

Jean-Marie Eveillard: The Chances of a Debacle are Zero...Approximately

Robert Huebscher
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Legendary value investor Jean-Marie Eveillard was one of the featured panelists at this year's Schwab Impact conference in Atlanta, GA. Eveillard, portfolio manager for the Global, Overseas, Gold, U.S. Value and Overseas Variable Funds at First Eagle Funds, was joined in the session by co-managers Abhay Deshpande and Matthew McLennan. He spoke on September 24, 2008.

Eveillard spoke candidly about the current crisis and its effects on capital markets, saying the seeds were sown by incautious central bankers in the 1980s and 1990s. "The mistakes were made by central bankers in the US and the rest of the world, when they took inflation down," he said. "The lesson that central bankers forgot in the 1980s and 1990s was that a credit bust follows a credit boom, like night follows day." Eveillard did commend bankers for their contribution to world prosperity over the last 25 years, but noted its similarity to the fleeting prosperity of the 1920s.

Now, arresting the credit crisis will be a drawn-out process, he cautioned, as it will rely on the inherently slow process of de-levering.

"Bernanke and Paulson were late in understanding how bad the situation would be, and they probably regret some of the statements they made," Eveillard said. "But today the risk that the system will implode is zilch," adding, after a short pause, "approximately."

Eveillard described the Bear Stearns, Lehman, and AIG outcomes as piecemeal responses, and he warned of "unintended consequences to the very unusual steps" contained in the proposed bailout program. He is most worried about a decline in the US dollar, and warned that "we are not out of the woods" with respect to future dollar devaluation. The defense of the dollar is predicated on the success of the proposed bailout program, he said.

From Eveillard's perspective, three possible solutions to the credit crisis are available to policy markets, but only one makes sense. Eveillard says we should not follow the "Asian solution," when in the late 1980s the international community, led by the IMF, required countries like Thailand, Korea, and



Indonesia to endure several years of painfully slow growth in order to “work off their excesses.” “There is no appetite for that in the US,” says Eveillard.

A second - and equally unpalatable - approach would be to follow the path of Japan, whose real estate bubble in the 1980s exceeded what the US now faces. “The truth is that their housing bubble and credit boom were so big they could not avoid the pain,” he said. “It was good to spread the pain across a decade,” referring to Japan’s “lost decade.”

The US solution, as Eveillard sees it, is “full speed ahead.” He expects to see a “ballooning” of the deficit, and the impact will be delays in funding major infrastructure projects. He said the deficit could rise to \$1 trillion (versus a forecast deficit of \$389 billion for 2008) and that, if the \$700 billion bailout does not succeed, “other steps must be taken.” He expects approval of the bailout package “one way or another,” but recognizes that a one-week timeframe to craft such a massive response is extraordinary, since the RTC bailout took six to seven months to work out.

“Some money will be printed,” said Eveillard, “but it is unlikely the taxpayer will pay the bill,” implying that the overall impact may be felt through future inflation, which, in addition to dollar devaluation, is the other risk facing policy makers. “But if there is inflation, I would rather own stocks than bonds,” he said.

“Prices are down quite a bit in the equities markets, and this is creating opportunities for us,” Eveillard said. He cited specifically the Japanese markets, noting that there are now many companies with half of their market capitalization in cash, along with some that are trading at three- to four-times operating profit. “There are some good businesses already priced for the risk of recession,” he said.

Eveillard holds 5-10% of his funds in gold as a defensive measure and he revealed that he will to continue do so “until the return of sustainable financial stability.”

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