January 4, 2016 - 2016's ECONOMIC HEADWINDS

David Stockman gives us lots to think about as he looks over the world's economy. First he takes on the commodity bubble fueled by the giant credit boom.

The giant credit fueled boom of the last 20 years has deformed the global economy in ways that are both visible and less visible. As to the former, it only needs be pointed out that an economy based on actual savings from real production and income and a modicum of financial market discipline would not build 65 million empty apartment units based on the theory that their price will rise forever as long as they remain unoccupied!

That's the Red Ponzi at work in China and its replicated all across the land in similar wasteful investments in unused or under-used shopping malls, factories, coal mines, airports, highways, bridges and much, much more.

But the point here is that China is not some kind of one-off aberration. In fact, the less visible aspects of the credit ponzi exist throughout the global economy and they are becoming more visible by the day as the Great Deflation gathers force.

As we have regularly insisted, there is nothing in previous financial history like the $185 trillion of worldwide credit expansion over the last two decades. When this central bank fueled credit bubble finally reached its apogee in the past year or so, global credit had expanded by nearly 4X the gain in worldwide GDP. ...

... The credit bubble, in turn, led to booming demand for commodities and CapEx. And in these unsustainable eruptions layers and layers of distortion and inefficiency cascaded into the world economy and financial system.

One of these was an explosion of CapEx in the oil patch and the mining sector in response to massive price and margin gains and the resulting windfall rents on existing assets. In the case of upstream oil and gas, for example, worldwide investment grew from $250 billion to $700 billion in less than a decade.

Needless to say, there is now so much excess supply and capacity on the world market that oil has plunged into a collapse that is likely to last for years, as old investment come on-stream while world demand falters in the face of the gathering global recession. ...

... The same kind of malinvestment occurred in the mining sectors where Australia's boom in iron ore, coal, bauxite and other industrial materials provides a good proxy. ...

... Nor was the credit-fueled CapEx boom limited to energy and metals. Bloomberg carried a story today outlining a similar super-cycle in the global rubber industry. As a result of massive rubber plantation expansion in response to soaring prices and windfall profits, the industry is now facing investment and job killing surpluses as far as the eye can see. ...

... The unfolding correction of the visible excesses of the credit inflation—such as overinvestment and malinvestment—— will destroy incomes and profits; the Great Unwind of the less visible effects, such as the sovereign wealth fund liquidations, are a giant pin aimed squarely at the monumental worldwide bubbles in stock, bonds and real estate.

Turning his attention to the stock market, **Mr.Stockman** posts on valuations pointing out that the price increase of just four stocks accounted for one half of a trillion dollars. He starts out with Amazon.

If you have forgotten your Gulliver's Travels, recall that Jonathan Swift described the people of Brobdingnag as being as tall as church steeples and having a ten foot stride. Everything else was in proportion——with rats the size of mastiffs and the latter the size of four elephants, while flies were "as big as a Dunstable lark" and wasps were the size of partridges.

*Hence the word for this fictional land has come to mean colossal, enormous, gigantic, huge, immense or, as the urban dictionary puts it, "really f*cking big".*

That would also describe the $325 billion bubble which comprises Amazon's market cap. It is at once brobdingnagian and preposterous——a trick on the casino signifying that the crowd has once again gone stark raving mad.

When you have arrived at a condition of extreme "irrational exuberance" there is probably no insult to ordinary valuation metrics that can shock. But for want of doubt consider that AMZN earned the grand sum of $79 million last quarter and $328 million for the LTM (Last twelve months) period ending in September.

*That's right. Its conventional PE multiple is **985X! ...***

... we are just completing a year in which the Fabulous Four FANG stocks (Facebook, Amazon, Netflix and Google) gained $500 billion of market cap while the remaining 496 companies in the S&P index went down by more than one-half trillion dollars.

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... Indeed, Amazon's $325 billion valuation is just plain irrational exuberance having one last fling. Spasms like this year $180 billion gain (125%) on the AMZN ticker or the $190 billion gain (55%) on the GOOG account are absolutely reminiscent of the final days before the tech wreck exactly 15 years ago.

In a recent post I demonstrated how the 12 Big Cap Techs of 2000—-led by Microsoft, Intel, Dell and Cisco——-saw their combined valuation soar from $900 billion to $3.8 trillion in the 48 months leading up to the March 2000 peak; and that they then plunged to just $875 billion a decade later.

To wit, their bubble era market cap got whacked by $3 trillion in the years ahead, even as their sales and earnings continued to grow. What got purged was irrational exuberance in a casino high on the central bank's monetary heroin. ...

... At the end of the day, AMZN's current preposterous $325 billion market cap has nothing to do with the business prospects of Amazon or the considerable entrepreneurial prowess of Jeff Bezos and his army of disrupters.

It is more in the nature of financial rigor mortis——-the final spasm of the robo-traders and the fast money crowd chasing one of the greatest bubbles still standing in the casino. ...

... So Amazon's total $325 billion valuation is just plain irrational exuberance. It is surely a sign that the third great financial bubble of this century has narrowed down to just a handful of brobdingnagian beanstalks that are soon to come crashing down from the sky.

When the big market break comes in the period just ahead, AMZN is sure to shed as much of its excess market cap as did Cisco after March 2000. That would be hundreds of billions of evaporating bottled air. It would be the short of a lifetime.

If all of that is not enough to trouble your sleep, here's **Harry Dent**.

A Yahoo Finance headline this morning reads: "Unhappy New Year: The U.S. Economy Is Stalling Out."

We recently learned that existing home sales in November crashed 10.5% from the month before.

Guess when the last time was when we saw these levels? The housing crisis of the mid- to late-2000s!

I also recently shared a chart showing a cataclysmic 82% drop in the ratio of new home sales to the U.S. population. To put it simply, we won't need more real estate for decades to come, with baby boomers increasingly dying to offset rising millennial home purchases.

I and a few other experts like David Stockman have continued to argue that this re-bound since 2009 has been all smoke and mirrors – artificial stimulus that has only created greater bubbles in financial assets like stocks, and financial engineering to create rising corporate profits. None of it goes toward real expansion for future jobs, productivity and growth… things like new office space and industrial capacity. ...

... financial engineering does not result in real growth.

And speculation does not expand the money supply.

It is only a sign of decreasing money velocity, and a bubble that will only burst – like in 1929, 2000, and now again!

It's a mirage.

It isn't real.

And it isn't sustainable.

Despite such endless financial engineering, sales for the S&P 500 have been declining for the last three quarters. And profits have declined for the first time since the 2009 expansion.

I'd be surprised if both didn't continue down in the 4th quarter.

This will end badly… which is the only way bubbles end.

My forecast today: the stock market will start to crash by early February, if not sooner, when it gets this clear realization.

Contra Corner

Now Comes The Great Unwind—-How Evaporating Commodity Wealth Will Slam The Casino

by David Stockman

The giant credit fueled boom of the last 20 years has deformed the global economy in ways that are both visible and less visible. As to the former, it only needs be pointed out that an economy based on actual savings from real production and income and a modicum of financial market discipline would not build 65 million empty apartment units based on the theory that their price will rise forever as long as they remain unoccupied!

That's the Red Ponzi at work in China and its replicated all across the land in similar wasteful investments in unused or under-used shopping malls, factories, coal mines, airports, highways, bridges and much, much more.

But the point here is that China is not some kind of one-off aberration. In fact, the less visible aspects of the credit ponzi exist throughout the global economy and they are becoming more visible by the day as the Great Deflation gathers force.

As we have regularly insisted, there is nothing in previous financial history like the $185 trillion of worldwide credit expansion over the last two decades. When this central bank fueled credit bubble finally reached its apogee in the past year or so, global credit had expanded by nearly 4X the gain in worldwide GDP.

Moreover, no small part of the latter was simply the pass-through into the Keynesian-style GDP accounting ledgers of fixed asset investment (spending) that is destined to become a write-off or public sector white elephant (wealth destruction) in the years ahead.

The credit bubble, in turn, led to booming demand for commodities and CapEx. And in these unsustainable eruptions layers and layers of distortion and inefficiency cascaded into the world economy and financial system.

One of these was an explosion of CapEx in the oil patch and the mining sector in response to massive price and margin gains and the resulting windfall rents on existing assets. In the case

of upstream oil and gas, for example, worldwide investment grew from $250 billion to $700 billion in less than a decade.

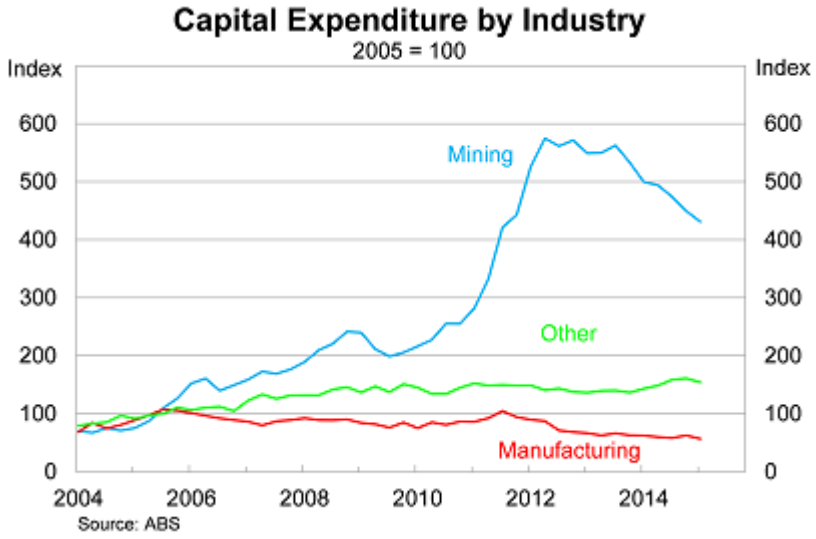
Needless to say, there is now so much excess supply and capacity on the world market that oil has plunged into a collapse that is likely to last for years, as old investment come on-stream while world demand falters in the face of the gathering global recession. Already, investment is estimated to have dropped by 20% in 2015, and that is just the beginning.

This unfolding collapse of oil and gas investments, of course, will ricochet through the capital goods and heavy construction sectors with gale force. Eventually, annual investment may decline by $250 to $400 billion before balance is restored, meaning that what were windfall profits and surging wages and bonuses in these sectors just a year or two back will evaporate in the years ahead.

Contrary to the circular logic of our Keynesian central planners and Wall Street stock peddlers, the pending massive loss of value added capital spending in the energy patch is not a part of some grand reallocation game; it won't be made up by households—-which are already at peak debt—— borrowing even more in order to go to the restaurant or yoga studio.

Instead, as the credit bubble begins to shrink it means that profits, incomes, balance sheets and credit-worthiness are all shrinking, too. So is the related GDP.

The same kind of malinvestment occurred in the mining sectors where Australia's boom in iron ore, coal, bauxite and other industrial materials provides a good proxy. As shown below, CapEx in mining grew by nearly 6X in less than a decade.



But given the massive oversupply and plunging prices and margins in these commodities, and the overhang of still more capacity in the pipeline coming to completion, it is fair to say that investment in the global mining industry is sinking into a depression that will last the better part of a decade.

Indeed, as shown above, global mining industry CapEx soared by 5X during the seven years through the 2012 peak, but the overwhelming share of that was in greenfield and brownfield investments. Yet given the massive global overcapacity in iron ore, copper, metallurgical coal,

bauxite/alumina etc., those kinds of projects are likely to be few and far between in the years ahead.

Needless to say, that means shrinking profits and the massive loss of high wage jobs and vendor service contracts. Even baristas at Starbucks do not earn a fraction of what had been paid to miners and UAW members on the Caterpillar assembly line.

Nor was the credit-fueled CapEx boom limited to energy and metals. Bloomberg carried a story today outlining a similar super-cycle in the global rubber industry. As a result of massive rubber plantation expansion in response to soaring prices and windfall profits, the industry is now facing investment and job killing surpluses as far as the eye can see.

Global demand for natural rubber, used mostly in tires, is slowing as the economy cools in China, the world's largest buyer of new cars. Supplies are expanding after a decade-long rally in prices to a record in 2011 encouraged top producers like Thailand, Indonesia and Vietnam to plant more trees. Output will exceed use for two more years, with the surplus quadrupling in 2016, according to The Rubber Economist Ltd., a London-based industry researcher.

……Rubber traded in Tokyo, a global benchmark, has tumbled 70 percent from a record in 2011, touching a six-year low of 153 yen ($1.26) a kilogram on Nov. 6. Futures in Shanghai have slumped 22 percent in 2015. The export price from Thailand, the top producer, is down 23 percent…..

Global production is set to exceed demand by 411,000 metric tons next year and by 430,000 tons in 2017, compared with a surplus of 98,000 tons in 2015, The Rubber Economist predicted on Dec. 9. Output will increase 3.8 percent next year to 13 million tons and will keep expanding through 2018, the researcher said. Consumption won't grow nearly as fast, which will leave stockpiles by the end of 2017 at a record 3.7 million tons, said Prachaya Jumpasut, managing director of The Rubber Economist.

Excess supplies may keep prices subdued for a decade, said Hidde Smit, an industry adviser who has studied the market for more than 30 years and is the former secretary-general of the International Rubber Study Group. Even with some smaller farms cutting back now, the planted area across 11 Asian countries that are the primary growers has surged 45 percent since 2004, he said.

So with producer profits and incomes falling in commodity sectors and capital goods industries all over the world, there is no prospect of a smooth rotation into more services and consumption. Deflation means not just lower oil or steel prices; it also means the evaporation of production and incomes which were falsely inflated by the 20-year credit binge.

And that's not the half of it. The massive windfalls on commodities and capital goods earned by producers during the great credit inflation were not entirely reinvested in new capacity and fixed assets. As the Wall Street Journal documented recently, it also enabled a huge increase in the balance sheets of sovereign wealth funds due to state ownership or heavy taxation of oil and mineral production.

But now the days of heady accumulation of "sovereign wealth" in Saudi Arabia, Norway, Kazakhstan and dozens of commodity producers in between is over and done. What is happening is that these funds are entering a cycle of liquidation which is unprecedented in financial history.

Indeed, the data for Saudi Arabia, Qatar, Kuwait, the UAE and other members of the Gulf Cooperation Council (GCC) is stunning. During the global credit boom they amassed sovereign wealth funds totaling $2.3 trillion. But with deficits now estimated at 13% of GDP and rising, the level of asset liquidation is soaring.

Thus, if crude oil prices recover to $56 per barrel next year, the GCC states will need to liquidate $208 billion of investments. Yet if prices fall to $20 per barrel, as Goldman Sachs has warned, they would need to liquidate nearly $500 billion of their booty in a single year.

But regardless of the exact crude oil path in the years ahead, prices are sure to stay in the sub-basement for an extended period. That means that the GCC states may need to liquidate the entirety of their sovereign wealth funds by early in the next decade.

The same is true on a worldwide basis for all of the energy and mineral based sovereign wealth funds. They will be in a liquidation mode for years to come as the great commodity deflation runs its course.

In a word, the unnatural Big Fat Bid of the sovereign wealth funds is going All Offers as oil and commodity producers struggle to fund their budgets.

Stated differently, just as the commodity bubble effects did not stay contained in the energy and metals markets as the global credit bubble expand, the same will be true in the deflation cycle.

The unfolding correction of the visible excesses of the credit inflation—such as overinvestment and malinvestment—— will destroy incomes and profits; the Great Unwind of the less visible effects, such as the sovereign wealth fund liquidations, are a giant pin aimed squarely at the monumental worldwide bubbles in stock, bonds and real estate.

ContraCorner

The Next Big Short——Jeff Bezos' Brobdingnagian Bubble

by David Stockman

If you have forgotten your Gulliver's Travels, recall that Jonathan Swift described the people of Brobdingnag as being as tall as church steeples and having a ten foot stride. Everything else was in proportion——with rats the size of mastiffs and the latter the size of four elephants, while flies were "as big as a Dunstable lark" and wasps were the size of partridges.

Hence the word for this fictional land has come to mean colossal, enormous, gigantic, huge, immense or, as the urban dictionary puts it, "really f*cking big".

That would also describe the $325 billion bubble which comprises Amazon's market cap. It is at once brobdingnagian and preposterous——a trick on the casino signifying that the crowd has once again gone stark raving mad.

When you have arrived at a condition of extreme "irrational exuberance" there is probably no insult to ordinary valuation metrics that can shock. But for want of doubt consider that AMZN earned the grand sum of $79 million last quarter and $328 million for the LTM (Last twelve months) period ending in September.

That's right. Its conventional PE multiple is ***985X!***

And, no, its not a biotech start-up in phase 3 FDA trials with a sure fire cancer cure set to be approved any day; its actually been around more than a quarter century, putting it in the oldest quartile of businesses in the US.

But according to the loony posse of sell-side apologists who cover the company——there are 15 buy recommendations——Amazon is still furiously investing in "growth" after all of these years. So never mind the PE multiple; earnings are being temporarily sacrificed for growth.

Well, yes. On its approximate $100 billion in twelve months sales Amazon did generate $32.6 billion of gross profit. But the great builder behind the curtain in Seattle choose to "reinvest" $5 billion in sales and marketing, $14 billion in general and administrative expense and $11.6 billion in R&D.

So there wasn't much left for the bottom line, and not surprisingly. Amazon's huge R&D expense alone was actually nearly three times higher than that of pharmaceutical giant Bristol-Myers Squibb. But apparently that's why Bezos boldly bags the big valuation multiples.

Not so fast, we think. Is there any evidence that all this madcap "investment" in the upper lines of the P&L for all these years is showing signs of momentum in cash generation? After all, sooner or later valuation has to be about free cash flow, even if you set aside GAAP accounting income.

In fact, AMZN generated $9.8 billion in operating cash flow during its most recent LTM period and spent $7.0 billion on CapEx and other investments. So its modest $2.8 billion of free cash flow implies a multiple of ***117X.***

Needless to say, the sell side chorus insists that one doesn't matter, either. At the drop of a hat Bezos could purportedly hit the investment "pause" bottom and unleash a surge of free cash flow.

The cynic might say good luck on that, considering the record. But then again, he might also ask ***why was Bezos' pause button massively rerated upward just as this bull market was reaching its fevered peak?***

That is, we are just completing a year in which the Fabulous Four FANG stocks (Facebook, Amazon, Netflix and Google) gained $500 billion of market cap while the remaining 496 companies in the S&P index went down by more than one-half trillion dollars.

In that context, AMZN's market cap one year ago was just $145 billion, meaning that it gained a stunning $180 billion or 125 percent during the interim.

By contrast, its free cash flow for the year ended September 2014 was $2.3 billion, meaning not only that it grew by a modest amount, but that a year ago the so-called "market" was valuing AMZN at just ***62X*** free cash flow. And to complete the picture, during the year ended in December 2011 Amazon generated $2.0 billion of free cash flow, meaning that is was then being valued at just ***40X***.

Can you say bubble mania? Bezos is surely the greatest empire builder since Genghis Kahn, and has never wavered in his determination to spend every dime the company generates in sales. Profits be damned.

But history will surely record that the 48 months since December 2011 comprised the final stages of the most stupendous financial bubble in recorded history. During that period, the casino re-rated Amazon's meager free cash flow from ***40X to 62X to 117X*** on virtually no improvement in performance.

It was just plain old multiple inflation gone wild with respect to the last momo stocks standing.

We have been here before, and there is no better analogy than Cisco and its fellow shooting stars in early 2000 on the eve of the dotcom crash.

Indeed, Amazon's $325 billion valuation is just plain irrational exuberance having one last fling. Spasms like this year $180 billion gain (125%) on the AMZN ticker or the $190 billion gain (55%) on the GOOG account are absolutely reminiscent of the final days before the tech wreck exactly 15 years ago.

In a recent post I demonstrated how the 12 Big Cap Techs of 2000—-led by Microsoft, Intel, Dell and Cisco——-saw their combined valuation soar from $900 billion to $3.8 trillion in the 48 months leading up to the March 2000 peak; and that they then plunged to just $875 billion a decade later.

To wit, their bubble era market cap got whacked by $3 trillion in the years ahead, even as their sales and earnings continued to grow. What got purged was irrational exuberance in a casino high on the central bank's monetary heroin.

In this regard, Cisco was the poster child last time around for this kind of top-of-the-bubble disconnect. During the 48 month run to March 2000, ***its market cap had exploded from $40 billion to $506 billion or by nearly 13X.***

By contrast, it net income had increased from $1.0 to $2.5 billion or by just 2.5X. Accordingly, its PE multiple was rerated during this classic era of irrational exuberance from ***40X to 200X.***

Even then, Cisco was not only the provider of all things for the internet, but was actually run by a CEO who had a decent respect for the idea of profits.

Indeed, during the most recent twelve months in the spring of 2000 CISCO had earned a respectable $2.5 billion of net income on $15 billion of sales. Moreover, this most recent net income posting had grown for eight straight years at a spectacular 50% compound rate from $100 million in 1992.

So its earnings track record was far more impressive and reliably rising than Amazon's recent results. In fact, AMZN's net income peaked at $1.15 billion way back in 2010 and has not come close to that high water mark since.

Still, Cisco's problem at the turn of the century was the market's lunatic valuation at 200X its smartly growing net income.

But here's the thing. Cisco was already a mature technology company. There was no growth rate in the known universe that would have permitted it to earn into a $500 billion valuation.

Even at a standard 20X market multiple on its existing fulsome net margins (17%), it would have needed $25 billion of net income on $150 billion of sales to make valuation ends meet.

In fact, during the next 15 years Cisco's performance steadily improved, but ***one and one-half decades later it is still at only one-third of the levels implied by its dotcom era market cap.*** That is, revenues have grown from $15 billion to nearly $50 billion, and its net income has more than tripled to nearly $10 billion per year.

Needless to say, it's market cap today at $140 billion is just 25% of its dotcom bubble peak!

In short, its market cap was driven to the absurd height recorded in March 2000 by the final spasm of a bull market, when the punters jumped on the last momo (momentum) trains out of the station.

At the end of the day, AMZN's current preposterous $325 billion market cap has nothing to do with the business prospects of Amazon or the considerable entrepreneurial prowess of Jeff Bezos and his army of disrupters.

It is more in the nature of financial rigor mortis——-the final spasm of the robo-traders and the fast money crowd chasing one of the greatest bubbles still standing in the casino.

And, yes, notwithstanding all the "good things it brings to life" daily, it is not the present day incarnation of even the mighty General Electric of the 1950s; and for one blindingly obvious reason. It has never made a profit beyond occasional quarterly chump change.

Not only has its net income been falling for five years, but what it has generated in the interim is actually a joke. To wit, during the last 23 quarters its has posted cumulative sales of nearly $380 billion but only $2 billion of net income, and half of that was in 2010.

That's right. The Kool Aid drinkers in the casino are betting $325 billion on a massive e-commerce distributor of books and merchandise that has a steady state profit rate at 0.5% of sales.

Admittedly, in these waning days of the third great central bank enabled bubble of this century, GAAP net income is a decidedly quaint concept. ***In the casino it's all about beanstalks which grow to the sky and sell-side gobbledygook.***

Here's how one of Silicon Valley's most unabashed circus barkers, Piper Jaffray's Gene Munster, explains it:

Next Steps For AWS… SaaS Applications? We believe AWS has an opportunity to move up the cloud stack to applications and leverage its existing base of AWS IaaS/PaaS 1M + users. AWS dipped its toes into the SaaS pool earlier this year when it expanded its offerings to include an email management program and we believe it will continue to extend its expertise to other offerings. We do not believe that this optionality is baked into investors' outlook for AWS.

Got that?

Instead, better try this. As indicated above, AMZN's operating free cash flow during its most recent LTM period was $2.76 billion compared to $2.26 billion way back in 2009.

So its six year free cash flow growth rate computes to just ***3.35%*** per annum. And on that going nowhere track record, AMZN is being valued at, well, like we said, 117X free cash flow!

The fact is, Amazon is one of the greatest cash burning machines ever invented. Its ***net revenues of just $8.5 billion in 2005 have since grown by 12X to $101 billion for the LTM period ending in September, meaning that during the last ten and three-fourths years it has booked $455 billion in sales. But its cumulative operating free cash flow over that same period was just $6 billion or 1.3% of its turnover.***

So, no, Amazon is not a profit-making enterprise in any meaningful sense of the word and its stock price measures nothing more than the raging speculative juices in the casino.

In an honest free market, real investors would never give a $325 billion valuation to a business that refuses to make a profit, never pays a dividend and is a one-percenter at best in the free cash flow department——that is, in the very thing that capitalist enterprises are born to produce.

Indeed, the Wall Street brokers' explanation for AMZN's $325 billion of bottled air is actually proof positive that the casino has become unhinged. For more than two decades, Amazon has been promoted as the monster of the E-commerce midway, which it surely is.

But this year's $180 billion market cap eruption has absolutely nothing to do with its newly developed capacity for same day delivery of healthy treats for your pooch. This most recent rip was all about the purportedly "scorching" performance of its AWS division——-that is, Amazon's totally unrelated business as a vendor of cloud computing services.

Indeed, CNBC recently gave air time to one of the most rabid analyst on the block, and this particular stock peddler from UBS left nothing to the imagination. Never mind whether anything emanating from that serial swindler and confessed criminal organization can be taken seriously, here's what the man said.

AWS is technology's second coming and is worth $110 billion. We know that because AMZN has recently been thoughtful enough to break out its financials.

They show AWS had sales of $2.1 billion in the September quarter and revenues of $6.9 billion on an LTM basis. So that puts its cloud computing business' value at 16X sales. No sweat!

Moreover, this means that the balance of the company——that is, its core E-commerce business—— is "only" valued at an apparently much more reasonable $215 billion. And by golly, said the UBS man, that's just 2.3X sales. So what's not to like?

Well, hold it right there. Someone forgot to do the math in all the excitement about AWS. Yes, the company's release did show that AWS posted $1.42 billion of operating income or about 20% of sales during the September LTM period.

But consolidated operating income during the quarter was only $1.72 billion, meaning that by the lights of subtraction, Jeff Bezos' great empire of E-commerce earned the microscopic sum of $300 million in operating income during its most recent year.

By the same magic of subtraction we can see that AMZN's E-commerce business generated $94 billion of sales. This means that its operating margin ***was exactly 32 basis points***.

That's right——after 25 years of crushing it on the E-commerce front, Amazon's core business operating margin is truly a rounding error.

And might we also ask why you would value at $215 billion the profitless sales of an E-commerce monster that just can't stop spending every dime it takes-in on distribution centers, package handlers, hired delivery trucks and drone prototypes; and now, apparently, same hour delivery service by out-of-work actors and bank tellers who happen to own a Vespa!

Stated differently, AMZN's $180 billion market cap gain in 2015 was not actually a re-rating; it was a bait-and-switch operation by the high-rollers in the casino.

Amazon is not the inventor and first-mover of E-commerce, after all. Instead, it's now suddenly held to be the monster of the midway in the totally unrelated business of cloud computing services.

By the lights of the UBS man and Wall Street's amen chorus, AWS is currently valued at a steaming 16X sales. But it will surely crush any competitor in the stretch ahead, and thereby grow its way into that outsized valuation.

Except don't tell Google, Microsoft, Oracle or several others about the beanstalk thing. Indeed, the current nattering about AWS was truly ridiculous. Why would anyone endowed with a modicum of sanity believe that these tech powerhouses are about to cede the cloud to Amazon merely because it comes first in the alphabet?

There is no other real reason for thinking so. Between them, the big three mentioned above have about $220 billion of cash and deep franchises in the world of computing and the internet.

Sure, when technology moved from owned boxes, corporate computer centers and software licenses to a rent-a-server model, Amazon got out of the gate first because it had no installed base of old technology to protect.

But there are no barriers to entry, no killer patents, no material brand equity, no irreproducible sales and service network etc. that will permit Amazon to ring-fence the cloud. So there will be vicious competition and prices will fall at a rate which will make Moore's law look tepid.

Indeed, Larry Ellison has recently promised to cut prices by 90%, and he has rarely failed to follow through on exactly that kind of competitive rampage.

Likewise, it would appear that the cloud is destined to be the future home of Microsoft's entire franchise. Surely it is probable that AMZN's Seattle neighbor can make the transition from selling computer software to renting cloud services.

In short, AMZN has disclosed almost nothing about AWS's detailed business model, its fixed and variable cost structure or the investment requirements of its rentable clouds and the rates of return on the massive amounts of capital employed.

Only the Wall Street boys, girls and robo-traders betting on red could come up with $110 billion valuation of a nascent business that is positioned in the cross-fire of the Big Tech battlefield.

So Amazon's total $325 billion valuation is just plain irrational exuberance. It is surely a sign that the third great financial bubble of this century has narrowed down to just a handful of brobdingnagian beanstalks that are soon to come crashing down from the sky.

When the big market break comes in the period just ahead, AMZN is sure to shed as much of its excess market cap as did Cisco after March 2000. That would be hundreds of billions of evaporating bottled air. It would be the short of a lifetime.

Economy and Markets Daily

The Deadly Truth About the Great Boom and This "Recovery"

by Harry Dent

A *Yahoo Finance* headline this morning reads: "Unhappy New Year: The U.S. Economy Is Stalling Out."

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Guess when the last time was when we saw these levels? The housing crisis of the mid- to late-2000s!

I also recently shared a chart showing a cataclysmic 82% drop in the ratio of new home sales to the U.S. population. To put it simply, we won't need more real estate for decades to come, with baby boomers increasingly dying to offset rising millennial home purchases.

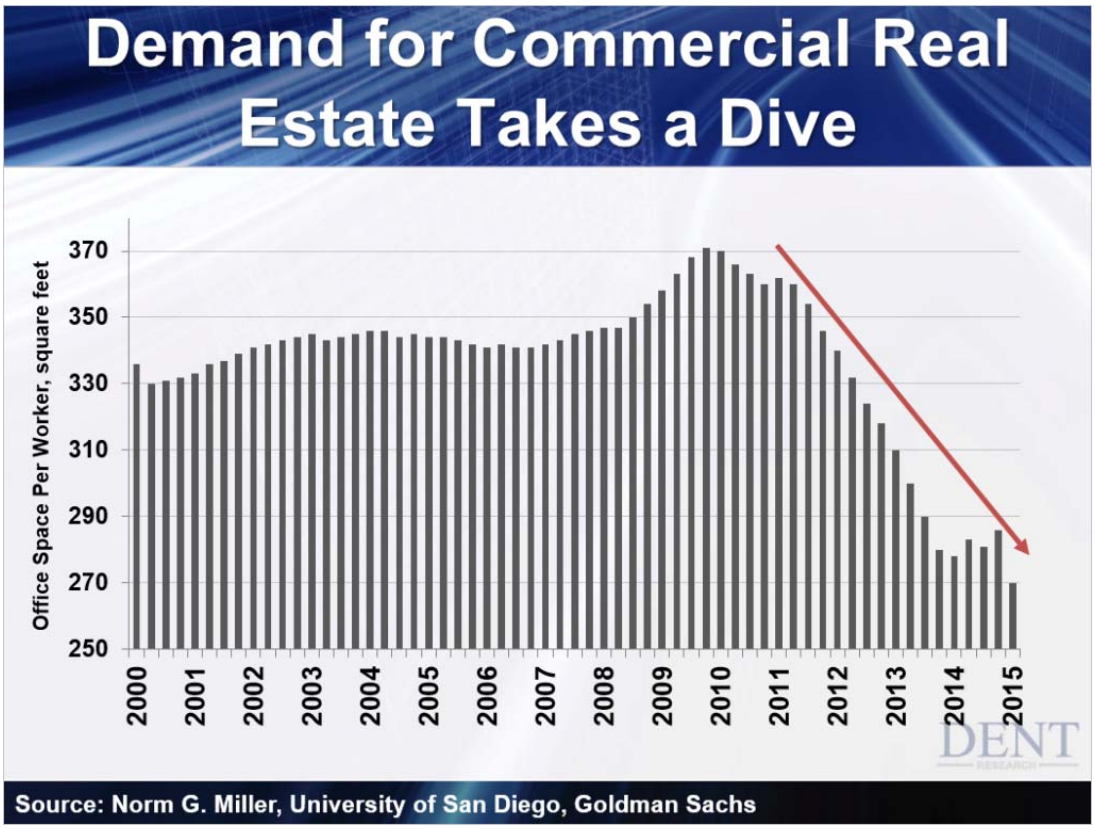
I and a few other experts like David Stockman have continued to argue that this re-bound since 2009 has been all smoke and mirrors – artificial stimulus that has only created greater bubbles in financial assets like stocks, and financial engineering to create rising corporate profits. None of it goes toward real expansion for future jobs, productivity and growth… things like new office space and industrial capacity.

Wall Street analysts and corporate CEOs can argue against this with their "this is not a bubble" logic, but this chart tells the real story.

Below is a chart that shows the office space per worker in square feet. It shows a rise into the height of the financial crisis, after which it's fallen like a rock!

At first this could seem counterintuitive. Why did the square footage per worker go up into the worst of the recession into mid- to late-2009? That's because companies were laying off workers going into that recession, meaning there were more workers per square feet.

But the real story comes in the recovery from late 2009 forward.



Square footage per worker has declined very sharply from 371 square feet to 270, down a whopping one-third in just over six years as businesses have rehired a large portion of the laid-off workers – which means largely NOT creating new jobs.

You should *not* look at this chart and assume that because less square footage per worker means more workers than in the past that everything is hunky dory.

What's more important is that the sharp decrease in square footage implies a lack of demand in commercial real estate. And that's because commercial real estate is already way over-expanded! We overbuilt it in the great boom of 1983 to 2007, so even these hires have not filled up the available space. Which means businesses aren't expanding their office or industrial space!

So while hiring more workers sounds fine out of context… it's masking much more severe, deeper-set issues in our capacity to build for the future.

This is the hard truth that no one is looking at: businesses are merely re-employing their past capacity, and not creating new plants and offices for future employment. All the 200,000-plus jobs numbers per month, if they are even fully real, are just catching up with the past. And we shouldn't be investing in such new work space as we already have all we need for decades ahead.

This is the reality of demographics that clueless economists just don't get.

Meanwhile, more and more people drop out of the workforce either from giving up on finding a job, or retiring earlier once their kids have left the nest.

And more jobs are part-time or in the low-end service sector – like bartenders and waiters, not the higher-paid manufacturing and professional jobs of the past.

To top it off, fewer and fewer people are entering or staying in the workforce. Hence, the workforce participation rates continue to edge down – after falling sharply for years.

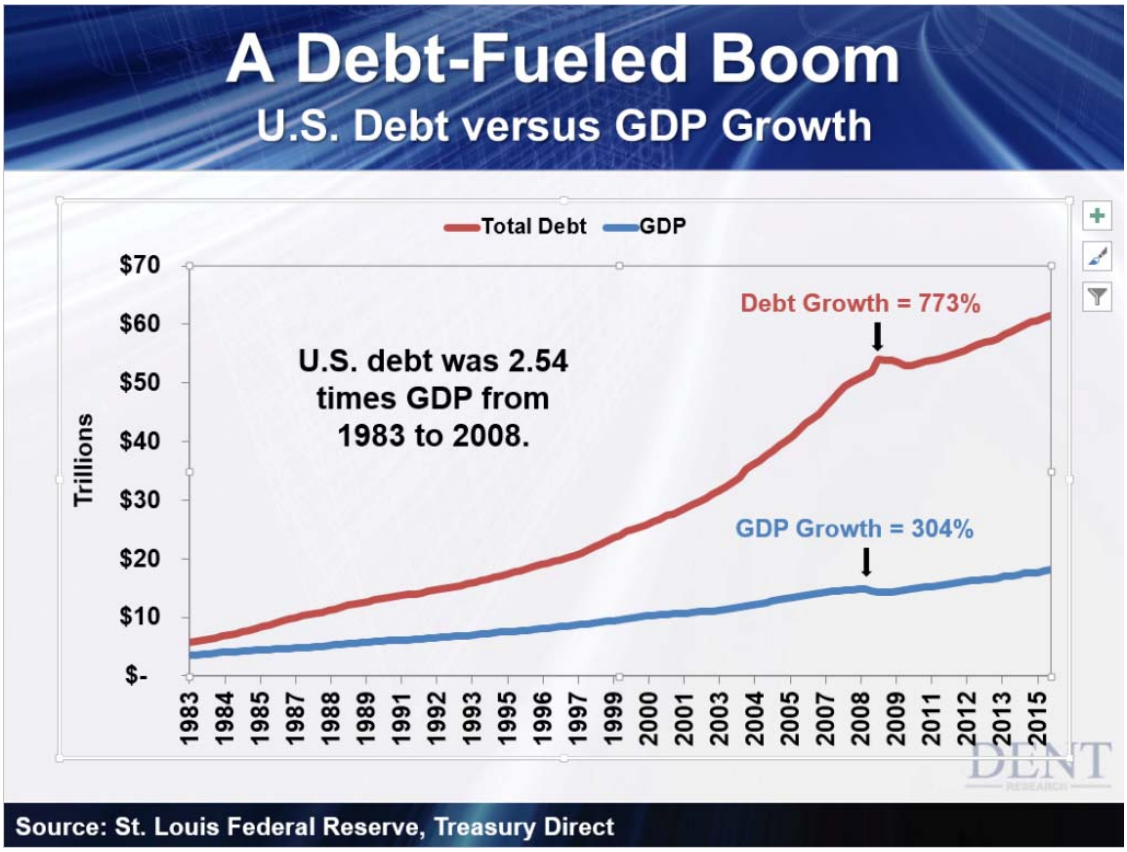
And all of that means… we're not even *at capacity* for all this overbuilt real estate.

Folks, this "recovery" isn't working! And no one has expected it to, given the over-expansion in the greatest debt bubble in U.S. history from 1983 to 2008.

Inflation hasn't risen due to excess capacity here and around the world, especially China…

Money velocity continues to drop without lending and productive investment to expand it…

Businesses are struggling with stagnant earnings because we already hit the peak of debt capacity and demographic spending growth in the great boom that finally peaked in late 2007, as I forecast two decades before.



Debt was running at 2.54 times GDP for 26 years. It doesn't take a rocket scientist or nuclear physicist to tell you that pretty much guarantees a massive period of deleveraging and depression – *not* continued expansion.

So since growth is all but impossible, corporations have resorted to financial engineering to keep the wagon rolling – all courtesy of the Fed, with near-zero short- and long-term interest rates.

They've had two options: either increase stock buybacks to leverage their stagnant earnings with rising earnings-per-share on fewer shares, or increase dividends to compete with lower and lower yielding bonds (also courtesy of the Fed). And they've been milking both options for all they're worth!

But financial engineering does not result in real growth.

And speculation does not expand the money supply.

It is only a sign of decreasing money velocity, and a bubble that will only burst – like in 1929, 2000, and now again!

It's a mirage.

It isn't real.

And it isn't sustainable.

Despite such endless financial engineering, sales for the S&P 500 have been declining for the last three quarters. And profits have declined for the first time since the 2009 expansion.

I'd be surprised if both didn't continue down in the 4th quarter.

This will end badly… which is the only way bubbles end.

My forecast today: the stock market will start to crash by early February, if not sooner, when it gets this clear realization.

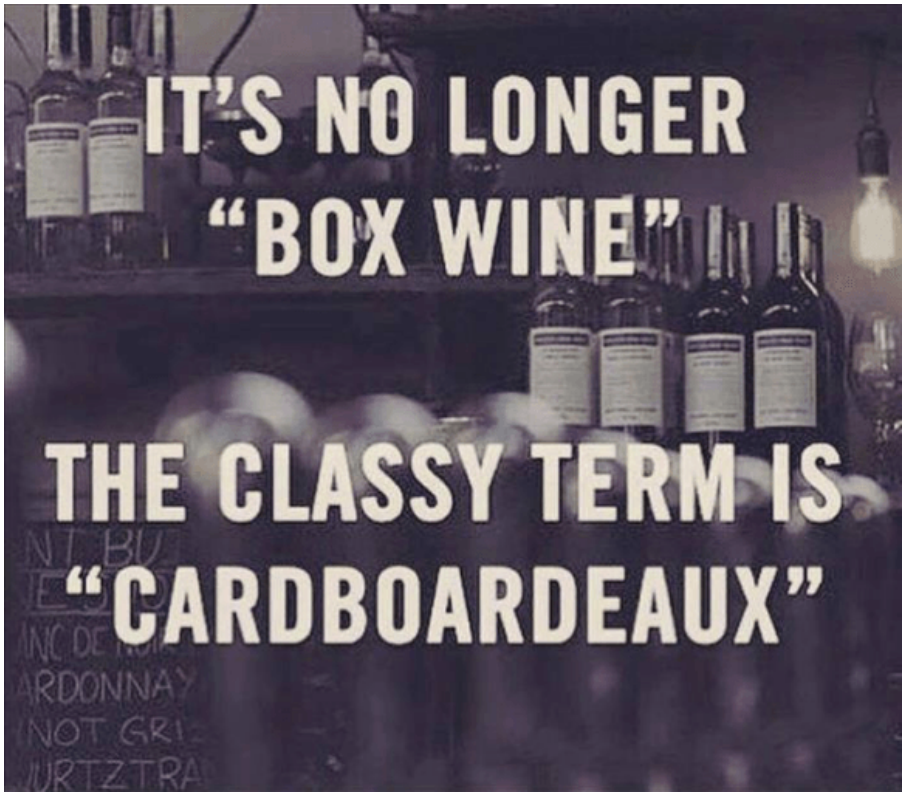
HOW ELECTRIC CARS WORK


IF YOU'RE COLD, THEY'RE COLD TOO.
BRING THEM INSIDE AND WARM THEM UP


THE FORK IS STRONG
WITH THIS ONE

DIET DAY 1 :

I HAVE REMOVED ALL THE BAD FOOD FROM THE HOUSE. IT WAS DELICIOUS.


IT'S NO LONGER
"BOX WINE"
THE CLASSY TERM IS
"CARDBOARDEAUX"


Dr. A Hedgeh
51
WARNING:
To whoever keeps adding
"og" to my doorsign,
if I catch you,
you are dead.
Dr. A Hedgeh