H.S. Grace & Company, Inc.

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FIFTH MID-YEAR REVIEW: WORLD ECONOMIC UPDATE

H.S. Grace & Company, Inc. (HSG) sponsored its fifth annual Mid-Year Economic and Governance Review Breakfast in New York City on September 18, 2013. Acclaimed economist Dr. Robert Aliber, professor emeritus of international economics and finance, University of Chicago Booth School of Business, presented his annual economic update. Dr. Aliber, with Charles P. Kindleberger, is the author of *Manias, Panics, and Crashes: A History of Financial Crises* (Sixth Edition). Following Dr. Aliber, an HSG panel led by Suzanne Gilbert, former Vice Chairman and CFO of Initiative Media Worldwide, discussed "Damage Issues in Complex Commercial Litigation." Set out below is a brief summary of their remarks.

World Economic Outlook – The Andy Warhol Theory of Economic Growth - Every Country Grows Rapidly for Fifteen Years - - or Thirty Years

Dr. Aliber continues to be generally optimistic about prospects for the U.S. economy, but cautioned there may be headwinds on the horizon in the form of increased taxes, decreased government expenditures and Federal Reserve tapering of bond purchases. Dr. Aliber discussed three principle areas in reaching this conclusion: energy, China, and the U.S. economy as a whole.

Energy

The U.S. currently has a unique role in "balancing" oil exports. The oil exporting countries have a trade surplus of $450 billion; Germany, Japan and China import oil but have trade surpluses because of manufacturing exports. The U.S. therefore ends up in the balancing role for oil exports with a deficit since all surpluses must have an offsetting deficit. Increased U.S. oil production, however, is changing this role, and Dr. Aliber predicts that within about 2 years energy prices will fall to the $70-$75 a barrel range.

China

Every country has its 15 minutes of fame. China's growth will follow Japan's trend. In the late 1980's, 7 of the 10 largest banks in the world were Japanese. But the Japanese bubble imploded, and growth slowed significantly over the succeeding years.

China's growth commenced in the 1980's when the Chinese government invited in multinational corporations, which were enticed by low wage rates. Rapid Chinese growth was driven by this demand for jobs with the multinationals and worker migration from the countryside to the cities. As a result, China accumulated massive international reserves with each Chinese citizen essentially owning $3,000 in Treasury bills.

But wage rates in China have surged, and the multinational firms are moving to lower wage and lower cost countries. Chinese exports will grow much more slowly, and the incentive to invest in the cities will decline sharply. The investment in cities currently absorbs 30-40% of the savings in China. With less investment in cities, the real estate bubble will burst, and China will experience a dramatic slowdown. The American concern is that China will seek to increase its exports to the U.S. to compensate for the slowdown in its domestic growth rate.

<u>United States</u>

Anecdotes about the U.S. economy are better than current data. Automobiles and housing drive the U.S. economy. The housing shortage coupled with the 10-20% rise in housing prices in the last year will likely result in an increase in household spending. Banks are flush with cash, and both the U.S. and the global economy continue to have excess capacity, which allows growth in the U.S. in the 4-5% range without significant price increases. Headwinds, however, exist in the form of potential increased taxes, decreased government expenditures, and Federal Reserve tapering of bond purchases.

Dr. Aliber also believes that bond prices are likely to decline in the next 1 to 2 years with increasing interest rates. He views gold's prospects similarly and called gold "an accident waiting to happen." The U.S. stock market continues to have possibilities for increase with business expansion and potential for increased profits, driven by economic factors such as possible job growth of 300,000 (per month) and possible GDP growth in the range of 4-5%.

HSG Panel Discussion – Damage Issues in Complex Commercial Litigation

HSG panel members discussed three real-world complex commercial litigation scenarios in which HSG had been requested to analyze damage issues. The cases were genericized to maintain each case's confidentiality. Discussion emphasized how important it is to look at the underlying business and financial issues and assumptions on which the plaintiff's damage case is based to determine not only whether the damages are overstated, but, equally important, whether there are even any damages at all that were caused by the liability facts alleged.

<u>**Panel Members:**</u>

H. Stephen Grace Jr., Ph.D., President HSG – Over 35 years of experience as consultant, CFO, and university faculty member. Grace is a noted author and speaker on economic and financial issues, with a focus on corporate governance.

Ronald H. Wilcomes, LL.B. - VP and Investment Counsel (Ret.), MetLife Insurance Co.

Steven B. Lilien, Ph.D. - Weinstein Professor of Accounting, Director of Center for Financial Integrity, Baruch College

Sheryl L. Hopkins, J.D., MBA - Former Practicing Attorney, Akin Gump, Vinson & Elkins, Locke Lord (f/k/a Locke Purnell) and Gordon Arata (Management Committee)

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Representative Issues Examined

- Lender Liability
- D&O
- Corporate Split-off
- Family Trust
- Health Care
- Professional Services
- Intellectual Property
- International Structured Finance Transaction
- Fraud
- Pension Fund Investments
- SEC White Collar Defense
- Stock Option Backdating
- Oil & Gas
- Real Estate
- Fiduciary Issues
- Contract Dispute
- Fund Management
- Market Timing Allegations
- Financial Derivatives
- Portfolio Management
- Special Purpose Corporation

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