

# GREEN PARTNERS<sub>LLC</sub>

December 31, 2011

Dear Partner-Clients,

Happy New Year!

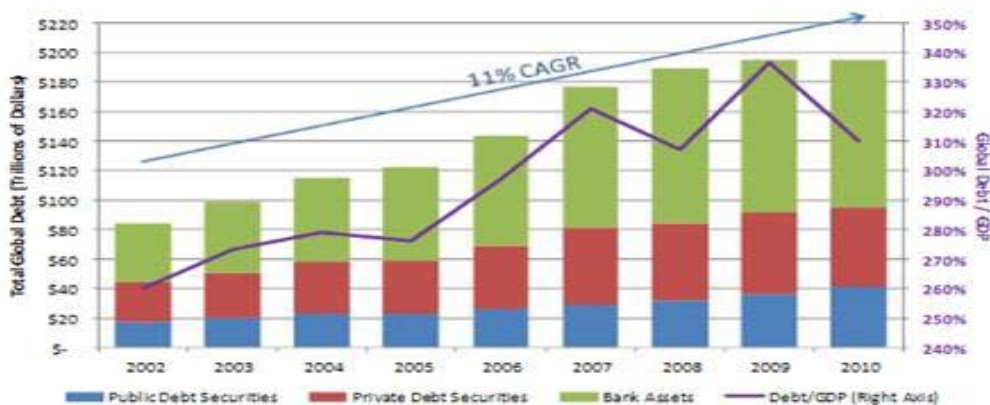
The markets have been vacillating between *unsustainable* government debts mattering to not mattering *from one moment to the next*. I believe unsustainable debts matter, especially when they hit tipping points such as now. Debts mattering are nothing new to us at Green Partners as I written about them ad nauseam, and since debts have for mattered for 3,000 years I'm not trying to be prophetic, just pragmatic thanks to my trusty old abacus.

While central banks and politicians are grappling all over the globe on what actions should be taken, and no matter what choices are made there can only be one of two outcomes in the near term, more on that in just a moment, we've been primarily positioned in neutral for the last half year waiting for fiscal and monetary policy to unfold for optimal asset allocation decisions for good reason.

Total global credit debt as a percentage of the world's gross domestic product is in uncharted territory, uncomfortably resting at 310% debt to GDP (just prior to the Great Depression total credit debt to GDP was 225%). When government debts are this high, either bond markets will call the problems out or politicians will be proactive. Unfortunately, in this era of re-elections trumping hard choices the world over, it is the credit markets calling the debt problems out.

With total global debt to GDP at 310% today it's no surprise that the world is having one debt crises after another, with politicians and central banks scrambling from one raging fire to the next with no credible solutions to date (telling the truth would be a good start). Unfortunately, there are no "easy" fixes, which the general populace wants so desperately to believe. No country in history has ever grown out of a total credit debt to GDP ratio greater than 260%. With total global credit debt to GDP above 310%, it's *inevitable* there are going to be clusters of debt destruction in one way or another.

Total Global Debt (Left Axis) and Global Debt/GDP (Right Axis)  
(S in Trillions)



As the chart from Hayman demonstrates, global debt has grown at an 11% compounded growth rate while economies have grown at a 4% annualized rate since 2002. This is clearly unsustainable, and countries have failed at trying to grow out of their debt problems with more debt unsuccessfully. A pencil and a cocktail napkin is all it takes to figure it out, yet it is hard to find any politician in the world running the big show willing to admit debt write-downs are the only real answer to a sustainable future.

This global debt trajectory is akin to the cash refinance bonanza in the housing boom where many Americans continued to spend far above their means as they used their houses as credit card ATM machines to fund unsustainable lifestyles—believing houses would always just go up and credit would always be available.

Where at a tipping point now, especially in Europe and Japan, where it is evident “growth” won’t be sufficient to fix the problem. Because of this, I believe there is a large probability that at least one sovereign default in Europe is in the near future—namely Greece, which will no doubt have ripple effects. If this should happen, I expect Japan to become front page news as well, which will be a larger problem than Europe.

In any case, whether countries such as Japan or the European Union or the United States decide to print or restructure, one outcome is certain: no matter what the policy decisions are, to restructure or to print, it will have enormous implications for investors.

In other words, their policy decisions will have binary results on investments—everything up or down. The markets are trying to anticipate which way policy goes *in multiple countries* which explains the bi-polar market over the last 6 months. We’re waiting patiently for policy response before we position ourselves far more constructively. Once we get it, we’ll be ready to take advantage of it.

### **Alignment of Interests**

Your relationship with me is *structured* in a way that, aside from your health and well being, the only thing that matters to me is your long-term success. We are totally aligned.

Sincerely,

Nicholas Green

