



The Privateer

2012 Volume - Mid February Issue - Number 697

THE PRIVATEER:

The Private Market Letter
For The Individual Capitalist.

Published since October 1984.
25 issues per year
© 2012 - All Rights Reserved

PUBLISHER:

William A. M. Buckler
P.O. Box 2004
Noosa Heads, Qld. 4567
Australia

<http://www.the-privateer.com>
capt@the-privateer.com

Phone: +61 7 5471 1960

ABN: 99 805 118 934
(Australian Business Number)

COPYRIGHT:

Reproduction in any manner
without permission is a breach
of law and property rights.

Permission given to quote
SHORT excerpts - provided
attribution is given - as follows:

© 2012 - The Privateer
<http://www.the-privateer.com>
capt@the-privateer.com
(reproduced with permission)

SUBSCRIPTIONS:

In AUSTRALIAN Dollars

Trial: 5 issues (once only) \$A 25
Six-Month: 12 issues \$A 100
Annual: 25 issues \$A 180
Two-Year: 50 issues \$A 300

**Australian residents: Please
add 10% for GST**

Subscribe at our website:
www.the-privateer.com/sub.html

GLOBAL REPORT

SPEAKING IN A DEAD LANGUAGE

Have you ever noticed that amongst people who do a reasonable amount of travelling, there is one linguistic group which stands out? We refer to people whose native (and very often only) language is English. In Europe especially but also in other non English speaking parts of the world, those who get “out and about” are almost invariably bi-lingual and often multilingual. But English speakers (including your Captain it must be said) speak their native tongue wherever they go. This is natural enough, but the amusing aspect is that they expect to be understood wherever they go. When visiting a non English speaking country, they have a tendency to simplify and slow their speech down as if addressing a young child or to shout every second word in an attempt to make themselves understood. When that doesn't work, they fall back on the old standby - **“Does anybody here speak English!?”** Almost invariably - someone does.

An amazing number of English speaking people regard all languages except their own as dead languages. But what is much more scary is the number of English speaking people who are doing their best to render their own language into a dead language. Nowhere is this more prominent than in the ranks of politicians, academia, the mainstream media, banking and finance and the investment community. Here, words are used not to communicate but to obfuscate. Fundamentals and basic principles are completely ignored. Any type of rational argument is left in mid air without a connection to the “real world”. And definitions are twisted to the point at which their original referent is entirely lost.

Humpty Dumpty Revisited:

“When I use a word,’ Humpty Dumpty said, ... ‘it means just what I choose it to mean - neither more nor less.’ ‘The question is,’ said Alice, ‘whether you can make words mean so many different things.’

‘The question is,’ said Humpty, ‘which is to be master - that's all.’”

That is a part of the dialogue between Alice and Humpty taken exactly as it was written by Lewis Carroll in *Through The Looking Glass*. It was written in 1871. In that same year, Carl Menger - widely regarded as the “father” of Austrian economics - published his *Principles of Economics*. Mr Carroll's book is a classic of children's literature, continually in print and read and enjoyed by millions of people of all ages. Herr Menger's work is still in print too but it has been read by hardly anyone who “matters” in our modern world of Humpty Dumpty political economy.

Sadly, in our world, Mr Carroll's “principles” as articulated by Humpty have become the guiding lights of “policy” while Herr Menger and the even greater economists who followed him are unknown, ignored or damned with very faint praise. When the issue is which is to be master, dead languages are very useful.

Three Quotes To Illustrate The Point:

The mainstream financial media on the internet provides a bottomless resource for these quotes, but here are three taken at random from one article which appeared on *Bloomberg* on February 8. The title of the article is: *Bernanke Economy Shows Critics Wrong on Fed*.

"I don't see how anybody in their right mind could form a strong argument for persistent, rapid inflation in the US." That's from John Lonski, the chief economist of Moody's Capital Markets Group. *"The criticism about the Fed being inflationary is not fact-based."* That's from Mark Gertler, an economics professor at New York University. *"It just doesn't look like there's any evidence right now. There are no alarm bells going off in terms of the current picture."* That's from Peter Cooper, you guessed it - another "chief economist" - this time at Deutsche Bank Securities Inc.

Imagine the reaction of these "eminent" economists to a doctor who found no evidence of physical trauma while examining them meticulously and blandly ignoring a compound fracture which was pumping blood all over his pristine white coat. Imagine their reaction to an insurance assessor who pronounced their car in perfect shape while omitting the fact that the entire front was missing and the engine was sitting in the back seat. Imagine their reaction to an engineer who praised the design of a dam while happily oblivious to the ten metres of water which was pouring over the top of it.

The language that economists (and politicians) use sounds just like the language that their counterparts in all these other disciplines use. But it isn't, it is replete with words which are either meaningless or which are defined in ways which bear no resemblance to the issue being discussed. "Inflation" - and "deflation" - are but two of them, there are many more.

Dry Streets In A Deluge:

As the old saying among rational economists goes, singling out changes in prices as the "cause" of inflation or deflation is like singling out wet streets as the "cause" of rain. It is a classic case of getting things entirely backward, of putting the cart before the horse, of defining the "cause" as being one of its many effects. It is a very useful procedure if your goal is to hamstring debate on the issue.

There is and always has been only one rational definition of "inflation" - an increase in the total stock of money. Naturally, "deflation" is the exact opposite. This definition has been banned from economic and political discourse for three generations. Had it not been, the continuous inflation of that entire period would have collapsed of its own weight a long time ago. A definition of inflation that focussed on money would have brought forward two other areas of debate. These are - what is money and who has the power to manipulate the stock of money. The answers are clear enough. In our credit-based economy, money is whatever those in power say it is. And those in power have the EXCLUSIVE direct or indirect power to manipulate the quantity of money.

Nobody living in the desert or on the seashore would choose grains of sand as the medium of exchange. Nor would anyone living in the vast open plains of the world choose blades of grass as their money. Having grasped the concept of a medium of exchange, anyone looking around for something to fulfil that function would not choose an economic good which could be procured by anyone without effort and in effectively unlimited quantities. Still less would anyone who DID choose such a medium of exchange assert that it was having no ill effects while watching the beaches stripped and the plains denuded.

Yet that is what modern "chief economists" do when they claim that *"the criticism about the Fed being inflationary is not fact-based."* The sole purpose of the Fed - or any other central bank - is to manipulate the stock of money. That doesn't "cause" inflation - it IS inflation. The Fed can create (or destroy) as many grains of sand or blades of grass as it deems "necessary". It does this continually and in potentially unlimited quantities. The deluge continually intensifies while the streets allegedly remain bone dry.

The Pathetic Nature Of Modern Economic Analysis:

Just over a year ago, in the early morning of February 3, 2011, Cyclone Yasi made landfall on the north Queensland coast of Australia. Mercifully, as far as the Aussie economy is concerned, the storm did not hit any major population centres. The damage, though devastating for those directly affected, was nowhere near what it could have been given the immense power of the storm.

Six weeks later, a huge undersea earthquake took place off the north coast of Japan. The damage from the quake and the much greater damage from the resultant tsunami devastated the nation. To this day, the Japanese government is still passing "supplementary budgets" to cope with the rebuilding effort. The fourth of these, all of them entirely "financed" by borrowing, was announced in early February this year.

Over the past decade, the US government has thrown away countless lives and destroyed the equivalent of \$US TRILLIONS worth of economic goods in its fruitless and entirely counterproductive wars in Iraq and Afghanistan. In the process, the US has turned itself into an international pariah, seen in most places around the world as the nation whose policies pose the single greatest threat to peace.

All of these disasters (and there have been many others), both natural and man-made, have been greeted by "economists" in a most singular manner. The rubble must be cleared. The shattered infrastructure must be made good. The devastated buildings must be reconstructed or restored. And while all this is going on, the people who have lost everything must be fed, clothed, housed and reassured that life goes on. A man whose house has burned down does not rejoice in the time, effort and money it costs him to replace it. While he is at this task, he cannot do any of the other things he planned to do. When he is finished, he once more has a house but he does NOT have any of the time, effort and money expended in the process of replacing the one he lost. These are irretrievably gone and he is poorer for their passing.

Yet when "economists" look at this process, they see a boost to what is called the "economy". They see the man fully employed. They see the new money borrowed into existence when he goes to the bank to get the loan to buy the materials. They see the increasing "demand" for goods which this new money makes possible. They see the production of the goods he needs for reconstruction. When the devastation encompasses a town or a city or a large part of an entire nation, they see a huge surge in what they call "growth". They plug all this "new" activity into their computers and come up with a series of numbers which purport to prove that devastation is the greatest boon to prosperity. Nearly two centuries ago, Frederic Bastiat called this the "broken window fallacy". Today, it remains the core of mainstream economic "analysis" and a potent contributor to the spectacle of economists speaking a dead language.

Moving The Goal Posts:

To have any utility at all, the process of measurement must begin with EXACT definitions of the units of measurement. Even more important, once these units of measurement are defined, they cannot change in the smallest degree. The more critical the measurement, the more rigid must be the unit of measurement.

Leaving aside the obvious fact that volitional action is fundamentally different from the action of inanimate objects and thus not subject to measurement, look at the way economists claim to "measure" economic activity. The most hilarious case in point in this regard is the January 2012 employment number recently released by the US Bureau of Labour Statistics (BLS). The raw number, greeted with awe and delighted wonderment by markets worldwide, came in at 8.3 percent - from 8.5 percent the previous month. To derive this number, the BLS counted the number of US "jobs", discovered that it had contracted by almost two million in December/January, and somehow concluded that unemployment was falling. Their methods for reaching this conclusion are a closely guarded secret. It is known, however, that had they employed the methods they used three decades ago, their result would be almost triple the headline figure. If the science of mathematics, which uses measurement as a starting point, was practised in such a fashion, the entire achievement of the physical sciences would vanish in a puff of smoke.

“Measuring” Prices:

The crowning glory of all the attempts to put an impenetrable barrier between perception and reality is the government and the economists’ obsession with “measuring” prices and deriving from them a picture of the economy. In our everyday affairs, we never “measure” prices, we simply compare them and decide which ones we want to pay and which ones we don’t want to pay. But when it is “measuring” the size and health of an economy, a government and its economists never bother with such a messy concept as an “exchange”. They simply take the prices of the goods and services in the economy, add them together, and come up with the “size” of the economy. That’s the size measured in terms of money of course, because money as the medium of exchange is the one constant which forms all price ratios.

By this method, the economists come up with the statement that the “size” of the US economy is a bit more than \$US 15 TRILLION. If it is “growing”, then the sum of all the prices is getting bigger. If it is shrinking, the reverse is taking place. In a normal economy - one in which money is not continually being created out of thin air - the tendency is for prices to FALL. But the US has not seen a “normal” economy since the years between the Civil War and WW I. Ever since then, prices have constantly risen. The reason for this is not hard to discover. It is that the common denominator of all prices - money - has increased in quantity far more quickly than any of the economic goods for which it is exchanged.

Looked at in this way, the “measurement” of economic growth which is the Gross Domestic Product or GDP does not measure the increase in real wealth, it measures the increase in money and the resultant loss of purchasing power of the monetary unit. Sometimes that loss of purchasing power is reflected in the prices of real goods and services. Sometimes it is reflected in the prices of what are called “financial assets”. But it is always there. Economists have made it the “measure” of wealth. It is in reality precisely the opposite. It is a measure of capital CONSUMPTION. In a normal economy where economic growth is stimulated by a combination of savings and investment, the resultant increase in real wealth is reflected in a LOWER price structure. The purchasing power of money is rising as new, better and more efficient methods of producing economic goods are being discovered and financed. But to our modern “economists”, falling prices are “deflation”, a fate to be avoided at all costs.

Higher Prices Are Bad Enough:

What is worse, far worse, are FALSE prices. Money - as legal tender - is the exclusive monopoly of the government. Its composition has long ceased to be an issue as far as modern economics is concerned. Its quantity is the only issue, and as far as they are concerned, the more the better. Interest rates are largely, though not completely, controlled by the government’s central banks. Their utility in reflecting the future expectations of borrowers and lenders has long ceased to be an issue as far as modern economics is concerned. What matters to them is that interest rates constantly and to the greatest extent possible induce ever increasing borrowing and consumption. Again going back to a normal economy, economic growth in it is reflected by the amount of production, savings and investment. In our modern economy, it is measured by the amount of consumption, indebtedness and government spending.

In order that this diabolical reverse image of a normal economy can be made to function at all, prices must be systematically falsified. If you look at the history of the cancerous growth of government rules and regulations in the economy since WW I, you will find that the vast majority have as their goal the falsification of prices. This is made necessary by the way in which government and central bank fuelled inflation (remember - an increase in the total stock of money) works. The increased quantity of money produced by government policy does not enter the economy in one huge chunk, it enters it in stages. The first recipients are the borrowers - the government being by far the largest of these. From there the new money goes to the government’s favourite “clients”. From there it filters slowly but surely through the entire economy. The first recipients of the new money do not face higher prices. The last ones, the wage and salary earners and those on fixed incomes, don’t see the new money until prices have already risen. To obscure the reason WHY prices have risen, the prices are falsified.

Where Everything Comes Together - The “Markets”:

The falsification of prices in general is seen by both the powers that be and the economists who clothe their policies in a pseudo-scientific haze as being absolutely necessary. If the constant lowering of the purchasing power of money which their intervention makes necessary was fully reflected in the cost of essential goods and services, there would long since have been hell to pay. Where it is no longer possible to prevent this - there IS hell to pay. The US got a small taste of this phenomenon in the 1970s. Latin America has borne the full brunt of it several times since then. And then there were instances when the whole thing got totally out of hand - as in Germany in the early 1920s. More recently, while the rest of the world was resorting to HUGE dollops of price falsification in the crisis of 2008 - early 2009, the government of Zimbabwe lost the plot completely and their money became confetti.

There are many ways to falsify the prices of goods and services. Government subsidies to both the producers and the consumers help. So do price controls, minimum wages and outright government grants of all descriptions. But in more recent times, and especially since the last global bout of escalating prices for real goods and services ended in the early 1980s, the preferred method has been to “siphon off” the majority of the new money being borrowed into existence into the so-called “financial asset” markets.

Between 1982 and 2000 in the US - inflation was said to be a dead issue. It was a dead issue because the prices of goods and services were not rising, or were rising very gradually indeed in comparison to the 1970s. But “other” prices were soaring. To take just one example, the Dow rose 1411 percent from 776 in August 1982 to 11723 in January 2000. The Fed and the economics profession watched this entire almost two-decade episode with happy and complacent unconcern. Not one point of this rise was deemed to be inflation or even the result of inflation. All of it was deemed to be a faithful reflection of the increasing wealth of the American nation.

It took almost 40 years of rigid “price control” followed by a 150 percent increase in US government debt (the foundation for the US Dollar) to boost the “price” of Gold by 2329 percent from \$US 35 to \$US 850 per ounce between 1971 and 1980. It took a 500 percent increase in US government debt to boost the Dow by a bit more than half as much in percentage terms in double the time between 1982 and 2000. The first price rise was looked upon as the epitome of “inflation”. The second was held to have nothing whatsoever to do with “inflation”. In reality, the fuel for both was exactly the same.

Since 2000? Well, Gold at its February 15 level of \$US 1730 is up 530 percent. On January 14, 2012, the Dow closed at 12422. That’s up 6.0 percent from its level exactly 12 years earlier. Is inflation back? Not according to the economists. But in reality, it has never gone away, it has just intensified.

Dead Languages Cannot Be Revived:

A language can die for a lot of reasons. The number of people who use it can fall below the level which is necessary for its continuation. The language itself can fail to deal with the widening concepts and discoveries which constitute knowledge and which require new and more precise terms to describe them. New generations can discover that a different language is better suited to convey thoughts and attitudes which their “mother tongue” just cannot handle.

Whatever the language may be, it prospers or suffers in direct proportion to the precision and universal understanding of its definitions. When a concerted effort is made to destroy both of these things, the language is in trouble. The “language” of economics has been debased in precisely this fashion for many decades. Not only is its money “elastic”, so are its concepts. Today, both have been stretched so far out of shape that neither is capable of doing the job they claim for themselves.

Mainstream economists are speaking a dead language. So are those who rely on them as a buffer between themselves and reality. The sooner this anti-discipline is given a decent burial the better - for all of us.

INSIDE THE UNITED STATES

NO FACTS - ALL CONFUSION

If you didn't know that 2012 was a presidential election year in the US, a swift glance at the daily avalanche of economic "news" would quickly bring you up to speed. Everywhere you look, the "party line" is that the economy is REALLY on the mend this time. Even Ben Bernanke's dour warnings about the less than ideal state of US employment and real estate hasn't damped the bubbling up of animal spirits. The problem is that these spirits are confined to the incumbent politicians, the mainstream financial media and the markets. They have most definitely not filtered down to the American public. With every day that passes, the contradiction becomes more acute. While the "press" regales us with upbeat news, most of their dwindling number of readers are doing a slow burn as the TRUE state of affairs gradually becomes clearer. In a very large part, they have Ron Paul to thank for that.

Late last year, when the US markets were once again poised to turn upward, the November 2011 US retail sales figures came in vastly below "expectations". That was followed by the December 2011 figures which were also alarmingly low given the time of year. Having reported the sales figures, the next step was to discover how US consumers managed to buy what they did buy. In early February, the consumer credit numbers for December came out. They showed the third biggest month on month increase in 18 years. The second biggest was in the preceding month. The biggest of all was in October 2007, which just happened to be the month when US stock markets hit what is still their all time high.

Shortly after that, the "unadjusted" retail figures for January 2012 came out. They showed the biggest "sequential" plunge in the history of the data. December retail sales totalled \$US 460 Billion. January retail sales plunged to \$US 361.4 Billion. That's almost \$US 100 Billion or nearly 22 percent. Don't forget in this context that the official 2.8 percent "growth" figure for the US economy for the fourth quarter of 2011 was almost entirely made up of a surge in business inventory. No sooner has US business finished restocking their shelves than consumer spending takes a spectacular tumble.

Another \$US TRILLION Plus Budget:

On February 13, President Obama rolled out his "budget" for fiscal 2013. The budget itself totalled \$US 3.8 TRILLION - \$US 12,150 for every man, woman and child in the US. The "\$US TRILLION plus" in the headline refers to the projected deficit. In fiscal 2013, which starts just over a month before the November elections, the deficit is forecast to be \$US 1.33 TRILLION. That will be the fourth straight annual \$US 1 TRILLION plus deficit. The Fed instituted their Zero Interest Rate Policy (ZIRP) in December 2008 - seeing the certain prospect that the US government would soon be embarking on the first of its \$US TRILLION plus budget deficits. That was supposed to be a "one off" event to save the system from the September/October *Lehman* debacle. Clearly, it was not - and there is no end in sight.

Mr Obama's budget and the heroic assumptions which were used to get the most palatable result possible have been under fire ever since he announced it. On February 16, Treasury Secretary Geithner was up in front of the (Republican controlled) House Budget Committee to do his bit to further confuse the issue as much as possible. Predictably enough, it was pointed out to him that the US was heading straight for a "Greek" - or at best a "European" - situation. Mr Geithner passed this off as overheated rhetoric. Echoing the comments made earlier by Fed chairman Bernanke, Mr Geithner scornfully dismissed any talk of "austerity" in a US context. Any steps in that direction would **"kill this economy"**, he said.

Mr Bernanke has promised to keep his ZIRP policy in tact well beyond his present tenure as Fed chairman, a good trick indeed. The Fed has been reported to be "buying" up to 91 percent of longer-term debt issued by the Treasury since the start of "operation twist" last September. *"We enjoy enormous confidence around the world"*, intoned Mr Geithner, *"you can see it in the prices of US financial assets."* That is the only place where it can still be seen - thanks to Mr Bernanke and Mr Geithner.

INSIDE JAPAN

THE WORLD'S FOURTH BIGGEST ECONOMY

If one looks at the various nations in the European Union (EU) as states, the Union as a whole is the world's largest economy. After the EU comes the US. And after the US comes China and then Japan as the world's third and fourth biggest economies. From 1968 until late 2010 the Japanese economy was the second biggest single nation economy in the world. Now, that mantle has passed to China.

Japan rose to the second ranking in 1968 when the flow of manufactured goods it had begun to export to the rest of the world in the 1950s began its exponential rise. Twenty years later at the end of the 1980s, the grounds of the Imperial Palace in Tokyo were famously estimated to be worth more than the entire State of California. Predictions were rife that Japanese economic "growth" was unstoppable and that it was only a matter of time until Japan overtook the US. Then came 1990 and one of the biggest boom to bust spectacles in modern history as Japanese valuations collapsed right across the board. Today, Japan is well into its third "lost decade" with its stock market more than 75 percent below where it was at the end of 1989 and its sovereign debt by far the biggest in the world as a percentage of "GDP".

The Recalcitrant Yen:

The Japanese government made three HUGE mistakes. First, they accepted IOUs - mainly in the form of US Dollars - in exchange for their exports. Second, like every other nation, they used these IOUs as the reserves behind their own currency, the Yen. Third, they twisted their economy all out of shape in continuous and ever more desperate attempts to prevent the Yen from rising against the US Dollar. Of all the failures of Japanese fiscal and financial policy of the past two decades, this last is the biggest one.

In the early 1970s, one US Dollar would buy 360 Japanese Yen. Late in 2011, one US Dollar would buy just over 75 Japanese Yen. This "shouldn't" have happened. After all, Japan more or less invented the modern "carry trade" by maintaining what have long been the world's lowest official interest rates. The Bank of Japan's official rate has not been above the 1.0 percent level since 1995. Today, it is the only official rate below the Fed funds rate. Japan's official rates are 0.00-0.10 percent.

For decades, Japan's interest rates have been the delight of every major bank and currency trader in the world. The demand for Yen has been insatiable because the arbitrage profit from borrowing Yen and using the proceeds to buy "assets" denominated in higher yielding currencies has been irresistible. But borrowing Yen and selling them for other currencies to take advantage of the higher rates puts downward pressure on the Yen, right? Right. The problem is that the arbitrage opportunities are so great when the usual leverage is involved that "carry traders" are skittish and exit their trades en masse at the first hint of global financial headwinds. That exit puts HUGE upward pressure on the Yen. The classic example is the Yen surge in late 2008 - early 2009 against a US Dollar soaring against all other currencies.

Over the years, and especially since the mid 1990s, global financial headwinds have been a regular occurrence. Every time one hits, the Yen soars. Each time the "crisis" is met with a new dollop of global credit money creation, the Yen stabilises again - at a higher level than the last "stabilisation" period.

The other contributing factor to the Yen's strength is the Japanese people themselves. On a per capita basis, funded Japanese sovereign debt is higher than its US equivalent. But almost all of this debt paper is owned by the Japanese themselves. It is not subject to "normal" market pressures.

The Japanese government has been employing what is politely called "stealth intervention" ever since the Yen hit its post WWII high late last year. Demand for what it produces is falling everywhere and its currency is steadily impoverishing its productive sector. Japan's curse is that its rise to global economic prominence has coincided almost exactly with the fiat currency era. No nation has paid a higher price.

INSIDE THE EUROPEAN UNION

WE'LL CROSS THAT BRIDGE WHEN WE COME TO IT

If you have been following the news coming out of Europe - and it is difficult not to if you follow the news at all - you will have noticed that the FINAL big “crisis meeting” which is to be held to FINALLY deal with the Greek “problem” keeps being put off. If we merely take the last two weeks into account, it has been a succession of postponed “summit” meetings. There was to have been a meeting of European finance ministers to thrash out a “deal” on February 6. It was postponed. The absolute deadline to implement the Greek debt “swap” and impose a large haircut on private holders of Greek sovereign debt was put at February 13. That was postponed too.

Then another meeting of European finance ministers was scheduled for February 15. At this meeting, the “troika” (European Union - EU, European Central Bank - ECB, International Monetary Fund - IMF) which is supposed to be cobbling together the latest bailout package wanted “assurances”. In particular, they wanted signed statements from ALL Greek political parties that they would go along in total with whatever the “troika” came up with as conditions for the bailout. One of the conditions being considered was to put the funds in an “escrow” account to keep the money out of the hands of the Greek government and to make sure that it went to debt servicing and was not gobbled up in “general revenues”.

This provision in particular is being greeted by all sides (and there are many) of Greek politics as an outrage. Even in their most “ruthless” days of bailing out wayward developing nations, the IMF never stooped as low as this. That is the message coming out anyway.

The latest plan being bandied about is to delay at least part of the bailout funds until AFTER the Greek elections which are scheduled for April. The problem with this approach is that the absolute deadline for the Greeks to get their bailout money has long been put at March 20. That is the day when the government has to pay back 14.5 Billion Euros to its bond holders. The Greeks can't just roll the debt over because the markets won't touch it. They can't simply get their central bank to print up the funds because the central bank isn't in Greece. They can't devalue their currency because they have no control over it. They have NONE of the means which governments all over the world have been using for years to roll over their ever increasing pile of sovereign debt. The Greeks are poised in front of the bridge and watching it disintegrate before their eyes.

A “Troika” At Cross Purposes:

As already stated, the “troika” which has supposedly got together to craft the latest bailout plan is composed of the EU, the ECB and the IMF. The EU is composed of twenty-seven European nations. A gathering of twenty-seven nations cannot even agree on the weather, as the United Nations has been industriously illustrating for decades. The ECB has so far been intent on recapitalising the European banking system. The furthest it will move towards a Greek sovereign debt monetisation (the ubiquitous QE) is to agree to forego the “profits” on Greek debt paper it already holds and “bought” at a 22 percent discount some years ago. And then there is the IMF, which wants in on the Greek bailout and also wants its coffers increased to the tune of about \$500 Billion by the rest of the world so it can stay in the “game”.

The IMF is, in essence, a US institution. It is based in Washington DC. Its birth coincides with the elevation of the US Dollar to sole reserve currency status after WW II. Most important of all, the US not only holds by far the highest “quota” of votes within the organisation, it is also the ONLY single nation which can veto ANY IMF decision by itself. Right now, BOTH sides of US politics are dead set against two things. They are against contributing anything to the IMF's request for an extra \$US 500 Billion. They are much more vehemently against the IMF participating in any way in any European bailout.

The “markets” assume that a bailout will happen. It probably will - and that will make things worse.

AUSTRALIAN REPORT

THE WORLD'S FIRST REDUNDANT CENTRAL BANK?

If Ron Paul has been reading the financial press coming out of Australia in recent days, we imagine he would be quite startled. All of a sudden, the Aussie central bank - the Reserve Bank of Australia (RBA) - has been labelled as “redundant”, “irrelevant” or just plain “ineffectual”.

The background is very simple. The RBA lowered their official rates in two 0.25 percent steps (from 4.75 to 4.25 percent) in its last two official meetings of 2011. As 2012 dawned, the expectation both inside and outside Australia was universal that the RBA would do it again when it met on February 10. The RBA duly met on February 10 and, to the shock and outrage of the entire Australian investment community and most Aussie “consumers”, left their official rates steady at 4.25 percent.

No sooner had the outcry over this move reached its crescendo, than an even more unexpected event occurred. One by one, the “big four” too big to fail Aussie banks began to announce INCREASES to their variable mortgage rates. These increases were very minor, ranging from 0.06 to just over 0.10 percent, but the outrage was out of all proportion to their size. After all, everybody “knows” that it is the function of a central bank to take the lead and have the commercial banks they “regulate” meekly follow along behind. When the central bank raises rates (they actually do that sometimes), the commercial banks are supposed to raise too. When the central bank lowers rates, the commercial banks are supposed to fall all over themselves to fall in behind.

Simon Says For “Grownups”:

If you remember the old game of “Simon Says”, you will have a good handle on the conventional relationship between the central bank and its commercial “clients”. The game is pretty simple. One player is designated to be “Simon”. He then issues a string of instructions to the other players. If he prefaces an instruction with the words “Simon Says”, the players MUST do what he says. If he does not, the players must NOT follow his instructions. If they get it wrong in either case, they are out of the game. The game continues until there is only one player left. He becomes the new “Simon”.

Any state functionary is very good at “Simon Says”. We are willing to bet that Ben Bernanke was a whiz!

Metaphorically speaking, governor Glenn Stevens forgot to say “Simon Says” when the RBA announced their decision not to cut official interest rates on February 10. Again metaphorically speaking, the Aussie banks immediately decided they didn't have to follow his lead and raised their rates, albeit by minuscule amounts. All of this has left the local financial community in a dither. Aussie Treasurer Wayne Swan is assuring everyone that the government doesn't have an interest rate “policy”. The Australian Greens, the party which holds the balance of power in the Senate, is urging a return to the 1970s when the government DID regulate interest rates. They also fixed the Aussie Dollar to its US counterpart. Mr Swan is denying any government plans in this direction. Meanwhile, he is urging Aussie mortgage holders to abandon the big banks for their smaller counterparts. The only problem here is that many of the smaller Aussie banks have already raised their rates even more than the big banks have done.

Yes - There Is A Debt Problem:

The situation is redolent of a nation mired in debt. Australia has been pointed to as THE developed nation which has not let its sovereign debt get out of hand, though it has been rising rapidly for several years now. It is true that Aussie government debt is comparatively low by global standards. The same cannot be said of Australian corporate and consumer/household debt which is the highest in the developed world and has been since 2007 and the start of the GFC. The RBA can't do anything about that - except RAISE interest rates. If it did that, being called “redundant” would be the least of its worries.

THE GLOBAL MARKET REPORT

LET'S GO FOR BROKE!

Over the week ending on February 17, stock markets in Asia as a whole completed their ninth straight week of rises - a string reaching back into late 2011. In Europe, the German Dax closed at 6848. That's a rise of 16.1 percent since the start of 2012 and a whopping 32.6 percent since the lows of late September 2011. In the US, the Nasdaq reached an eleven year high and the Dow ended the week closer to 13,000 than it has been since late May 2008. On February 17, the Dow closed at 12950 - up just over 6.0 percent on the year. The Dow hit its "Lehman low" on March 9, 2009 when it closed at 6547. A doubling of that low would require a close of 13094 - less than 150 points above the Dow's current level.

Earlier this year, the Fed blandly announced that under its "operation twist" it had been and was continuing to buy up to 90 percent of all the long-dated paper being issued by the US Treasury. In December 2011, the ECB announced a huge increase - more than 500 Billion Euros - in its bank recapitalisation. The money was "lent" to the banks at a fixed rate of 0.50 percent for three years. The ECB is now poised to offer a second "tranche" of these funds - at the same terms as the first "tranche" - on February 29. According to the head of the European Banking Authority, Andrea Enria - this massive injection of "liquidity" is going well. Mr Enria must be watching the German market.

The US government raised its Treasury's debt limit in three stages by a total of \$US 2.1 TRILLION between August 2011 and late January 2012. On the current borrowing trajectory of the US government, the current limit of \$US 16.394 TRILLION will be hit sometime around September this year - two months BEFORE the election. The \$US 2.1 TRILLION will have lasted just over a year. In the UK, the Bank of England is still pumping under its QE program. In Japan, the Bank of Japan is doing the same. Anywhere and everywhere one looks, an ocean of new "money" is being pumped into the system.

The Greek "Glitch":

Cast your mind back to the first half of 2007. In the US, Fed Chairman Bernanke was telling his colleagues that the sub prime mess was "grave but largely contained". Meanwhile, at the White House, President Bush was echoing his predecessor. When the first signs of the Asian Crisis of the late 1990s began to emerge, President Clinton called it a "glitch in the road". Mr Bush used the same phrase to describe the sub prime situation in 2007. Fast forward to the new potential financial crisis, this time in Europe. As far as the global markets are concerned, this is yet one more in the long line of "glitches".

The Asian crisis was not allowed to derail the global financial system. It was "fixed" by throwing a huge amount of money at it. The result was the "tech wreck" of 2000-2002. The sub prime mess in the US was not allowed to derail the global financial system. It was "fixed" by so much money that it made the Asian crisis bailouts look like a shower of loose change. The result was the global stock market swoon of late 2008 - early 2009. That one was "fixed" by trotting out the financial "nuclear option", the direct monetisation of sovereign debt by central banks which came to be known as "Quantitative Easing" (QE).

The current crisis is a sovereign debt crisis. This one is focussed on Greece and has a publicised deadline of March 20 - just over a month from now. On that date, the Greek government must roll over a "tranche" of debt coming due. The amount of this debt is 14.5 Billion Euros. In the context of the serial reliquification of the global system which has been the recurring theme of the last two decades, this sum is less than a rounding error. It is a sub-atomic particle in the structure of the global system.

That fact, in itself, should be enough to starkly show how fragile the entire system is. When the prospect of a nation being unable to roll over a paltry few Euros of maturing debt is enough to galvanise the entire financial world into monetary excess exceeding anything imaginable as recently as late 2007, one must conclude that the markets are skating on the thinnest ice in their entire existence. But skate they are.

Trading By The Numbers:

The first thing about modern markets, the thing that must never be forgotten, is that most of the “trading” which goes on in them is untouched by human hands - or brains. To an overwhelming extent, modern markets are “automated”. By “automated” we mean that at least eight out of ten (some estimates put the ratio higher) of all transactions are controlled exclusively by means of computers and the programs built into them. The numbers - sourced from government departments or from the central bank - are plugged into the programs and the programmed “actions” are taken.

As many people have pointed out, the process of “reporting” in the mainstream media these days consists largely of taking press releases from various government departments, printing them all but verbatim and calling the result “news”. This is bad enough. The process of trading on mainstream markets today is even worse. A well known quote from the “econometrics” profession goes as follows: ***“Truth is that which fits economic equations.”*** This is a perfect description of computer trading. The equations or “algorithms” are written and incorporated into the trading program. It is the only way that modern trading can function since the complexity and the speed of the calculations necessary are beyond any human brain to process. The problem is this: The human brain thinks - the computer does not.

There are two ways in which human reason enters the picture. The computer programs and algorithms have to be written in the first place. Then, when an event which was NOT taken into account when the program was written hits - and it always does - the programs have to be overridden. The more pervasive that programmed trading becomes, the more disastrous become the instances when the trading equivalent of the “blue screen of death” appears on the monitors.

The Market Assumptions:

First and foremost, whether it is computerised or not, pretty well all trading taking place today is based on the underlying assumption that the debt-based global monetary and financial system is a viable one. No matter how much evidence for a contrary conclusion piles up, the idea that money based on a promise to pay will EVER prove unviable as a medium of exchange is never allowed to enter the picture.

Once that is established, the next assumption is that “risk” is something that can be negated. In the first place, systems can be set up which will yield positive returns no matter what the market does. The assumption here is that the only way not to make money on the market is to be trapped in a market which does not move at all - either up or down. This assumption has taken some hefty hits over the past two decades, none bigger than the 2008-09 collapse, but while it has been shaken, it still remains. That is because of a further assumption. This one is that no matter what happens, the markets like the banks which feed them are “too big to fail”. In any imaginable extremity, they will be bailed out and put right by governments and central banks feeding enough debt-based fuel into them to keep them functioning.

Lastly, there is a convenient assumption upon which debt-based markets have been feeding throughout the fiat money era. This is the assumption that no matter how much inflation there is, it will not be recognised as inflation as long as its effects can be confined to the financial markets and prevented from leaking out into the wider economy. Almost everybody equates inflation with rising prices, but very few equate inflation with market booms. The doubling of the cost of a litre of milk is seen as being inflation. The doubling of a stock or bond or futures or commodity or derivatives index is not. And because it is not, the assumption goes, it will not affect that bane of all money managers and central bankers - “inflationary expectations”. The sad fact is that this is true. Booming markets do not fuel inflationary expectations. That is why so many people are taken completely by surprise when they collapse.

Right now, the assumption is that the paltry 14.5 Billion Euros which Greece must roll over next month will be forthcoming. And after that? The assumption is that there is no limit to the debt-based fuel upon which the markets feed. Just like all its predecessors, 2008-09 was just one more “buying opportunity”.

The Lessons Of The Real World:

Popular delusions are real and so is the madness of crowds. But as President Lincoln said so many years ago - *"you can't fool all of the people all of the time"*. What he didn't say is that most of the time - that isn't necessary - as long as you CAN fool enough of them. On February 9, Mark Hulbert published his latest survey on the attitude of US "insiders" (corporate executives and CEOs) to the markets. He pointed out the ratio between sellers and buyers had reached its highest level since late July 2011 - just before the US government was stripped of its AAA rating by Standard and Poor's. Not only has the ratio of sellers to buyers in this group skyrocketed since late last year, the selling activity has ramped up markedly so far in February. "Insiders" normally rely on their own judgement, not somebody else's.

The other stark contrast between the real world and the world of markets and the banks which feed them shows up starkly in the process of borrowing itself. While Mr Bernanke is promising no-cost loans to the banking system for the next three years, the banks have tightened their criteria for recycling this lending into the real economy to the choke point. This is true in the US and across the world. On February 17, CNNMoney ran a story on US small businesses turning to "riskier financing". They cannot get loans from the banks at any interest rate so they are going elsewhere.

Small business in the US is going to what is called the "cash advance" industry. The lenders here are glad to make the money available, on the condition that they have first claim to a large portion of the revenue generated by the borrower. Typically, they will skim off the first 15 percent or so of every sale the business makes. These cash advances are typically for six months and carry annualised interest rates of between 104 and 177 percent. This is how the REAL world finances itself in the US - and elsewhere.

Recent Events:

The closer we get to the March 20 "deadline date" for Greece, the more confident the markets become. Multi-year highs have been set by stock markets all over the world in the past two weeks. The huge dive in servicing costs for "challenged" European sovereign borrowers which began with the ECBs bank reliquification program in December is holding. In the US, Treasury rates across the board remain near their historic lows. The reaction of the Greek people to the prospect of unending indentured servitude to the global system is being noted - and dismissed.

The attitude on the markets is all but universal: ***"Just bail the bums out and let's get on with it!"***

Gold:

For more on Gold - please see Gold This Week (GTW):
<http://www.the-privateer.com/subs/goldcomm/gold.html>

What's Next?:

The absolute deadline for the Greek "bond swap" was supposed to have been February 13. Clearly, it wasn't. As this issue goes to press, the foreign ministers of the G-20 nations are in the middle of a meeting in Los Cabos, Mexico. The meeting is a preliminary to the Heads of State G-20 summit in June. The public agenda is innocuous. In the background will be the recent request by the IMF to have their bailout "fund" topped up by \$US 500 Billion. The G-20 is the potential source of the vast majority of this money. The US has already said they won't contribute. The other major G-20 nations want more say in the IMF in return for a contribution. The US cannot afford to lose its sole IMF veto.