rate experiment and marched higher.

Naturally, for all investments, perspective is everything.

It looks great from up here!

Unfortunately, perspective is formed on the basis of subjectivity. And to demonstrate just how poor perception can alter reality, consider recent conversations we had with other managers around the world:

New York – Head of a Derivatives Trade Desk had no idea that interest rates in Germany were negative – "truthfully, we only monitor the US market."

Chicago – Senior Bond Manager – "we only watch the FED, really, everyone else doesn't matter."

Toronto – Bank Economist – "housing is the only thing anyone is talking about and asking about these days."

To put this another way, and once you grasp this all-important piece of knowledge, you'll better appreciate all the gibberish spouting from the big-bank-lead talking heads – there are very few, true global investment managers in the world.

In fact, we estimate over 90% of investment managers always see the world from the eyes of their own country, and are either unwilling, unable or simply restricted from seeing the world from any other lens.

What's in Toronto now is undeniably, both fun and terrifying to watch.

The fun part is seeing what so many others will not. The terrifying part is understanding what happens when the housing market bubble breaks.

And just to remind everyone, understand that all bubbles pop – it's science, it's inevitable, and the point that breaks it will completely surprise the majority of those who are expecting it to pop.

For starters, ask anyone in Toronto if they believe there is a bubble and their answer depends whether they are a home owner or not.

Those who own a home, will claim prices may have gotten a bit out of whack, but things will stay flat for a while at worst.

Meanwhile, those who do not own a home claim prices are indeed bubblicious and once the bubble splatters, they'll be there to scoop up condos faster than Roberto Alomar scooping up double plays.

For those who are not familiar with the Toronto market, or its baseball stars from yesteryear, just know that the clock that keeps Toronto ticking is the good ole' financial industry.

Just as the Calgary market crashed when oil crashed, and the Tokyo market crashed when the Yen crashed, anyone who is forecasting the safety or the demise of the Toronto market must completely understand the main driver of the global financial industry.

Which is of course – long term interest rates.

And once you've figured this out – your vantage point will be even better than from atop the mighty CN Tower.

Darwinism

Chart 1 next page, details the evolution of the global financial system since the 2008-09 credit crisis.

The good news is that after 7 years of financial oppression, those who have not benefitted from extreme monetary stimulus, the playing field will once again be level for all players.

The bad news is that after 7 years of financial oppression, those who cannot recognise the risks that have accumulated, are about to be red carded right off the field.

Let us explain.

For a number of reasons, the vast majority of investors around the world solely look at the stock market. Everything good and everything bad always comes from and away from the stock market.

In truth – the grease that keeps the world's mighty economy and debt eating machine chomping through the night is ladened with interest rates.

Yet, few are able to see, speak or even dream about interest rates. The big banks are especially unable to articulate their importance.

Instead, their compliance-approved, snooze-worthy market commentaries occasionally dare to mention everyone's favourite financial axiom – *valuation*. And even then, the trained eye can see the rather lack of conviction in the use of the word.

To better grasp the vital importance of this discussion, just know that long-term interest rates are to the bond market as oil prices are to the energy market.

From 2003 to 2008, oil prices shot to the moon dragging along every investment with even the slightest positive linkage.

The same also occurred in 2014 – but with a negative reaction when oil prices crashed from $100 to $50.

Yes, prior to the most recent devastating oil correction, people couldn't get enough real estate in Alberta and Texas. And they couldn't get enough energy stocks and their high paying dividends.

In both cases, the perceived risk was non-existent. Oil prices would only go in one direction – up, and that was the end of story.

Well, we all know now that it wasn't the end of the story. In fact, it was only the beginning of another story, one in which turned into a nightmare for all of those riding the great oil express.

Today, the exact same story is playing out.

Instead of it occurring in the oil patch and affecting a smaller segment of the investment universe, the story today is occurring in a field that covers the world from east to west, north to south and every nook and cranny in between.

This field of course, is the interest rate field and the entire bond structure used by investors everywhere.

Chart 1: developments since 2008-09 Crisis

2008 → 2017

Solution to last crisis
- $14 TRILLION QE
- 700+ rate cuts
- 0% NIRP
- NEGATIVE% ZIRP

Created Distortions
- Created artificial global yield curve
- all interest rates suppressed lower
- Cheap credit for Borrowers
- Low/No income for Savers

Unexpected Results
- declining M2
- sluggish growth
- Rising inequalities
- growing anti-establishment politics
- Deteriorating deficits
- Rising debts

Unwanted Consequences
- Brexit
- Trump
- Le Pen
- 5 Star
- Italian banks
- Migrant crisis
- All Lives Matter
- Russia/China/NK

Cracks Appearing
- 30-Yr Bond
- Great West Life
- BMO MBS
- Home Cap
- Moody's
- Westpac
- Italian Banks

Crises Strikes
- European banks
- European sovereign debt
- Emerging market debt
- Surging USD

Source: IceCap Asset Management Limited

As easy as 1-2-3

Returning to Toronto – understand that when the long-term interest rate bubble pops, two things happen:

1) bond investments lose a lot of money
2) piles of jobs are lost from the many companies dependent upon interest rates which so happens to include practically every bank, insurance and financing company.

So, from a pure fundamental, aggregate income and valuation perspective; the breaking of the bond market will have a serous downward impact on salaries, bonuses and perks in Toronto. That alone creates heavy pressure on house prices.

But, the other simultaneous whammy is the surge in mortgage rates which makes the amount qualified to borrow to decline as well.

In other words, there will be less money available to buy houses and the money that is available, will not be able to borrow as much as it could before.

The result: prices go down, way down.

Understanding why this is about to occur is really the key to happiness.

The happiness occurs as there are several ways to prosper significantly once the crisis begins.

The process of why it will occur is explained in 3-easy steps.

Step 1:

The foundation of the current bubble in the Toronto housing market (and the bubble in bond markets) was firmly established in 2008-09.

Recall, that was the year the Americans and their Wall Street financial assassins created deathly lending products which eventually went boom in the middle of the night.

It was the response to this boom that sowed the seeds for the next crisis, which just so happens to be manifesting itself today in Toronto's housing market, and even more concerning – in the world's bond market.

The **chart next page**, shows collectively, central banks of USA, Japan, Eurozone, and Britain created over $14 trillion out of thin air.

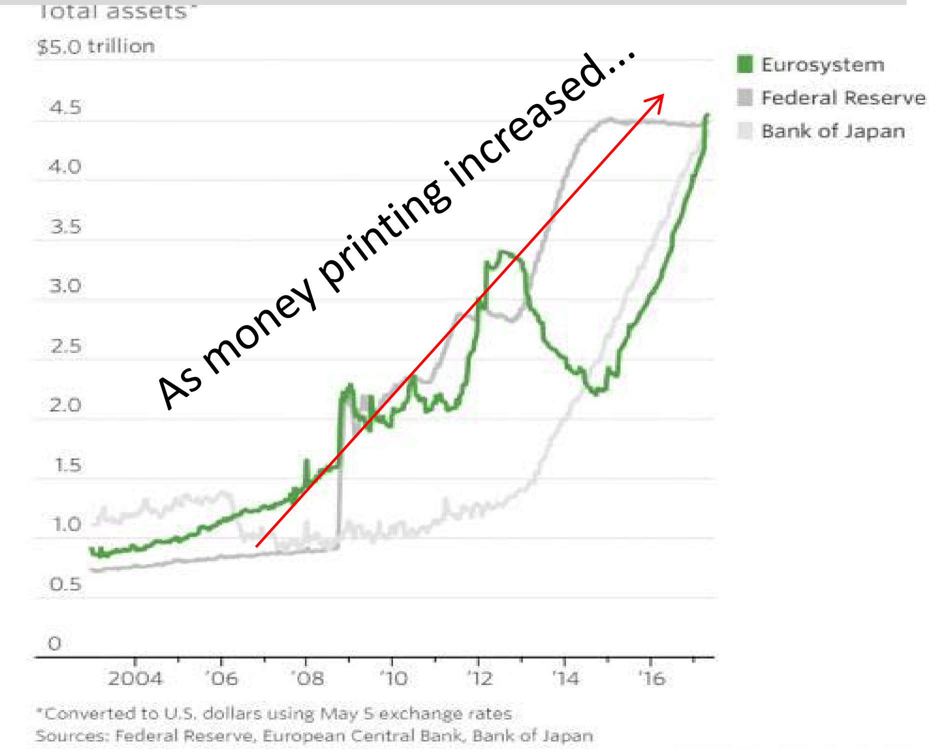
Top government economists swore printing money would stimulate the economy, creating new jobs, raising taxable income which would pay down debt everywhere.

But, instead of actually printing money and mailing a cheque to everyday average people to actually spend, economists decided to make an easy stimulus plan a complicated stimulus plan.

It became complicated when the money was instead use to buy government bonds. The thought was that by buying government bonds, interest rates everywhere would decline which would benefit everyone.

Mega-Stimulus

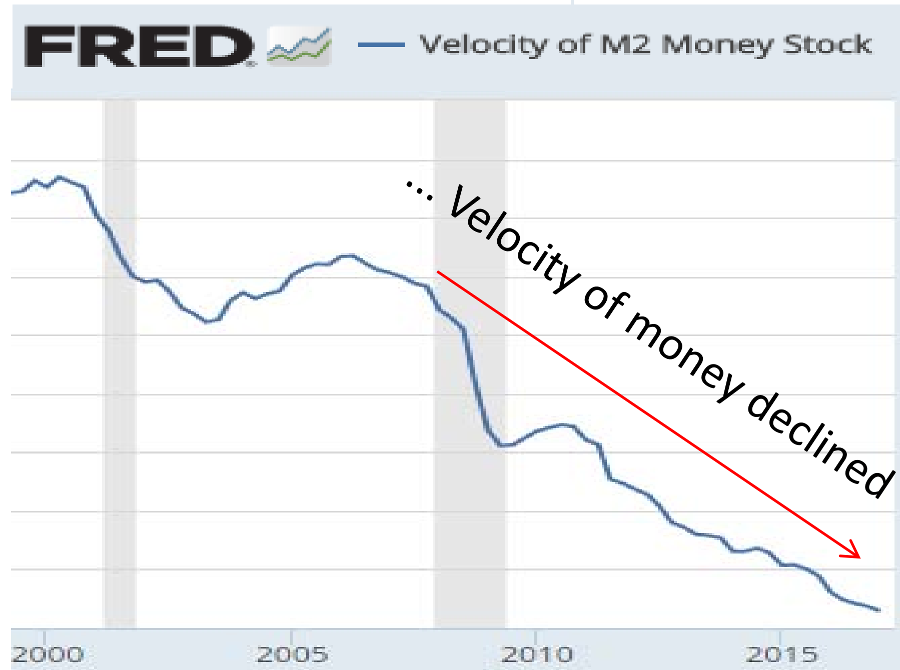
Step 1: >$14 TRILLION QE



In effect, this entire money printing or Quantitative Easing (QE) experiment was really one arm of the government lending to the other arm of government.

The intentions were good – after all, the thought was that this $14 trillion would be swished around the global economy faster than the speed of light.

Instead, it actually had the opposite reaction as seen in Chart below that shows the Velocity of Money actually declining.



Now, just in case this $14 trillion wasn't enough to heal the wounds, all of the world's central banks agreed to add an extra layer of stimulus.

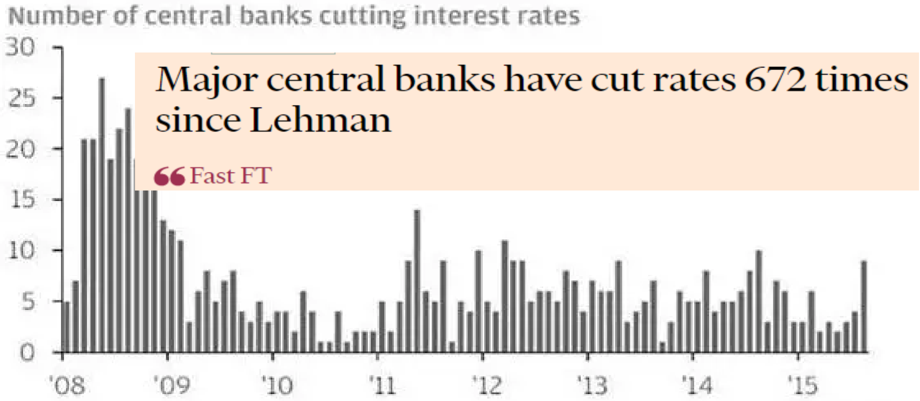
Which brings us to Step 2.

Just in case…

Step 2:

Simultaneous to printing $14 Trillion, government economists also announced they would cut interest rates to the bone. And when we say bone – we mean 672 interest rate cuts over 7 years.

Step 2: 672 interest rate cuts



Source: Bloomberg, J.P. Morgan Asset Management; data as of 25 March 2016.

The thought was that 672 interest rate cuts would stimulate the global economy by making money super cheap to borrow, which would creates jobs and create more tax revenues for governments.

But central banks still weren't done.

Just to ensure their plan would work the ultimate cherry on top was added in the form of NEGATIVE INTEREST RATES.

Step 3

Just in case the $14 trillion of new money + 672 interest rate cuts were not enough, 5 of the world's central banks played the sneakiest card of them all by creating NEGATIVE interest rates across Europe and Japan.

Central banks with negative interest rates

Whereas the thought that $14 trillion of money printing and 672 interest rate cuts would encourage people to borrow and spend, the thought was that the use of NEGATIVE interest rates would force people to spend.

Either way – savings and savers would really going to struggle.

In the end, the combination of steps 1 + 2 + 3 didn't provide nearly the amount of global stimulus as thought.

The Bottom Line

Instead, it lowered short term, medium term, and long term interest rates to never before seen levels, merely encouraging borrowing from 2 groups of investors:

1) Home buyers
2) Governments

Which of course squares the peg as follows:

$14 Trillion money printing
\+ 672 interest rate cuts
\+ Negative interest rates

= record low interest & mortgage rates

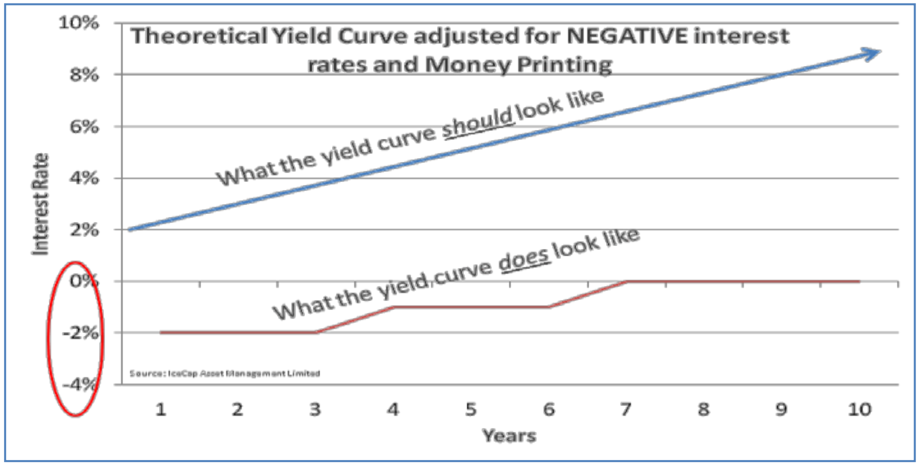
What investors must realize and understand today is that interest rates are the key cog in the global money wheel.

And over the past 7 years, this wheel has been flattened, pushed around and outright forced to look, feel and behave in a certain way.

However, where this becomes the most important foresight to hear – interest rates (and especially long-term interest rates) cannot remain in its current, forced/coerced/manipulated state forever.

Eventually it will change. The change will be abrupt. And it will definitely be the shock that breaks the housing market in Toronto and it will certainly be the shock that forces the Eurozone to restructure.

Here we show you how interest rates should look in a normal market compared to how they currently look in Europe.



The question that should be on everyone's mind – especially those in Toronto waxing on about demand for housing vs supply of housing, <u>what happens to mortgage rates when the RED line returns upward to a normal functioning market environment?</u>

Recall: The RED line has been created by STEPS 1,2,3. It has kept interest rates artificially low now for 7 years making it possible for the Toronto (and let's not forget Sydney, Australia too for that matter) market to catapult higher, as well as all of southern European governments and banks to continue humming along as if all is normal.

Next, we'll show you why interest rate markets are about to soon hum a different tune.

Going Deep

The Majority are always wrong

IceCap is a global macro manager, and like other global macro managers, we see the risks and imbalances in the world today have very clearly been created by governments and their central banks.

We know this. Governments know this. And the central banks especially know this.

Yet, just about everyone else <u>doesn't</u> know this.

And since the risks and imbalances created have reached astronomical levels, it has become very important to the central banks to ensure those that don't know what is happening remain in the dark and are unable to see these risks and imbalances.

This is where all kinds of make-up, mascara and lipstick is needed to make everything look pretty and beautiful.

And when it comes to lipstick, no one in the financial world is better at applying it than the President of the European Central Bank.

And, no one is better at wearing it than **Italy**.

Let us explain.

Chart 2 next page shows the interest rate Italy had to pay to borrow money for 10 years.

Everyone ought to know that the less you pay in interest the better – it means you can borrow more, your interest payments take up less of your income, and more importantly, it means lenders view you in a favourable light.

When lenders do not view you in a favourable light – bad things happen, with the worst being no one will lend you any money at all.

When this happens, you are shut out of the loan market.

And when you are a government and sovereign state, you cannot ever be shut out of the lending market. Once this happens – it is game over and out.

As a country, being unable to borrow, means you are unable to pay policemen, the military, nurses, doctors, teachers, and garbage collectors.

You are also unable to pensioners, engineers, social workers, and snow plough operators.

And of equal importance, you are unable to repay old debt that is coming due.

In other words – you're in deep doo.

And, this is exactly what happened to Italy in 2011.

Chart 2: Italian Government 10 Yr Bond Yield

Oct 2010 to Nov 2011, Italian long-term interest rates spiked from 3.8% to 7.1%

Source: OECD

Normal is good

Now, if Italy wasn't connected to a larger currency and monetary union, it would have been left to the wolves.

Italy would have defaulted on its debt. Doctors, nurses, teachers and pensioners would not have been paid. Its currency would have dropped by over 50% and then the IMF would be heard knocking on the door.

This is normal. This is what happens when you cannot pay your bills.

But – Italy doesn't exist in the normal world of finance. And because there are other "Italy's" in Europe, the word "normal" hasn't existed in the financial world for over 8 years.

For those of you who do not live in Italy, take no solace. What is happening in Italy and the rest of Europe is soon coming to a conclusion. And when it does, Italy and others will have no choice but to return to the normal world of global finance – which means there will be bills to pay, but no money to pay them.

The real question, real people ask is "why?"

Why has Mario Draghi worked so hard applying lipstick to an obvious financial pig, when it should simply let nature take its course?

The answer – removing the make-up, will spell the end of the Eurozone. And, there are Trillions of dollars at stake and thousands of government jobs at stake, and a tonne of pride at stake.

Unfortunately, the stakes are starting to pop out of the ground and all the lipstick and guy lines won't be enough to prevent normalcy from returning.

Returning to **Chart 2** (previous page), note how from 2010 to 2011 Italy had to increasingly pay more and more interest every time it borrowed.

In fact, in a little over 1 year, Italy's interest rate paid to borrow for 10 years increased from +3.8% to +7.1%.

That would be the same as your mortgage rate doubling in less than a year.

Of course, by the time Italy's rate reached +7.1% it was stopped out of the world's bond market. No one in the entire world was willing to lend any money to Italy.

As a reminder, headlines from those frightful days included:

> Analysts say Italy's 1.8 trillion euro public debt -- the third-largest in the world -- would overwhelm the euro zone's current financial defences if the country had to ask for help like its smaller EU partners did.

> Italy is probably already in recession, ratings agency Fitch said on Thursday, adding that it would cut the country's credit rating further if Europe's third largest economy was shut out of the debt markets.

Germany wins

Silvio Berlusconi was the Italian Prime Minister at the time.

Make no mistake, Berlusconi's past was checkered resulting in him being despised by millions of Italians and even more in Brussels and Germany.

As a result, he faced stress and pressure from not only all of Italy, but also from the Troika - aka the European Union (EU), the International Monetary Fund (IMF), and the European Central Bank (ECB).

To put it mildly, stakes in the Italian crisis were astronomically high.

If a solution wasn't found, Italy would plunge into financial chaos by the time the first espressos were being served the next morning.

And, if Italy plunged into chaos, so too would the rest of Europe, North America, Asia and anyone else who used money.

Berlusconi was no stranger to financial stress, A lifetime businessman and politician taught him that defaults and crisis occurred all the time.

This time was no different, and Berlusconi and many Italians already knew that joining the Euro monetary system was not all that it was suppose to be.

The worst kept secret amongst those who choose to know – Germany benefitted significantly from the creation of the Eurozone, while most other countries suffered.

Table 1 next page details exactly how the creation of the Euro helped Germany while it didn't help others.

For starters, prior to the creation of the Euro currency, Germany's currency (Deutsche Mark) was one of the strongest in the world. Germany was an exporting powerhouse providing its economy with fuel to create terrific jobs and strong tax revenues for a fiscally prudent government.

Joining the Eurozone, immediately switched Germany's expensive Deutsche Mark for a the new Euro currency which was about 40% cheaper.

The direct result for Germany was the new opportunity to sell its cars, pharmaceuticals, industrial machinery and chemicals at prices 40% less than before which virtually ensured it even more market share, more profits, more jobs and more tax revenues to the government.

Other Eurozone countries were not so fortunate.

Italy, Spain, Greece and Portugal have not enjoyed any of the advantages that fell into Germany's lap.

Winners vs Losers

Creation of the Euro							
Country	**Currency Strength**	**Economic Growth**	**Deficits**	**Debt**	**Political Stress**	**Social Unrest**	**Main Concern**
Germany	DEPRECIATED	STRONGER	DECLINED	DECLINED	INCREASED	INCREASED	Bailing Out Greece, Italy, Spain, Portugal
Greece	APPRECIATED	WEAKER	INCREASED	INCREASED	INCREASED	INCREASED	Not benefitting like Germany
Italy	APPRECIATED	WEAKER	INCREASED	INCREASED	INCREASED	INCREASED	Not benefitting like Germany
Spain	APPRECIATED	WEAKER	INCREASED	INCREASED	INCREASED	INCREASED	Not benefitting like Germany
Portugal	APPRECIATED	WEAKER	INCREASED	INCREASED	INCREASED	INCREASED	Not benefitting like Germany

Instead, it's been the exact opposite.

Whereas the Euro effectively gave Germany a currency that was 40% cheaper than the Deutsche Mark, Europe's southern countries had the opposite experience.

In these countries, the implicit stronger currency made exports more expensive than before. The economy weaker, less tax revenues available for governments and the one factor that is infrequently discussed – it made their outstanding debt increase by 40% and higher.

In a normal financial world, in times of trouble, a country has the ability to make either internal or external adjustments to its economy

Internal adjustments means wages are lowered and productivity is increased which should make the country's products more attractive to foreign buyers.

External adjustments, means a country makes its products cheaper and more attractive to foreign buyers by devaluing its currency.

Since people prefer not to have their wages reduced, most would undoubtedly not choose internal adjustments.

Which means, external adjustments are usually the stimulus measure by default.

Every country in the world has the opportunity to do this.

The Big Bluff

Well, every country except for those trapped within the Eurozone.

Ever since the world crashed in 2008, countries everywhere have made both external and internal adjustments.

The Americans did it. Canadians did it. British, Australian and even the Chinese all took advantage of both internal and external adjustments to readjust their economies, put their heads down and plow on ahead.

Greece (especially Greece), Italy, Portugal, Spain and Ireland all had no choice – they were threatened with the choice between internal adjustments, or the horror of being booted out of the Eurozone and having their economies and citizens being blown back to the dark ages.

Or so they thought.

In understanding the above scenario, one simply has to understand poker and the art of the bluff.

And the only thing you need to know is that Germany has made the BIGGEST bluff in the history of global finance.

Make no mistake, the TROIKA (EU + IMF + ECB) is controlled by Germany, and they want nothing more than for the Eurozone to hold together.

This is for 2 reasons:

1) With the Euro intact, Germany will continue to make money hand over fist until the end of time.
2) Should the Euro break – Germany becomes a DOUBLE loser with its economy tumbling AND it losing BILLIONS owed to it by Italy et al.

Should the Euro break up, each country will either return to its old currency or maybe even create a new Southern Euro, Northern Euro or something of that nature.

Whatever currency is adopted by Germany instantly increases in value by up to 100%.

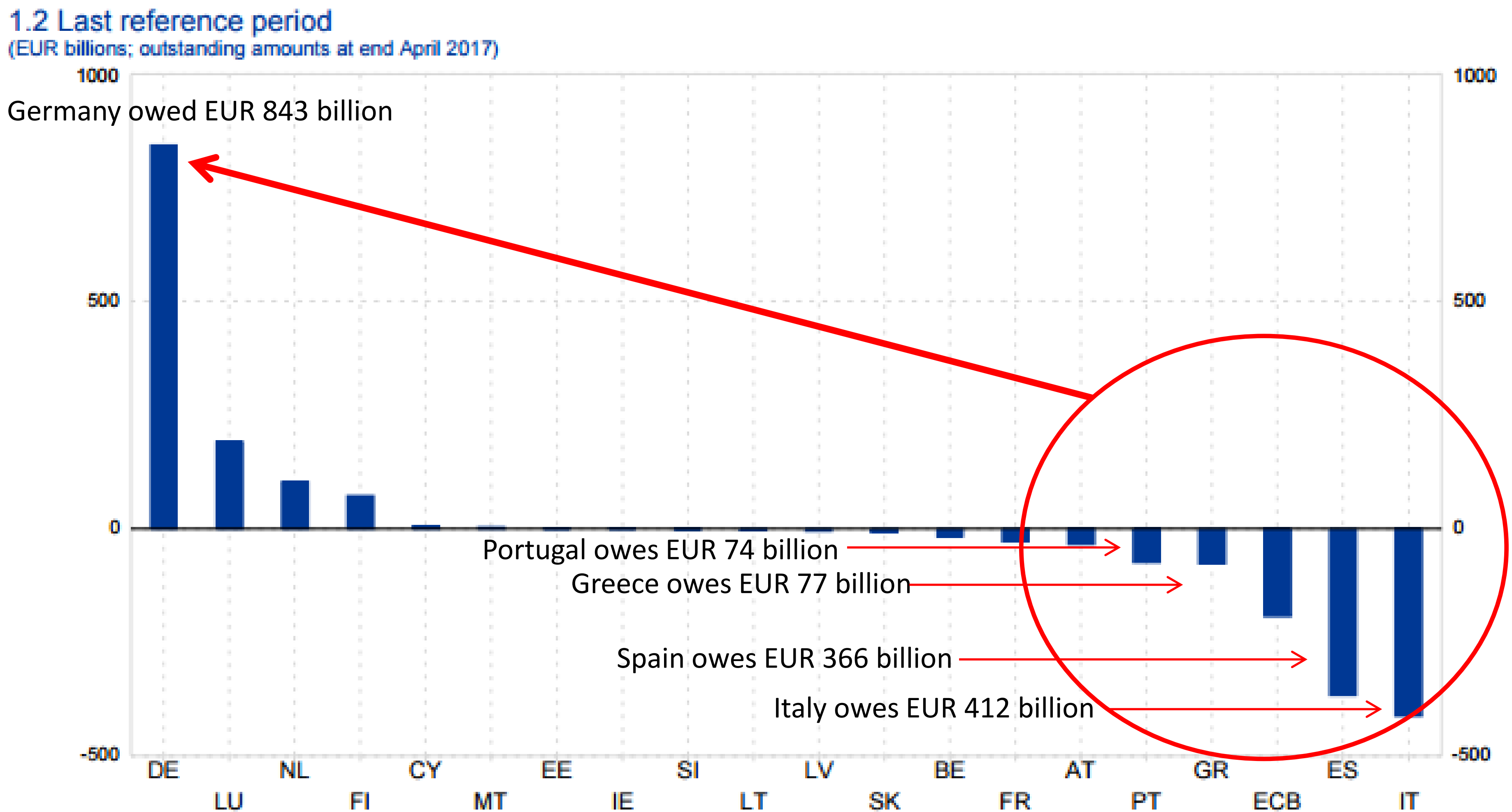
New currencies from Italy, Spain et al, instantly decrease by up to 50%.

All else being equal, a stronger currency is bad for exports, while a weaker currency is good for exports.

Yet, the real stinger for Germany lies within the central bank accounting system used by countries within the Eurozone.

Chart 3 next page details Target 2 balances for all countries that use the Euro currency.

Chart 3: ECB Target 2 Balances



Source: ECB, ECB calculations.

Keepin' it real

Target 2 Balances is yet another European financial reporting creation which stands for Trans-European Automated Real-time Gross Settlement System.

Regardless of the fancy name, it records money moving from one country to another.

Target 2 Balances is perhaps one of the most confusing, misunderstood, and under-reported problems from the Eurozone.

It is also, the clearest illustration as to why Germany has to keep the Eurozone intact, because without it, Germany will be owed a whole bunch of money of which it will never collect.

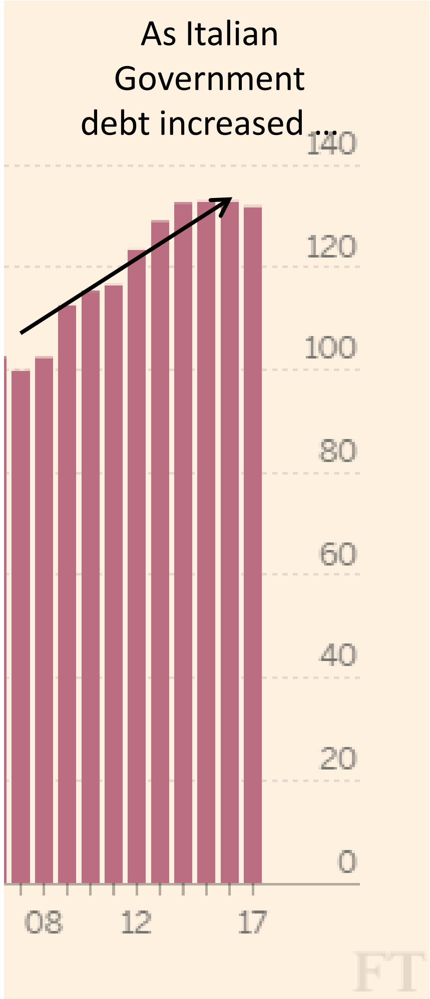
To really understand Target 2 Balances, just know that collectively Italy, Spain, Portugal and Greece owe Germany almost EUR 1 TRILLION.

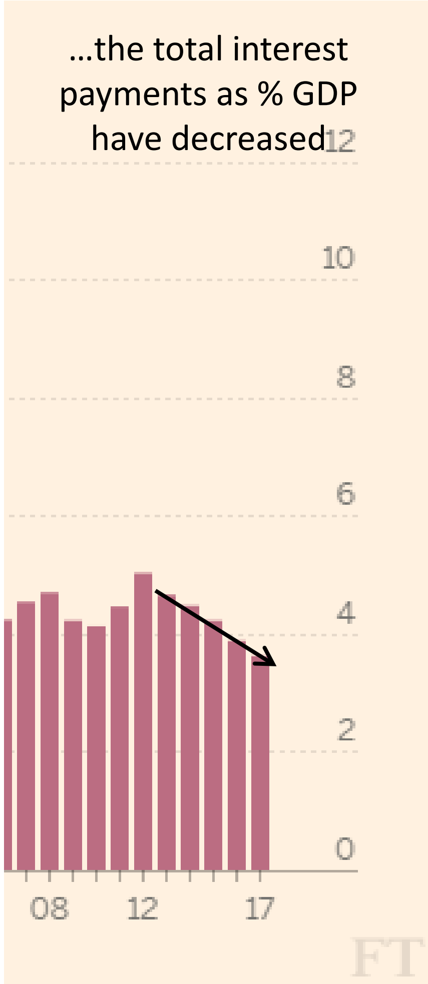
Reflecting upon the old adage "if I owe you a $1000, it's my problem. If I owe you a $1 Trillion, then you have a problem."

Considering this, now you can better understand the real reason why the ECB didn't simply write a cheque to every person in the Eurozone – it wouldn't help the governments and countries to fund their debt.

In other words, the only real way to help Italy and others was to lower interest rates to extreme levels so that interest payments on debt became immaterial.

To demonstrate the effect of artificially low interest rates, consider the following charts detailing Italy's debt and interest expense:





The Burning Question

And as interest rates became immaterial, it helped everyone wear a temporary facial mask to hide the large blemishes created by extreme levels of debt, and deficits running into infinity and beyond.

To truly appreciate the current situation in Europe, if you knew:
- A country's economy was declining
- its deficits were increasing
- its debts were increasing

You would automatically assume the country would have to pay higher interest rates when borrowing.

After all, their ability to repay the debt has certainly diminished due to a worsening money problem.

Yet, for Italy, Spain, Portugal, and Ireland - interest rates have DECREASED.

To ensure interest rates remain low in these crisis countries – and to ensure Germany remains in its favourably financial situation; Mario Draghi and the ECB are applying as much make-up as possible to give the appearance that these countries are healthy.

So, the question burning a hole in your pocket is as follows: how is Mario Draghi putting lipstick on Italian bonds?

The answer: he is printing money and using the money to buy every bond issued by Italy.

Not only is he buying bonds issued by the Italians, he's also buying bonds issued by the Spanish, Portuguese, Irish, French, Dutch and everyone else who uses the Euro.

By buying these bonds – interest rates are forced lower, giving the world the impression that all is well.

Make no mistake – this entire plot is designed to keep Italy afloat. Once Italy floats no more, the Euro becomes no more, which means German trade dominance also becomes no more.

This use to be a well kept secret only discussed by those who bothered to look.

Today however, it is a different story with many media outlets starting to see and understand exactly what is happening in the Eurozone.

It is well reported that Mario Draghi and his brethren in Japan, United States, and Britain have purchased over $18 Trillion of bonds from governments.

Considering the entire bond market is just $54 Trillion – no one should take any comfort in knowing that a full 1/3 of all government debt has been purchased by printing money.

But this isn't just a European story – this is a global effort by global central banks to artificially suppress interest rates everywhere.

How much interest do you pay?

Which of course is having wide reaching effects, especially in Toronto and its sky-high housing market.

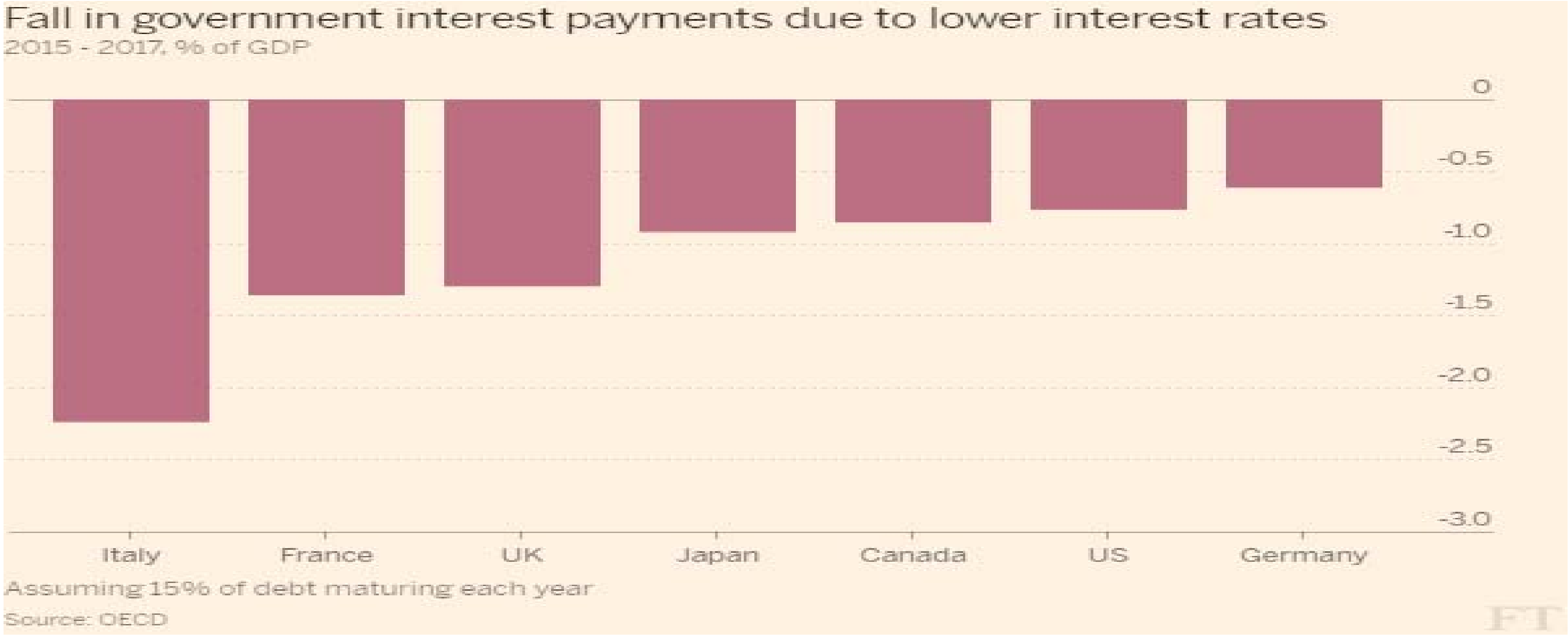
To demonstrate the effect of lower interest rates, consider the below chart which details exactly how much interest rates have fallen for various countries around the world.

Some will say this is all good. Lower rates helps everyone – including government finances look and feel better.

Yes this is true if interest rates were naturally lower. Instead, we have to consider and understand that rates are artificially lower.

There is a difference and the effects are starting to show in several ways.

For starters, 8 years of fantasy level interest rates has had an adverse effect on everyone who depends upon interest payments from bonds, GICs and term deposits to live.



A bank jog quickly turns into a run

The first corporate blemish has raised its hand where in Canada when the insurance company, Great West Life, finally made the decision to reduce head count by 1500 people to directly reduce costs.

What the company didn't say and what the pundits didn't see is that all insurance companies everywhere in the world are completely dependent upon interest rates to produce a regular stream of income.

We fully expect to hear more insurance companies announcing significant corporate restructurings to help offset the reduced income being earned due to lower rates.

Also in Canada, we saw Bank of Montreal announce they were selling a chunk of their mortgages as a MBS. This is also an interest rate story as the bank has also identified that higher rates are right around the corner and when it happens, the housing market simply declines.

Selling mortgages was a keen move by the bank.

Now, whoever bought these mortgages will have some explaining to do once rates rise.

Next up to bear the brunt of artificially lower rates is Canada's very own housing crisis poster child – Home Capital Group.

This company was also feasting off the low interest rate environment by providing mortgage loans to higher risk borrowers.

Life was good until suddenly, investors started to lose confidence in Home Capital Group's ability to pay back deposits.

Just to remind everyone; banks are levered entities. This means every $1 withdrawn from the bank reduces their capacity to lend by 10-30 times.

As the number of withdrawals increased, it resulted in Home Capital Group going under in less than a week.

Yes, that's how fast things can unravel when you lose access to funding markets.

And to top things off, the icing on the Canadian cake occurred when Moody's downgraded all of Canada's banks due to the heightened risk of the mortgage loan and housing market – or in other words, the risk of long-term rates surging higher due to the crisis in Europe.

Meanwhile, back to the Italians and their crisis from 2011 – now you have a better understanding for what happened next.

In the middle of the night, Prime Minister Berlusconi told the EU, the ECB and the IMF that he was pulling Italy out of the Euro.

In Berlusconi's eyes, leaving the Euro and bringing back the Lira would at least give Italy a chance.

In reality, he stood no chance.

You're fired!

By 3 am, Berlusconi (the elected Prime Minister of Italy) was removed from office by non-Italians, and replaced by an EU appointed official.

Hours later, Mario Draghi whipped out the largest stick of lipstick known to mankind and began what would be a 5 years (and counting) experiment of trying to make, not only Italy's financial situation look beautiful, but all of the Eurozone countries look beautiful.

Which brings us today's headlines:

Catalonia calls independence referendum for October

Spanish government has vowed to do everything it can to prevent long-awaited and highly controversial referendum from taking place

Spain's economic powerhouse, the Catalonia region continues pressing hard to leave Spain.

Meanwhile, also in Spain news of a Banco Popular going under forced millions of losses on investors – most notably PIMCO, which so happens to be one of the world's largest bond managers.

FINANCIAL TIMES

US COMPANIES MARKETS OPINION WORK & CAREERS LIFE & ARTS

Banco Popular Español SA + Add to myFT

Pimco hit by price plunge in teetering Spanish bank's bonds

Of course, for those unaware, companies will always experience times of stress and during these times of stress it is very common for the CEO to communicate with employees everywhere.

This is normal.

However, as soon as you see the Chairman of the Board sending out "stay calm, there's nothing to fear" communications – then you know the company is dead in the water.

Banco Popular Head Tells Staff to Stay Calm,

By REUTERS JUNE 3, 2017, 7:33 A.M. E.D.T.

MADRID — The chairman of Banco Popular has told his executives that the struggling Spanish lender was solvent and urged them to remain calm and confident, while a source said he would hold a routine meeting with the European Central Bank next week.

Popular's shares fell almost 40 percent in the past three days on concern it

You're so popular!

Naturally, if Spain's Banco Popular wasn't doing so well, we can only imagine the state of Spain's unpopular bank.

Meanwhile in Italy, its banking system remains stuffed with bad loans. To demonstrate how dire the situation is, consider that there is an estimated EUR 360 billion in bad loans compared to just EUR 225 billion in equity.

In other words, in the real world, one without interference from Mario Draghi, the bad loans in Italy would be written off as losses, and since there isn't enough equity to offset these losses – every bank in Italy would have its doors nailed shut.

Yes, it is that serious.

By now, you know everyone in the world is affected by interest rates and all banks and governments eat and sleep off the same interest rate structure.

You also know, that the only reason global interest rates are at their lowest levels in 100s of year is due to central banks printing money and buying bonds.

And you also know that central banks cannot continue doing this forever – and within Europe especially, many people are unhappy with the Euro, and many banks and governments are hanging by the thread.

Meanwhile, consider that when the interest rate bubble in Europe does break, it not only becomes a problem for the entire global bond market, but the corresponding surge in US Dollars makes it a very uncomfortable day for everyone in emerging markets.


Global Finance Fate Entangled in Web of Emerging World, BIS Says


MARKETS | HEARD ON THE STREET

Emerging-Market Debt: How Big a Threat Is It?

Emerging-market companies have relied more on bond-market borrowing since the 2008 crisis, but that could breed a whole new set of problems

Let's be clear – there is a gigantic bubble in long-term interest rates. And when it breaks, it will have devastating affects on everyone who replies upon the bond market in one way or another.

Including the Toronto housing market.

There is good news. As bonds, housing and most currencies decline – other investments will move sharply in the opposite direction generating significant gains for those who can see through the make-up.

We've increased equities

Our Strategy

Global trends continue towards a crisis in long-term interest rates, which will be reflected:
- negatively in fixed income strategies and most currencies.
- positively in USD, most equities, and eventually gold & commodities.

We continue to structure our strategies for minimal exposure to these high risk markets, and maximum exposure to others.

Bonds

There's been no change to our long-term outlook for bonds. All of our portfolios continue to hold minimum allocations to bonds, with no high yield, no emerging market debt, and no long duration.

Granted, long-term bonds have rallied a bit since their sharp correction last November, yet nothing has occurred to alter the fact that long-term interest rates reached their major lows last year, and the future remains grim.

We continue to see bonds as the riskiest long-term investment in the market place.

Stocks

Since our last update in March, we increased allocations to equities. Market internals remain strong, while market sentiment improved from being too optimistic towards more of a neutral position.

Unless equity markets experience a significant correction (>10%), we'll remain invested and continue to add further to our strategies when opportunities arise.

Currencies

USD has declined modestly and our short-term models are beginning to show opportunities to add further to long USD positions.

We suggest investors not be fooled by the near-term rally in EUR. Unless it breaks 1.16 range, we expect it to bounce down hard.

Commodities

We remain with no allocations to direct commodities. Oil remains incredibly weak, and unless we see a surge towards $60, we expect further downside.

For gold, again price action is still not favourable. Despite the mass negative headlines on Trump, North Korea, Qatar, terrorist attacks in Britain, and increased division between the left and the right, gold remains stuck.

With all of the negativity in the world, one would think gold would be soaring – but it isn't. Which means something else is a foot.

We remain patient on gold. The opportunity will come to own a lot of it, but we're not there yet.

Opportunities

As always, we'd be pleased to speak with anyone about our investment views. We also encourage our readers to share our global market outlook with those who they think may find it of interest.

Keith Dicker, CFA founded IceCap Asset Management Limited in 2010 and is the President and Chief Investment Officer. He has over 20 years of investment experience, covering multi asset class strategies including equities, fixed income, commodities & currencies.

Keith earned the Chartered Financial Analyst (CFA) designation in 1998 and is a member of the Chartered Financial Analysts Institute. He has been recognized by the CFA Institute, Reuters, Bloomberg, BNN and the Globe & Mail for his views on global macro investment strategies. He is a frequent speaker on the challenges and opportunities facing investors today, and is available to present to groups of any size.

Our Team:

Keith Dicker: keithdicker@IceCapAssetManagement.com

John Corney: johncorney@IceCapAssetManagement.com

Haakon Pedersen: haakonpedersen@IceCapAssetManagement.com

Andrew Feader: andrewfeader@IceCapAssetManagement.com

Conor Demone: ConorDemone@IceCapAssetManagement.com

We want Partners

Since 2010, IceCap Asset Management has consistently demonstrated a unique and correct understanding of the world's global macro environment.

Our ability to communicate this understanding in both our investment portfolios and through our highly successful **Global Market Outlook** is a feature we would love to leverage.

IceCap Asset Management is a growing firm, and we are completely open to discussing all opportunities, ideas and ventures with other firms, fiduciaries and individuals anywhere in the world.

Opportunities may include:

1. white labelling of funds
2. sub advisory of funds or managed platforms
3. speaking engagements for small or very large groups
4. joint ventures
5. Canadian licensed advisors, portfolio managers & financial planners
6. other corporate opportunities

Contact Keith Dicker 1-902-492-8495 or
KeithDicker@IceCapAssetManagement.com