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Asia – The Coming New Financial Capital of the World

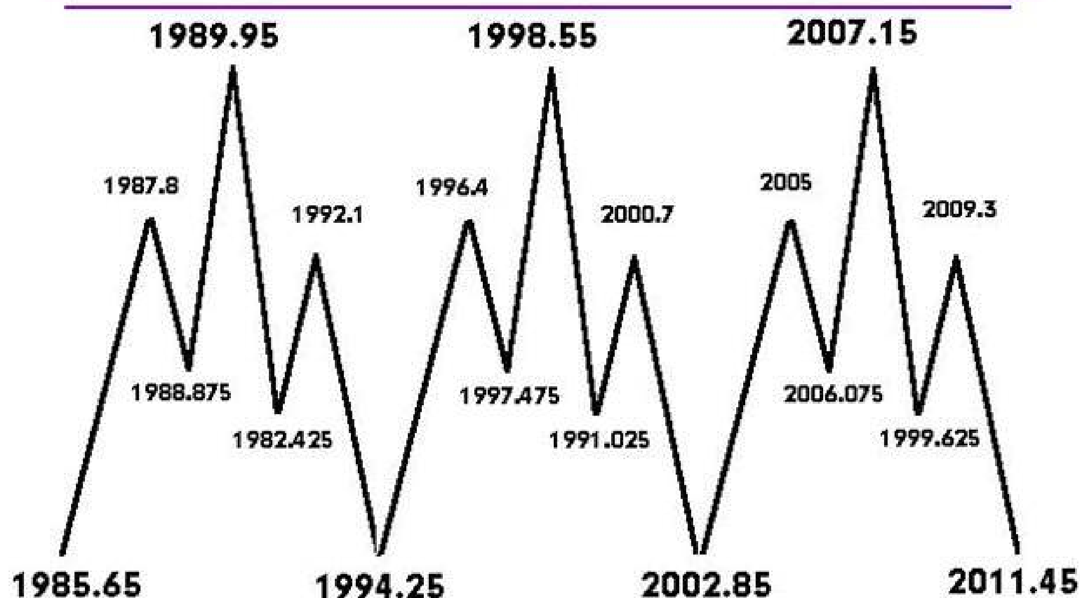
By Martin Armstrong

One of the most stunning achievements of our **Economic Confidence Model** has been its application on a global scale. Here is a chart of the Thailand Share Market with the dated highlighted according to the **Economic Confidence Model**. This is truly the **Global Business Cycle** and its accuracy right to the very day has astounded many. Justin Fox of ***Time Magazine*** wrote on November 30, 2009 ***Riding the Waves of Irrational Behavior.*** He explained that this model ***"made several eerily on-the-mark calls using a formula based on the mathematical constant pi."***

Time Magazine

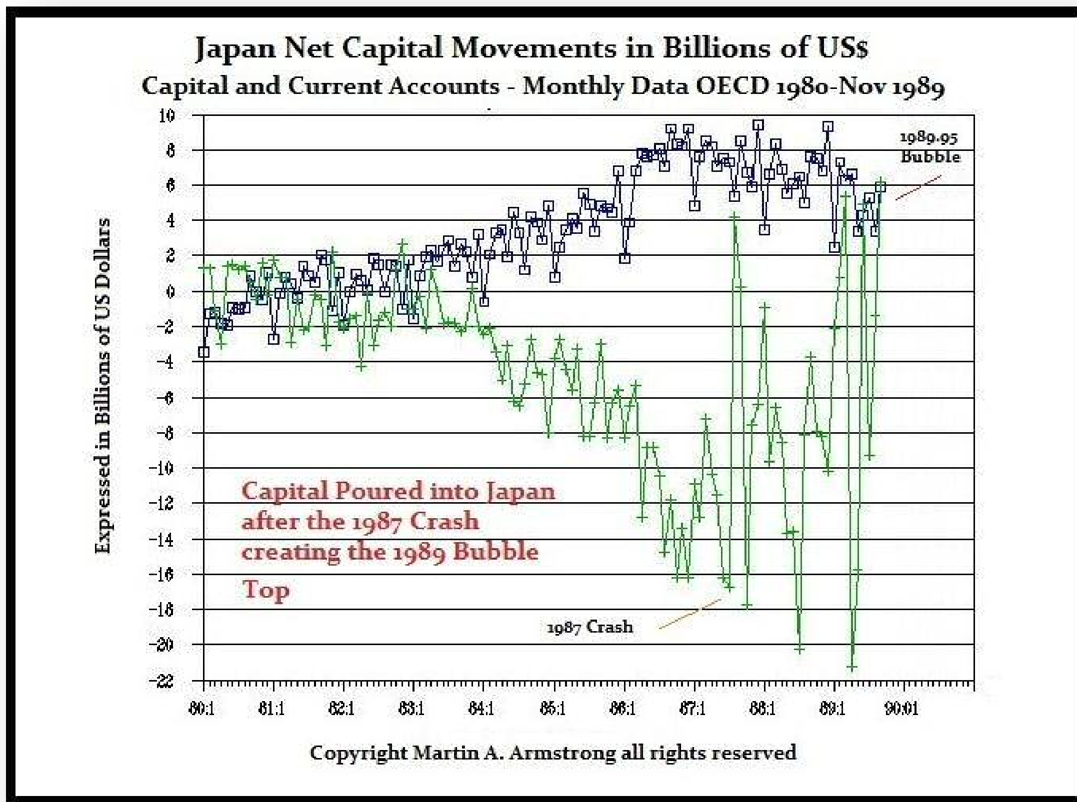
Riding the Waves of Irrational Behavior

By Justin Fox Monday, Nov. 30, 2009

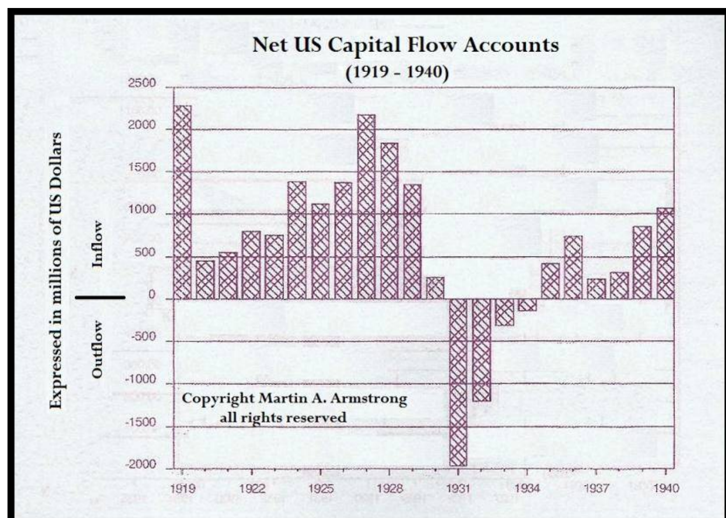


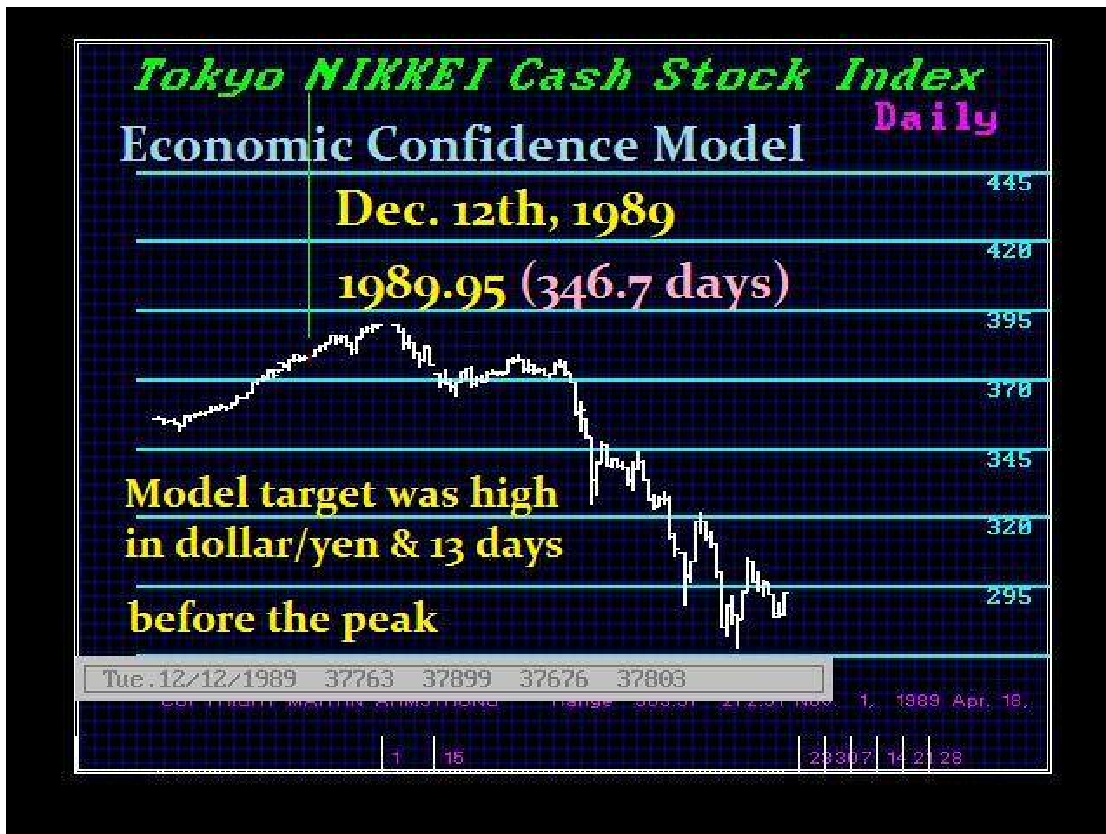
Indeed, by 1983, the Wall Street Journal highlighted me the highest paid financial analyst in the world. I was a frequent contributor to academic journals and often was sought for comment on financial topics. But it was this **Economic Confidence Model** that captured the attention of the elite around the world. The importance of this model is how it has redefined the **Business Cycle** and exposed how capital rushes around the global landscape. Capital always concentrates in a single market that becomes the **"hot"** investment like the Internet going into 2000 or the Railroad during the 19th Century to the new Industrial Age and the Automobile for 1929. However, capital also acts in the same manner on a global scale. Capital concentrates from one nation to the next. The USA became the emerging market for European capital after World War I with the Industrial Revolution creating 1929. Likewise, capital concentrated in the United States going into 1985 when interest rates were at insane levels above 15% attracting capital internationally. This led to the creation of the G5 (now G20) at the **Plaza Accord** in 1985 precisely in line with the **Economic Confidence Model.** That manipulation by Governments was in sync with the model and capital began to leave the United States culminating in the **1987 Crash**. However, that Crash was signaling not a Great Depression as so many analysts predicted, but it highlighted the flight of capital from the US and shifting to Japan to create the 1989 Bubble.

This model became famous for predicting the **1987 Crash** to the day where October 19th proved to be the famous panic and the lowest close. Yet more importantly, that Crash came on the half-cycle. The fact that the **LOWEST CLOSE** unfolded precisely to the day rather than the high, signaled that the low had just been established. The forecasts that were then put out were truly significant that the low made that day would hold and new highs would be seen going into 1989. When virtually every analyst was predicting the next Great Depression, brokerage houses were sponsoring speaking tours for Armstrong worldwide to tell their audiences the market would make new highs not lows. Brokerage houses around the world were now begging me to address their retail audiences since everyone was calling for a Great Depression and with this model it was clear new highs were on the horizon going into 1989. Midland Doherty Financial Corp. of Canada (later Midland Walwyn, then Merrill Lynch) and Bain & Co in Australia were two such firms that assembled audiences of thousands to listen to the fact that this model was predicting new highs.

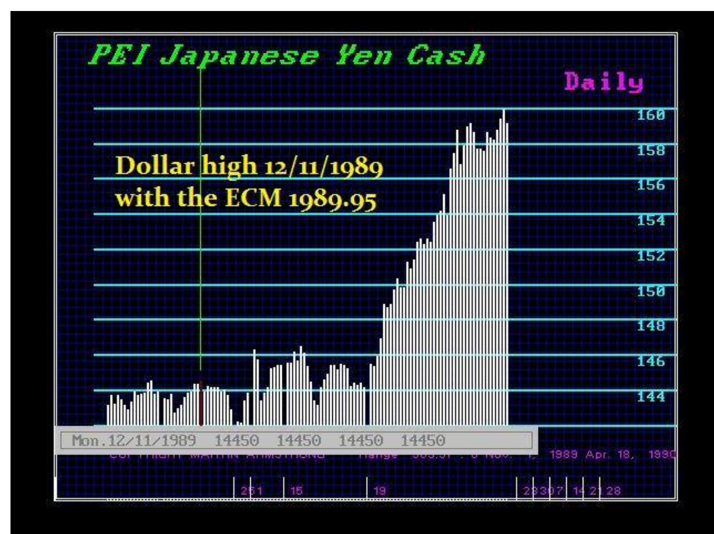


The significance of the **1987 Crash** was precisely what we were forecasting – it was a Foreign Exchange driven event. The capital poured out of the United States and this is where the **Economic Confidence Model** was the <u>**ONLY**</u> tool correctly forecasting what was really happening. We can see the net capital outflows of capital back to Japan during the **1987 Crash** were spectacular. There was no change in the underlying economic conditions. In fact, we were also forecasting the beginning of a brand new Private Wave of investment that would see the Dow Jones Industrials explode rising near term by some 600% from 1985. It was the G5 and currency that was causing the **1987 Crash** and the capital retracting into Japan that cause the capital concentration that manifested into the famous 1989 Japanese Bubble. The same swing in capital outflows took place during the Great Depression. Capital flows went crazy around the **1931 Sovereign Debt Crisis.**



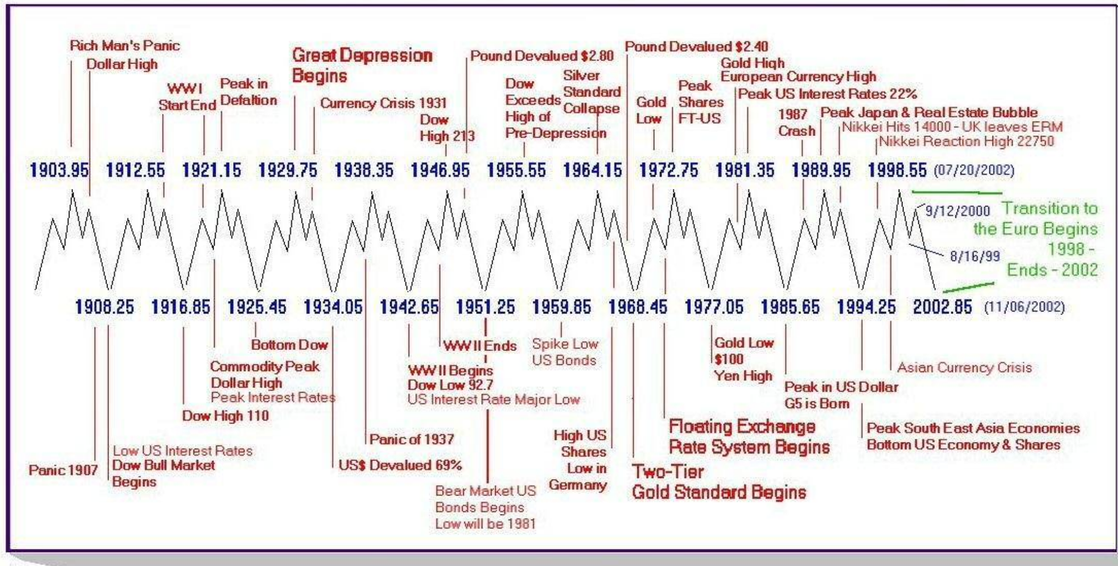


Illustrated here was the **Economic Confidence Model** target date was 13 days before the final high in the Japanese share market. At first glance, one would say it did not perform to the day in 1989. However, this was a currency driven event. When we look at the Dollar/Yen, this precise day was reached in the currency forewarning that foreign capital saw the bubble and was beginning to buy the dollar and sell the yen as capital was now starting to exit Japan from the foreign perspective precise as it had been the foreign investors that sold in 1987 due to currency that Americans could not see.



Indeed, the dollar rose from about 142 to nearly 160 by April 1990. This was the key to understanding the 1989.95 turning point – International Capital Flows being driven by currency first, investment decision in assets second. Hence, it was the G5 that was driving capital out of the dollar. That was the primary moving trend. As capital was being driven back to Japan, the yen

Economic Confidence Model



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rose in value. That attracted foreign capital and this caused the capital concentration in Japan. Then the shares captured the capital inflows driven first by currency. This is why the model worked first in yen and 13 days later in the shares. It had not been the Japanese share market alone that attracted foreign capital. We can see the explosive move in the dollar illustrated here.

The **Economic Confidence Model** has helped tremendously in redefining how capital moves both for currency and assets on a global scale. It was this shift in capital flows because of a US dollar devaluation by the G5 after 1985 that caused the capital concentration in Japan as it fled the United States. The model is a global one that illustrates the **Business Cycle** is international. We can see that the highs and lows of many markets around the globe conform to this mode. The same was true of Southeast Asia as we will explore.

What made the Japanese Bubble must be viewed internationally. As capital was driven from the US dollar, it was recalled to Japan by Japanese investors who were virtually told to get out. What would have been a normal peak and a 2-3 year correction under free market conditions was set for a Long Depression in Japan. It was Japanese government's attempt to prevent the collapse of the bubble and to pledge support for the market that encouraged Japanese companies to hold their investments rather than sell. This led to a prolonged economic decline since had the free market prevailed, the Japanese investors would have taken their losses quickly, and would have reinvested creating the recovery. The Japanese government succeeded in creating a Long Depression that typically lasts 23 to 26 years. For this reason, the final low in Japan is still on the horizon for 2013 at best to 2015.75 at worst.

It was the exit of capital from Japan that then targeted Southeast Asia. Here we can see the how capital moved as overlaid upon the Malaysian share market once it began to shift in 1994 away from Southeast Asia. The International Capital Flows had won a taste of profit (blood) in Japan. They now looked around the same as drawing blood from Greece of late in the **Sovereign Debt Crisis**. There, capital then looked at Portugal, Spain, and Italy and began to attack their bond markets driving their interest rates higher. The same tendency took place once international capital was abandoning Japan. It had gathered a taste for Asia and then looked around and said to itself – ***"Gee! South East Asia looks cheap!"***

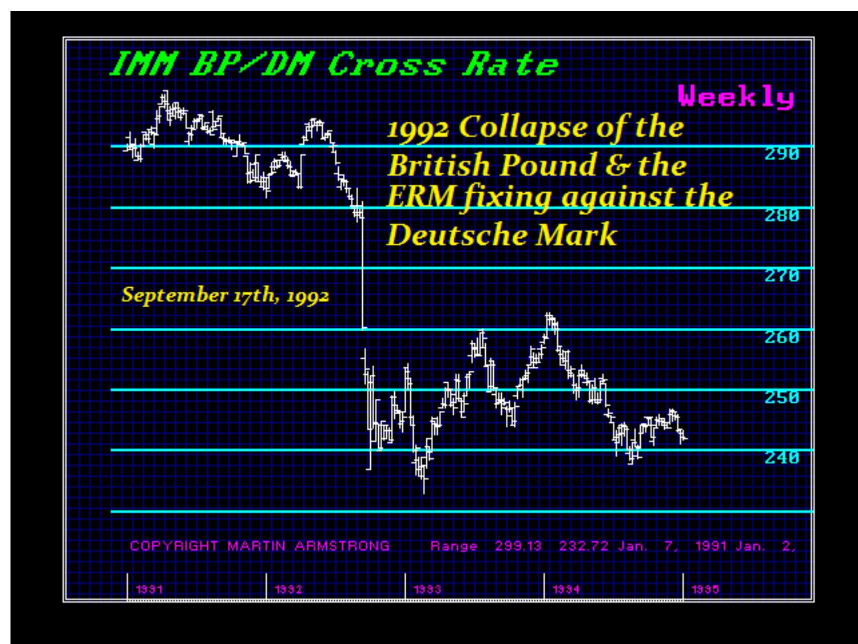
President Herbert Hoover wrote in his memoirs on page 67 Vol. 3, that this same trait of how capital rushes around the globe took place during the Great Depression.

"During this new stage of the depression, the refugee gold and the foreign government reserve deposits were constantly driven by fear hither and yon over the world. We were to see currencies demoralized and governments embarrassed as fear drove the gold from one country to another. In fact, there was a mass of gold and short-term credit which behaved like a loose cannon on the deck of the world in a tempest-tossed era."

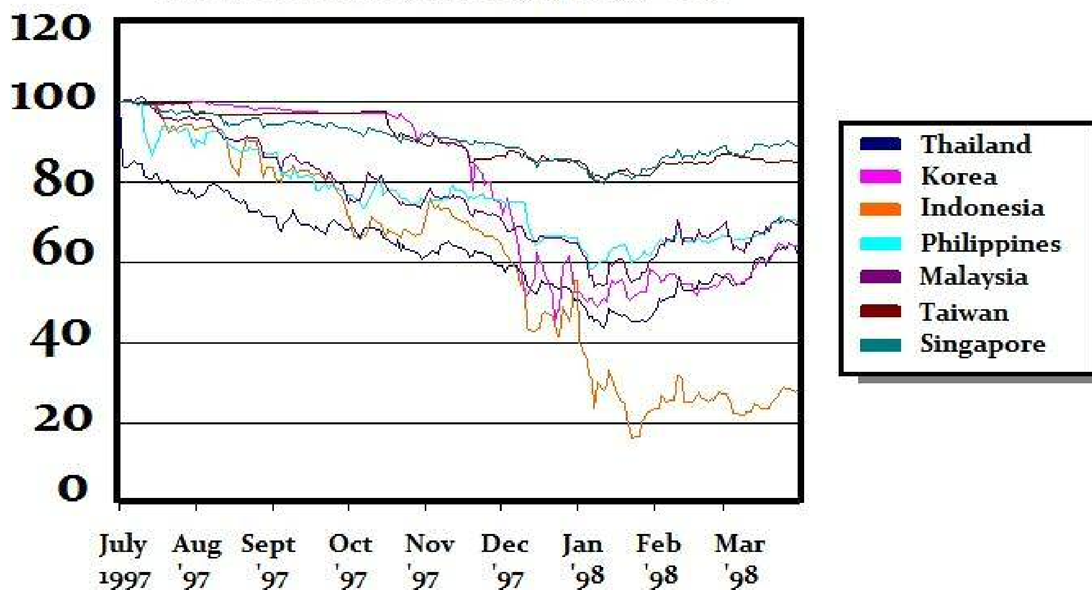
The 1994.25 turning point on the model pinpointed the next major shift in International Capital Flows. Not only did 1994 represent the major high for Southeast Asia, but it shifted the focus of international capital back to the United States and Europe. We can see that 1994.25 was the precise day of the low in the US share market.

The **Asian Currency Crisis of 1997** was a profound event. It was becoming obvious that institutional investors were starting to hoard together. The first sign that institutional investors were starting to join forces internationally appeared in 1992. The pound peaked at $2.01 during the third quarter of 1992, and then crashed into the first quarter of 1993 falling to $1.41. Germany boomed and the UK slipped further into recession as the expectation for Germany skyrocketed with optimism about also reunion. The fixed strength of sterling, maintained within the ERM's limits, caused British exports to decline. Prime Minister Major's government made desperate overtures to the Bundesbank to lower interest rates in theory to weaken the deutschemark. But these requests were counter to the fear of domestic inflation in Germany since it is always fight the hyperinflationary event compared to the USA fighting the Great Depression and deflation leading to to always stimulate.

The Britain and Germany were now diametrically moving in opposite directions. At the Bath meeting of European financial ministers in 1992, the differences in philosophy between Britain and Germany were exposed for the world to see. At the summit Norman Lamont, Major's successor as Chancellor of the Exchequer, harangued the Germans over their interest rate policy that was causing deflation in Britain thanks to the ERM. It was at this time that institutional investors (hedge funds + banks), led by George Soros, could see that the political policies between Germany and Britain would force a break of the fixed ERM between the two currencies. Sterling was overvalued relative to the deutschemark and something just had to give. Fixing currencies proved to be a fantastic trade. If one was wrong, there was no downside since governments were guaranteeing the peg. If traders were correct, then they had tremendous upside by shorting the pound and negligible risk.



On **September 17th, 1992**, the Chancellor, Norman Lamont, announced that the Government could no longer hold the line at the end of a day of desperate and futile attempts at propping up sterling, which included spending what the City estimated as £10 billion from Britain's reserves and a two-stage rise in interest rates to 15 per cent. Mr. Lamont later rescinded the second rise, and said interest rates would be pegged at 12 per cent, two points above the rate on the previous night. The announcement sent sterling tumbling in New York trading last night, hitting DM2.69 - nine pfennigs below its former permitted ERM floor against the German mark. He shifted exchange rates up from 12 per cent to 15 per cent on that one day, but his attempts to support the currency came to nothing. The pound devalued and Mr. Soros, who was rumored to have made as much as $2 billion in his bet against sterling, was christened "***the man who broke the Bank of England***" by the Daily Mail. That day became known as **Black Wednesday** boosting the ***Eurosceptics*** that would eventually help to keep the pound out of the Euro. John Major remarked afterwards: "***It was a disaster, a political disaster, there is no doubt about that. It was an embarrassment for the United Kingdom.***"

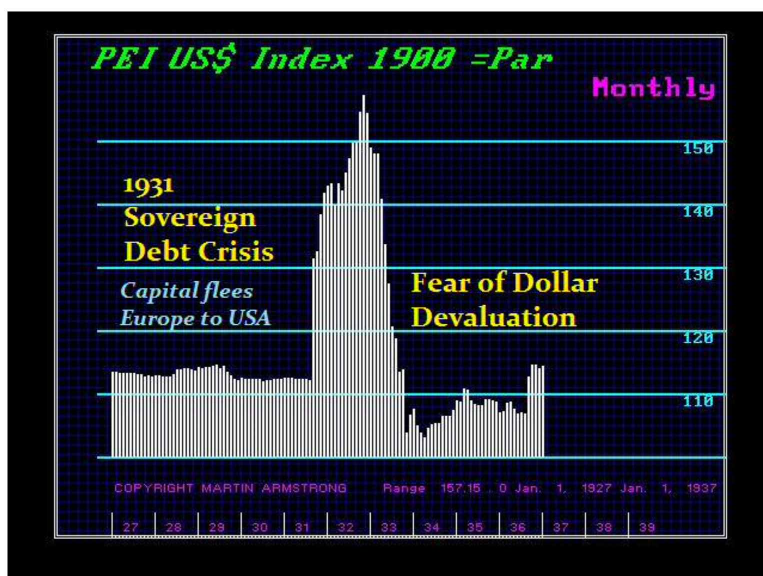


This was the event that drew First Blood and encourages Institutional Investors to prow the global markets in search of the next play. That same problem of fixing currencies was the cornerstone of Southeast Asia going into 1997. Of course, non-experienced economists look at the event from a very sterile perspective of account balances etc. The impact of the Asian crisis is long over and it had nothing to do with "crony capitalism" or even structural weakness. It was all about the movement and concentration of international capital. When capital fled, they tried to rationalize the event in a normal economic manner. Sorry – it was hot money. Of course many different things are exposed such as irregularities and accounting practices are also exposed. Those are the aftereffects – not the cause of the event.

At the time of the mid-1990s, Thailand, Indonesia and South Korea had large private current account deficits that were misunderstood since foreign capital investment goes into the capital account whereas interest, dividends and profits paid to foreign investors goes through the current account. This fact has always led to confusion and assumed that when the current account deficit becomes larger it is a trade imbalance. This is simply not true in a global economy where capital is free to circulate. The maintenance of fixed exchange rates has also been misunderstood since academics do not trade markets. The fixing of the currency eliminates perceived risk and encouraged external borrowing in foreiogn currency by domestic investors and corporations. This escalated the potential excessive exposure to foreign exchange

risk in both the financial and corporate sectors. But what is not understood outside of trading rooms is that when nations fix their currency they are guaranteeing the other side of every trade. Hence, a trader can short the currency, and he assumes no risk for the currency is fixed. However, if he is right and the currency will collapse, he wins. Thus, fixing currencies is simply a guaranteed trade. This is what broke the British pound in 1992.

The generally accepted lesson is first concerning macroeconomic and financial issues. The criticism is that the developing and transition countries opened up financially by the early 1990s and became "emerging markets" attracting foreign loans and investments. In developing East Asia, short-term commercial bank loans were the dominant form of capital inflow (Asian securities markets were underdeveloped). At first, this caused domestic booms and asset market inflation. But later, as the market sentiment turned for the worse and foreign investors pulled their money out, the balance of payments came under a severe pressure. Speculative attacks rapidly depreciated Asian currencies, and the illiquidity problem--inability to rollover the short-term bank loans since foreign banks demanded immediate repayment--occurred. The domestic banking sector froze up and domestic demand fell sharply as wealth is hoarded, causing a serious recession that lasted for one to two years. This view recognized the inflow of foreign capital as the cause, which was similar to the United States during the 1920s. Keep in mind that Britain had been the Financial Capital of the World up until 1914 and thus World War I sent capital fleeing to the United States. That capital flow, however, was making the United States an emerging market at the time. Singapore to this day has still a rising anti-foreign sentiment among itself people putting pressure on government to restrict foreign capital. This is the source of the resentment. Everyone fights the last war. Southeast Asia remains concerned about the influx of foreign capital creating another bubble, while the United States immediately stimulates and sees everything as deflationary, and Germany takes the opposite approach because it is still fighting the hyperinflation of the 1920s demanding austerity.



Milton Friedman's assessment of the Great Depression took the position that the money supply contracted because the Fed didn't act as a lender of last resort to save the banks in the United States from insolvency setting off a contagion of bank runs. So Friedman would have said that the Fed could have prevented M2 from falling in the

first place if it had acted aggressively as a lender of last resort as it was originally intended in the wake of the **Panic of 1907**. It is true that a banking crisis always takes place because banks take short-term deposits and lend long-term. When the depositors demand their money, the banks cannot pay because it was lent long-term.

Milton's argument, however, was too parochial because it ignored the worldwide deflationary spiral caused by the **Sovereign Debt Crisis** in 1931. That was an external stimulus that initially drove capital from one currency to the next and it was consolidating into the dollar. This was very similar to the capital concentrating in Southeast Asia, but this was for investment flows, not because capital was fleeing elsewhere other than the shift out of Japan. Hence, the **Asian Currency Crisis of 1997** was clearly caused by external shifts in capital flows and it need not be for domestic consideration but can also take place because the opportunity appears better elsewhere**.**

Milton Friedman (1912 – 2006)

Milton saw the tremendous gold reserves that had fled to the United States but criticized the Fed for not monetizing those reserves thereby increasing the money supply. The bank failures thus added to the increase in demand for gold resulting in hoarding, but again this was the knee-jerk reaction not the source of the event. The assumption that the Depression could have been prevented by the Fed if it had flooded the money supply with the gold that concentrated in the USA from the rest of the world has recently been shown that such a policy would not have worked just looking at the Fed's actions post-1997 and Japan post-1989.

Moreover, Roosevelt's abandoning the gold standard or devaluation of the dollar from $20.67 to $35 per ounce of gold was clearly effective in stopping deflation, but its anticipation is what accelerated the bank failures and the hoarding of gold. The rumor was out that Roosevelt would adopt such a policy forcing him to address the nation the night before the elections to deny that would take place. It did not promote recovery on a long-term sustainable basis as evidenced by the sharp recession in 1937. Nevertheless, any devaluation forces investors out of the currency and to then convert it to some tangible form of asset.

Of course in Southeast Asia there was the balance-sheet vulnerability that most see as being caused by the weaknesses of Asian banks, nonbanks and corporations. But the very foundation of a bank is really a vulnerable system. They are lending short-term deposits long-term so

whenever confidence declines, people demand their cash, banks lent it out, and failures then spread like a disease. Firms are highly dependent on indirect finance through bank loans for working and investment capital and this is always the weak link in the system.

Furthermore, the local banks had exposure to two kinds of balance-sheet mismatches. First they borrowed in USD and lent to domestic projects in local currency introducing currency risk that infiltrated Australia with Swiss franc loans in the 1980s and look at Iceland post-2007. Secondly, they borrowed in short term loans but lent to long-term domestic projects creating the typical maturity mismatch, the very thing the central bank was intended to patch. When the currency depreciation began, the balance sheets of these financial institutions were immediately hit and bad debt accelerated. When foreigners demanded repayment, they had no foreign cash.

This is a liquidity problem that further deepened the crisis creating insolvency as well. But again, these facts are **NOT** the cause, but rather the effect. International capital is moving. It is not looking for long-term investment. The presumption that such capital would not have left if the structure was sounder is naïve. Capital left because it saw no further short-term gains to attract it. Thus, capital saw a brighter smile elsewhere.

The collapsing demand domestically, which was caused by panic, credit crunch and the wrong political policy prescriptions in some countries, merely damaged the real sector and led to the accumulation of bad debt while then creating misperceptions about what could have been done to keep that capital in Southeast Asia. Hence, many see the **Asian Currency Crisis of 1997** was primarily caused by the wrong speed and sequencing of external financial liberalization. Government failed to understand how international capital moves and was incapable of properly monitoring what was happening no different than what Herbert Hoover had written about the events of 1931.

These events have led to the view that you must open up your financial sector gradually and in the right order. The pace of financial liberalization must match the pace of strengthening the domestic financial sector and the monitoring capability. The government must make utmost effort to improve domestic banks. The **Glass-Steagall Act** that attempted to prevent banks from speculating with other people's money helped to curtail future crisis but as soon as that was revoked in the United States, the banks created the biggest financial crisis with the 2007 collapse perhaps in the history of the world. Banks simply cannot be allowed to use deposits for proprietary trading.

Those most affected by the **Asian Currency Crisis of 1997** were the ASEAN4 nations namely Thailand, Indonesia, Philippines, and Malaysia along with Korea. China, India, Vietnam, Myanmar and Cambodia were not affected by the Asian Currency Crisis. This is not because the

productivity and their financial institutions were superior as an economic review might suggest. In reality, their domestic systems were much worse. One can argue that they were not directly hit because they did not open up financially. However, the truth lies in the trader mentality of fixed currency rates and what that offers as an opportunity for trading profit rather than the structural weaknesses of the developing economies. The real solution must be the removal of these structural weaknesses according to the general economic viewpoint, yet this still presumes government is capable to managing the economy.

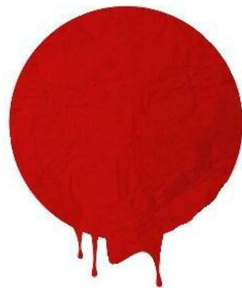
It has been argued that of the 26 banking crises in recent history, 18 were preceded by financial sector liberalization within a five year period. This has led academics to assume that this is the cause of the problem and that linearization should be undertaken cautiously. They argue that such financial liberalizations accurately signal 71% of all balance of payments/currency crisis and about 65% of all banking crises. The examples put forth are Chile 1982, Mexico 1994, Southeast Asia, and Latin America that the non-experienced academics argue strongly confirm this general tendency. However, what they are ignoring is the manner in which capital concentrates in one sector and nation and moves from one to the other sometimes simply because the opportunity appears better elsewhere. One cannot fully grasp the significance of these events by purely analyzing them from an academic perspective. As Herbert Hoover explained, capital was moving from a trading perspective that it simply demoralized domestic economies.

True, many have focused on subjects such as overlending and excessive risk taking in Chile in 1992 and the **Southeast Asian Currency Crisis of 1997**. Lending booms often take place because the bankers fail to understand migrant capital and that it will quickly turn from the domestic economy into another. Lending such capital is highly risky beyond the 2-year window. True, there is an empirical link between lending booms and financial crises that is very strong largely because bankers fail to distinguish between domestic and foreign capital deposits. Similar events were self-evident not just in Chile but also Mexico, Argentina (1981), Colombia (1982-83), Uruguay (1982), Norway (1987), Finland (1991-92), Japan (1992-93), and Sweden (1991).

Reserve requirements can be a useful tool in stabilizing a banking system, as was the experience of Argentina in 1995 demonstrated. However, this is typically argued against by the banks because it would be far more effective than the raising and lowering of interest rates that at the very best is just indirect. The In the United States and Japan, lowering of interest rates to virtually zero wiped out savings and has utterly failed to create any immediate stimulus for the economies of either nation. Rather than help the economy, in both instances such zeroing out of interest rates was a covert bailout tool for the banks.

The United States has adopted the same position post-2007 and QE1 and QE2 have failed completely and now we have QE3 Indefinite proving their complete failure as any policy. In the case of Japan, it inspired the Yen Carry trade where Japanese capital fled the country to US bonds to earn 8% compared to 0.1%. The USA buying bonds to inject cash into the system failed to comprehend that this is now a fully integrated global economy. There was no way to buy back only American held bonds and thus foreign held bonds purchased by the Fed only exported the money never stimulating the domestic economy achieved the same migration of capital witnessed in Japan.

Indeed, when I was invited to Beijing by the Central Bank of China to discuss the Asian Currency Crisis, they were deeply concerned about the collective forces of capital rush around the globe. Since the people in the Bank of China had been sent to the West to work in banks on dealing desks, they understood trading unlike any central bank in the world. That was the sole reason why the Bank of China had extended the invitation to travel to Beijing because of personal trading experience rather than academic posturing.

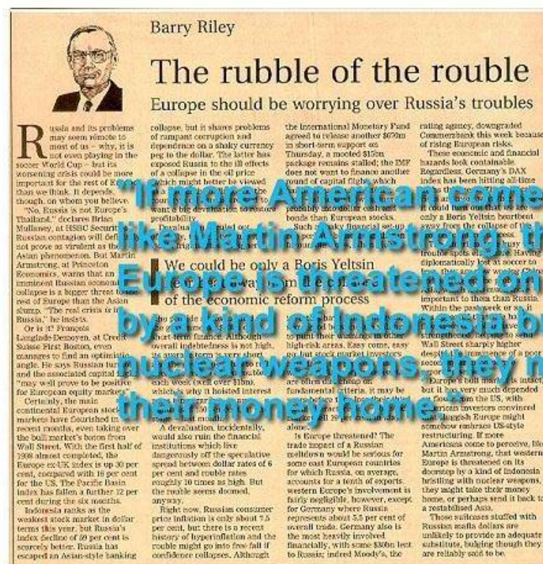


Japan Foreign
Direct Investment

Another important aspect of international capital flows at this time concerned the geographic distribution of Japanese foreign direct investment into Asia. For a very long been, Japanese foreign direct investment into Asia had targeted Hong Kong, Singapore, Indonesia, Malaysia, Thailand, Philippines, South Korea, and Taiwan. In 1990, China's manufacturing sector accounted for barely 5% of all of Asia. However, by 1995, that manufacturing share of China rose dramatically to 43%. Almost 60% of Japanese firms with overseas production had opened facilities in China. It was ironically the Japanese who invested the most in China very rapidly. It is a natural phenomenon that the higher developed countries increase taxation and labor costs causing manufacture to always migrate. It was this initial trend that set the tone for the boom in Southeast Asia going into 1994. Now China displaced Japan in one-third of the time of the Japanese economic miracle.

The **Economic Confidence Model** from this point in time once again correctly provided the precise day of the high for the United States stock market on July 20th, 1998 (1998.55). Not merely did this provide the precise day of the high, but it was also showing the collapse in Russia as an emerging market. We provided that forecast in a London conference and the ***London Financial Times*** covered this placing it on the front page of the second section. Indeed, his forecast that Russia would collapse in a matter of weeks manifested in the **Long-Term Capital Management (LTCM) Crisis**. Ironically, **LTCM** was founded in 1994 by John W. Meriwether, the former vice-chairman and head of bond trading at Salomon Brothers that blew up when it was caught manipulating the US Treasury Bond auctions in 1991.

Members of **LTCM's** board of directors included Myron S. Scholes and Robert C. Merton, who shared the 1997 **Nobel Memorial Prize in Economic Sciences** for a ***"new method to determine the value of derivatives"***. Of course, their model proved to fail in the end for it lacked the historical depth to within major panics. **LTCM** lost $4.6 billion in less than four months following the **Russian Financial Crisis of 1998** requiring financial intervention by the Federal Reserve because it owed money to the bankers. Since our firm was managing a hedge fund for Deutsche Bank and for Magnum Global Investments, while **LTCM** lost, our funds jumped by 60% in one month thanks to this model resulting in being named fund manager of the year in 1998.

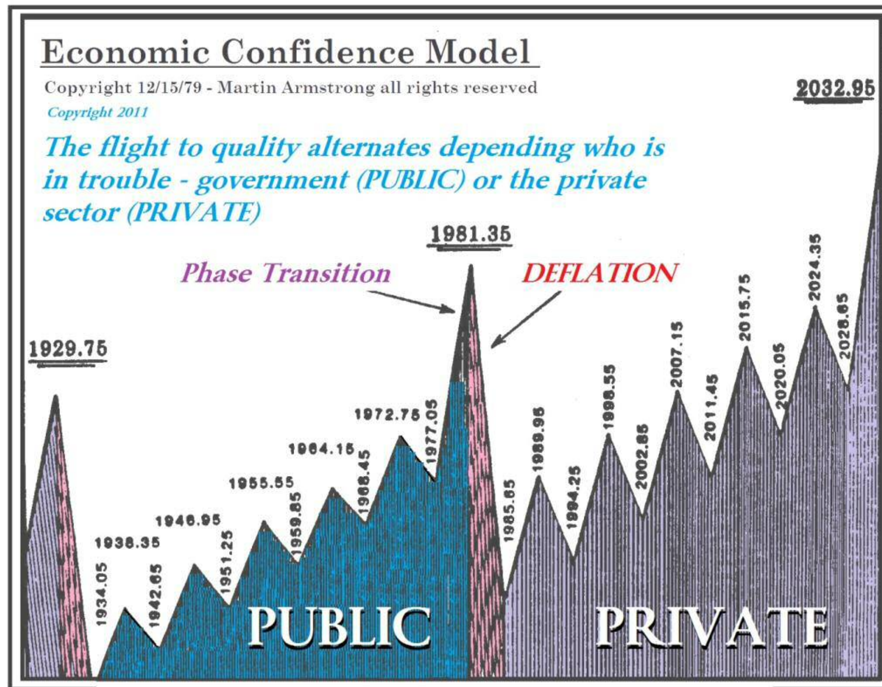

Barry Riley

The rubble of the rouble

Europe should be worrying over Russia's troubles

"If more American come to perceive, like Martin Armstrong, that western Europe is threatened on its doorstep by a kind of Indonesia bristling with nuclear weapons, they might take their money home."

... If more Americans come to perceive, like Martin Armstrong, that western Europe is threatened on its doorstep by a kind of Indonesia bristling with nuclear weapons, they might take their money home, or perhaps send it back to a restabilised Asia.



Capital not only moves around internationally as Herbert Hoover himself witnessed during 1931, but then it also moves back and forth between two extremes of confidence. This is best described as **Public v Private Confidence**. There are times historically where people are confidence about government and live peacefully within its protective shadow. Then there are times when government becomes abusive and suppresses the right of the people causing civil unrest and eventually this manifests in war or revolution.

To create movement, you need two extremes. Like a sidewinder snake, it moves rapidly by propelling its body between two extremes on either side. Like a pendulum, moving to the extreme on one side provides the energy to swing back to the opposite extreme. The economy moves in this manner always between two extremes the same as a market moves between **BULLISH** and **BEARISH**. This is the mechanism by which the economy moves based upon **CONFIDENCE.** This is why we call major declines **DEPRESSIONS** because people are depressed and lack **CONFIDENCE** to invest.

Joseph Schumpeter (1883-1950) saw this cyclical movement between two extremes and dubbed the process as one of Creative Destruction. Indeed, the US Great Depression began with 40% of the civil work force employed as farmers. Thanks to the Dust Bowl (7 year drought), these people may have seen their livelihood destroyed, but it was a necessary process to force them into an industrial skilled labor force. Hence, the movement between two extremes indeed propels the economy but also provides the force for change – Creative Destruction.

Joseph Alois Schumpeter
(1883 - 1950)

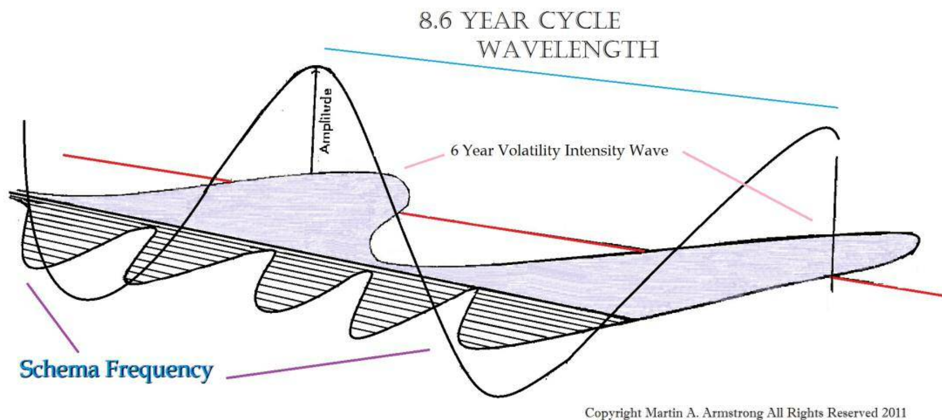
Others have caught glimpses of how things must move between two extreme forces like a pendulum in order to sustain movement. George Hegel (1770-1831), observed these two forces within philosophy which is why we have left and rights wings, Democrats and Republicans. Traditionally, Hegel's thought has been analyzed in terms of the categories of thesis, antithesis, and synthesis, although he tended to avoid these terms. The **thesis** is an idea or a historical movement that contains within itself an incompleteness that gives rise to opposition, or an **antithesis**, a conflicting idea or movement. Hence we get Republican v Democrat philosophy. Eventually, this then merges resulting in the conflict a third point of view that arises blended from the points of truth contained in each view that we call the **synthesis.** This hybrid overcomes the conflict by reconciling at a higher level the truth contained in both the thesis and antithesis. This **synthesis** becomes a new thesis that generates another **antithesis**, giving rise to a new **synthesis**, and thus the process of two extremes in thought always exists. For example, it was the Southern Democrats that fought and died for slavery. Yet with time, the constant churning of ideas between two extremes ultimately leads to what one could call cross-dressing. The two extremes will often switch beliefs. Even in politics, Oliver Cromwell revolted against the king, beheaded him, and then produced coins with his own image as if he were king minus royal titles. Napoleon crowned himself emperor of France. John Quincy Adams (1767–1848; sixth president 1825–1829) said ***"we have conquered the enemy. We occupy their hill. We have become the enemy."*** This is the fashion that the process of intellectual or historical development is continually generated creating waves of Creative Destruction. Karl Marx and Frederick Engels used Hegel's theory of the dialectic to back up their economic theory of communism they believe was the synthesis, but failed to understand that it too would fail.

George Wilhelm Friedrich Hegel (1770-1831)

Everything moves between two extremes. People often ask what if everyone followed the **Economic Confidence Model**? The actual answer is – impossible. There will always be an opposition. There must be to create the movement. The movement of the Earth propels the Foucault pendulum at the Pantheon in Paris. Hegel's dialectic explains these opposite forces even within the thinking process of mankind. Hence, it becomes the swing in confidence and who do you believe now – the Private sector, or Public (Government).

Observing the economy on a global scale reveals how capital moves, invests and flees in time of uncertainty both from economic change (raising taxes) as well as geopolitical (war). Capital is always seeking the best opportunity with the lowest perceived risk. This leads some down the road of corruption to manipulate the government in order to create the riskless trade. This has led to bankers convincing government they cannot be allowed to take a loss for it would lead to a depression. This is nonsense, but it has worked from Long-term Capital Management bailout of a hedge fund to the $700 billion TARP bailout from the aftermath of 2007.15.

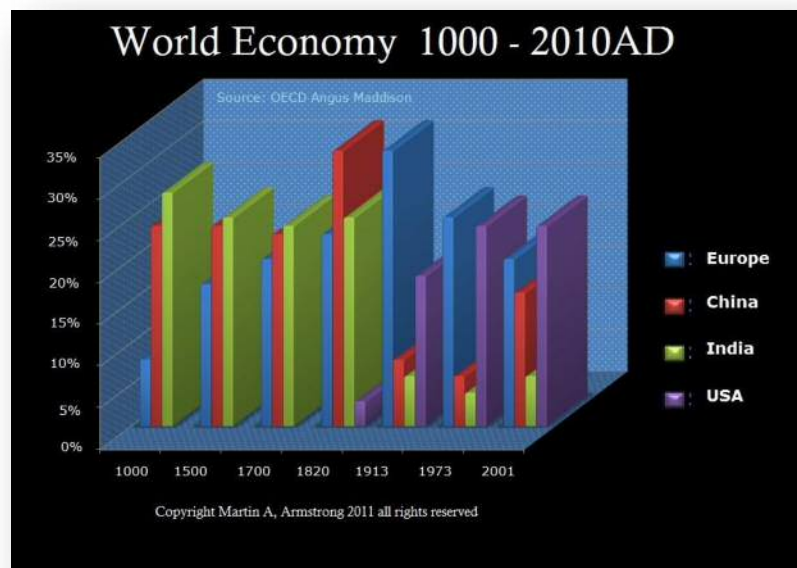
Nevertheless, it will soon become clear that there is this shift between **Public** and **Private Confidence** that provides the underlying movement within politics and economics. Whenever corruption runs high in government, CONFIDENCE collapses and society veers away from government trusting the private sector in its place. When the private sector collapses as in the Great Depression, the people turn toward government for a safety net. If everyone is fat and happy, they will elect to ignore the rising trend preferring not to rock the boat. That trend will reach its extreme and then change erupts in the political-economy. Major waves of intensity als take place with this mechanism and here we find the rise and fall of nations. As corruption became ramped in Rome, people fled the taxes and corruption moving toward the suburbs that even the Romans called in Latin - ***suburbium*** *(the flight from the cities)*. With time, the pendulum will swing and revert back in the opposite direction toward collective cohabitation giving rise to civilization.



Consequently, the issue of **INTENSITY** also oscillates on a different frequency but accounts for the movement of the system between the two extremes and is bound to the **Business Cycle** internally. Consequently, we emerge with a generational cycle defined by **INTENSITY** shaped into periods of 51.6 years compose of a group of 6 individual **Business Cycles** of 8.6 years in length each building in volatility (**INTENSITY**).

The most interesting aspect of this dynamic interlocked movement between **INTENSITY** and the **Business Cycle**, has been the realization that absolutely nothing remains constant, nor is there any one system that will every prevail. This is why there is the inevitable rise and fall of empire, nations, and city states. Everything remains in a constant state of flux oscillating between two opposite extremes.

Looking at the rise and fall of empires, nations, and city states, what is stripped naked and laid prostrate before us is history in the making. The **Financial Capital of the World** constantly migrates around the globe because of this perpetual contest between two extremes.



Work by Lui Liu

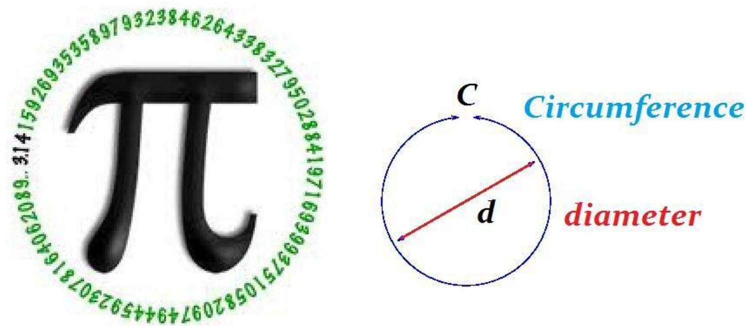
The model then exposed something tremendously important. It is a global model that includes every country around the world. The entire global economy is correlated and in so doing, the capital flows can be easily seen as the rush around the world causing booms and busts. What was truly discovered beyond the mere boom bust cycle, has been that the international concentration of capital is the key. The fortunes of empires, nations, and city states constantly change because generally man remains ignorant of the trend in motion. It is like the Precession of the Equinoxes in that the cycle is 25,800 years and to move just one degree in the circle takes 72 years. Consequently, it took several generations to discover that phenomenon.

Here is the spectacular painting by Lui Liu. This illustrates the changing positions and fortunes of empires, nations, and city states. America is still clothed but starting to lose. China has lost her shirt but displays her tattoo symbolizing her new modern posture. Russia is on her back who also lost her top flirting with America and China. To the left is Japan stripped naked for she has lost everything. Standing to the right, timid, yet uninvited, stands Taiwan – the political orphan between the great powers.

The **Economic Confidence Model** worked rather interesting in defining the **Dot.COM Bubble of 2000**. A number integral to the **ECM** beyond 8.6 has been 26. There were 26 international panics within a period of 224 years which produced the number 8.6. Therefore, the number 26 double is 52, and the major wave of the 8.6 year **ECM** is 51.6 years. Here we can see that the peak in the **DOT.COM bubble** in the NASDAQ Composite took place 26 weeks before the **ECM** half-cycle wave. The low in 2002 came 3 weeks before the ideal date 2002.85

LISTING OF YEARS IN WHICH INTERNATIONAL PANIC STRUCK

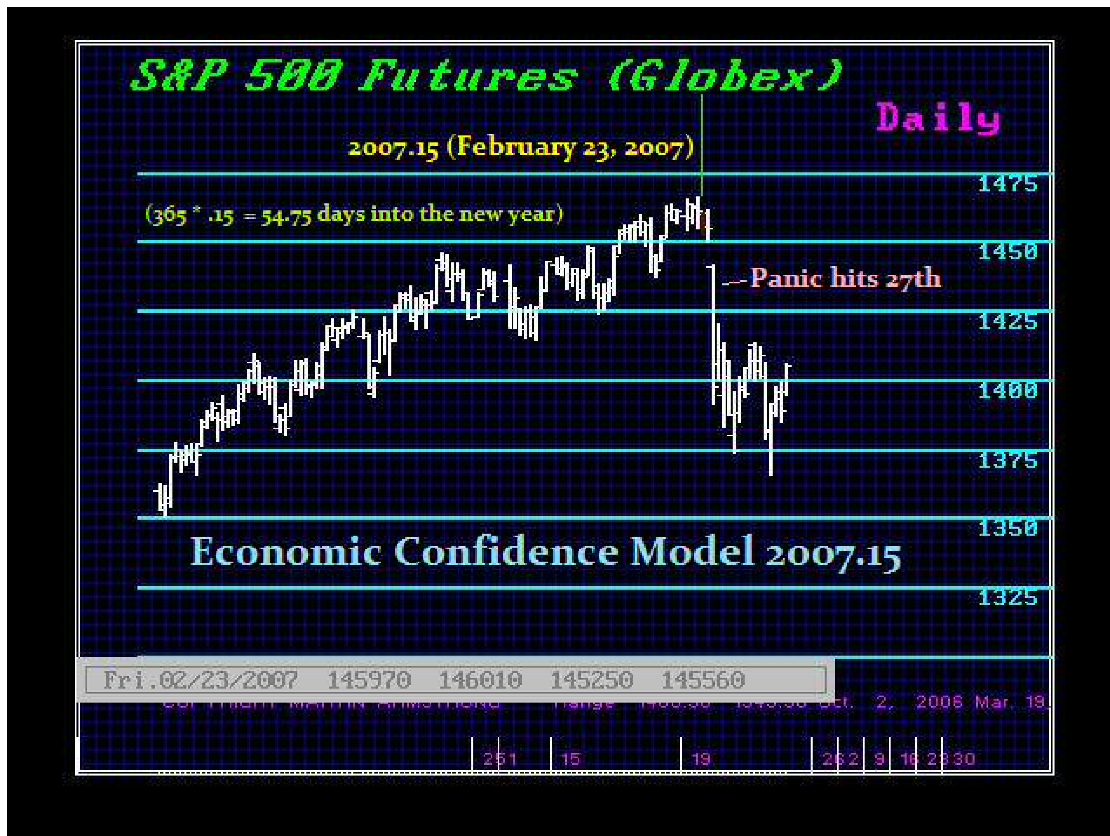
1683							
1711	1720	1731	1745	1763	1772	1783	1792
1814	1818	1825	1857	1866	1869	1871	1872
	1873	1884	1890	1893	1895	1896	1899
1901	1903	1907					



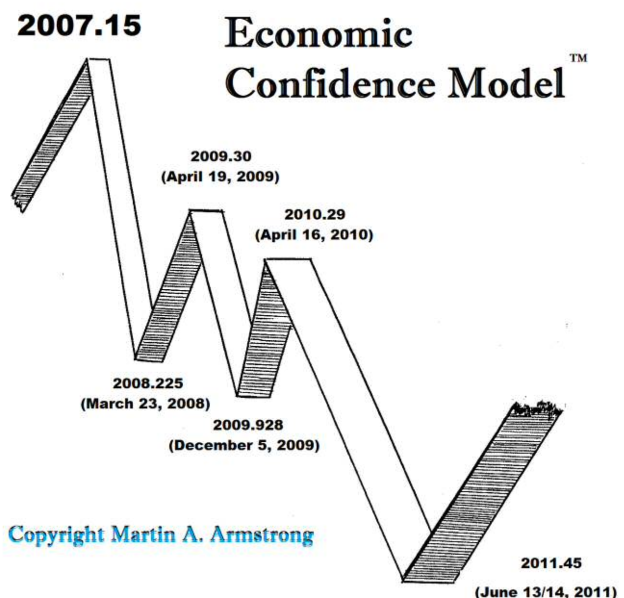
π is commonly defined as the ratio of a circle's circumference to its diameter

When this frequency was first discovered, it seemed that 8.6 was a rather odd number that just didn't fit mathematically. In trying to test the validity of this frequency, however, it became quite amazing. The accuracy to the very day made no sense. How could something work to the very day? When October 19th, 1987 unfolded right to the day, it could only be understood in terms of the perfect cycle. The total number of days within an 8.6-year Business Cycle was 3141. In reality, the 8.6-year cycle was equal to π (Pi) * 1000. True, π had been that illusive number that was far beyond a mere coincidence. This was certainly not random and the number of precise events ruled out coincidence. The number of variables involved in projecting the future became dynamic and complex with each individual market and nation beating between its two extremes according to its own frequency. The relationship of 8.6 to π (Pi) confirmed that indeed the Business Cycle was in fact a perfect natural cyclical phenomenon that warranted further investigation.

Indeed, the precision to a day appeared numerous times around the world in different markets. Both the 1994.25 and the 1998.55 turning points also produced clear events precisely to the day as was the case for the peak in the Real Estate Index 2007.15. The probability of coincidence of so many targets being that precise to the day was well into the billions. Indeed, the relationship of π to the Business Cycle demonstrated the existence of a perfect cycle that returned to its point of origin where once again it would start anew. The complexity that arose was that while the cycle could be measured and predicted, precisely which sector of the global economy would become the focal point emerged as the new research challenge. It was the correlation of markets and nations to the ECM that allowed one to see how capital rushed around the globe and the rise and fall of empires, nations, and city states unfolded.



When the next high in the **Economic Confidence Model** 2007.15 came 54 days into the next year (February 23rd, 2007) and this was one day after the high, they were calling this forecast ***"Armstrong's Revenge"***. This turning point market to the day the high in the real estate index and it unfolded with time as the **Mortgage Backed Crisis of 2007**. So just how could there be a coincidence when so many targets came in on the precise day?



As the half cycle was now approach on the way down into 2011.45, on April 15, 2010 the EU monetary chief Olli Rehn said there was no possibility that Greece will default on its debts and no reason to doubt Germany's commitment to an EU pledge to help. The International Monetary Fund official says that Greece has expressed interest in a three-year precautionary IMF agreement, which will only be tapped when Greece requests the funding. Parliament adopted a tax reform bill, backing government moves

to tackle tax evasion and shift the fiscal burden to higher-income earners in Greece as Athens looks for ways to slash its massive budget deficit. Then on April 16, 2010, the European finance ministers met in Madrid to discuss Greece's debt crisis but said Athens was seeking to clarify how an emergency aid mechanism would work, rather than requesting it. Of course that was the precise day on the model. From that day onward, even the Greek General Share Index collapsed moving into a low in 2012 56 months from the 2007 high.

Then we come to the turning point 2011.45 on the **Economic Confidence Model,** which so far has proved to be a truly profound shift in the global economic trend. Where the majority were calling for the collapse in the share market still insisting that a Great Depression was on the horizon, this model was saying no way. To create such a catastrophe, it must arrive from an extreme bubble peak as we saw in 1929 in the United States and 1989 in Japan. The model was suggesting a reversal of fortune and that the share market would rally back to the old highs. This was correctly report by **Barrons** on June 25th, 2011.

BARRONS - JUNE 25, 2011

The man who called the '87 crash is now calling for a long-term market rise.

" It looks like the stars are aligning for market theorist Martin Armstrong and his devout followers….—his method of sizing up confidence in the economy is pointing to an upturn in the stock market.

Armstrong is the developer of the Armstrong Economic Confidence Model, best known for calling the crash of 1987 to the very day. The model pegged June 13-June 14, 2011, as the start of a long-term upward trend in the market; the market obliged by notching its first weekly rise since April 29.

Buy Signal: An esoteric theory based on cycles that relate to the ratio pi recently signaled the start of a long-term market uptrend.

The model holds that every 8.6 years there are shifts in market sentiment, with public confidence waxing or waning in response to world events. Also key are quarter-cycles of 2.15 years. The low of the bear-market cycle on March 6, 2009, to the peak of April 29, 2011, spanned 785 days, or 2.15 times 365. The June 13-June 14 period marks 8.6 years since the last major bottom of 2002, and is 4.3 years (two times 2.15) from the 2007 peak of easy money and the tightest credit spreads ever.

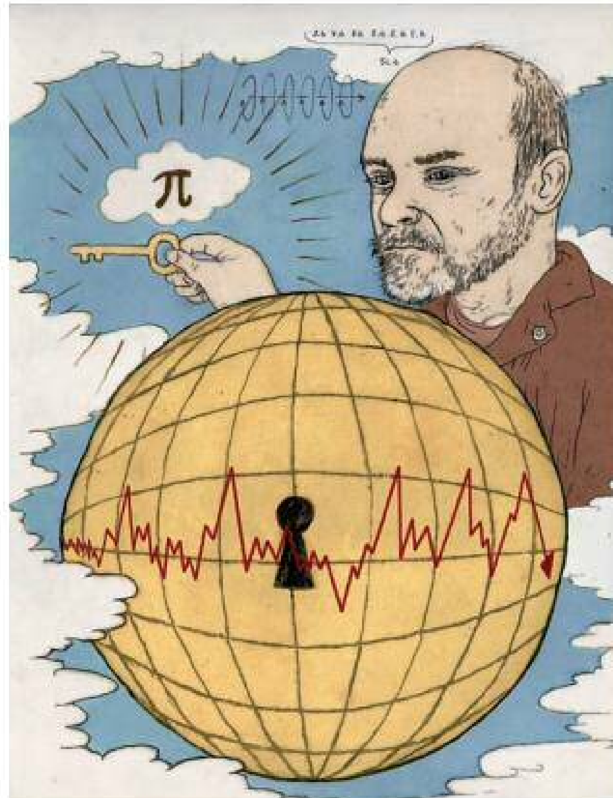
The model is known as the "pi" cycle, because there are 3,141 days in an 8.6-year cycle, reflecting the value of pi (3.14159…) times 1,000. Pi, the ratio of a circle's circumference to its diameter, is a revered number among mathematicians and, in Armstrong's view, may help explain the model's predictive power."

OUR LOCAL CORRESPONDENTS

THE SECRET CYCLE

Is the financier Martin Armstrong a con man, a crank, or a genius?

BY NICK PAUMGARTEN

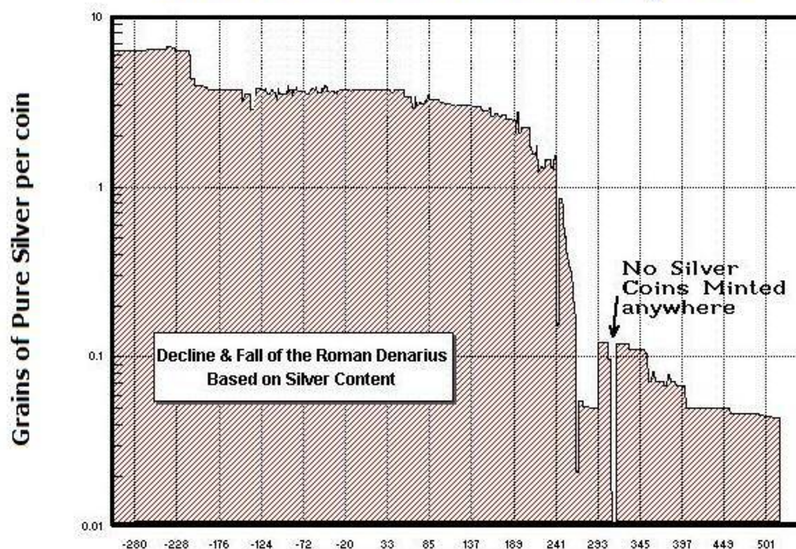


The accuracy of this model clearly went beyond personal opinion. The world was stunned by its forecasts and some assumed that it was really the result of too much influence rather than a discovery of untold proportions. ***Time Magazine*** wrote on November 30, 2009 ***Riding the Waves of Irrational Behavior*** that this model ***"made several eerily on-the-mark calls using a formula based on the mathematical constant pi."*** Even Bloomberg News had to acknowledge the model "called Russia's financial collapse in 1998" and that the "model … also pointed to a peak just before the Japanese stock market crashed in 1989." Then there was the forecast of October 1997 that the creation of the euro ***"will merely transform currency speculation into bond speculation, leading to the system's eventual collapse."*** The model became known as the ***"Secret Cycle"*** and the ***"pi-cycle model"*** after it was featured in a 10 page article in the **New Yorker Magazine** on October 9th, 2009. Nick Paumgarten wrote that π (Pi) ***"was, after all, the magic number associated with the swing of a pendulum, Heisenberg's uncertainty principle, and the Great Pyramid at Giza. Why not the vast monuments of data known as the financial markets?"*** Quoting Armstrong, Paumgarten wrote: ***"Suddenly I saw it in my mind's eye," he wrote. "There was a Geometry of Time itself."*** The New Yorker continued: ***"Pi suggested some future turning points, … Among them was December, 1989, which marked the Nikkei's peak before it crashed. This call earned him the magazine Equity's award as the top North American economist, … Another big pi date was July 20, 1998, which turned out to mark the high point in the S. & P. just before a Russian default broke the giant hedge fund Long Term Capital Management and nearly wrecked the financial system. Armstrong by now was running a couple of hedge funds, and the Magnum Hedge Fund Reporter named him Fund Manager of the Year."***

In the United Kingdom, for example, a popular financial magazine ***Money Week*** published an article on Martin Armstrong on March 27, 2007, where they highlighted that the model had predicted a major top in financial markets for February 27, 2007, with the next major bottom being June 18, 2011.

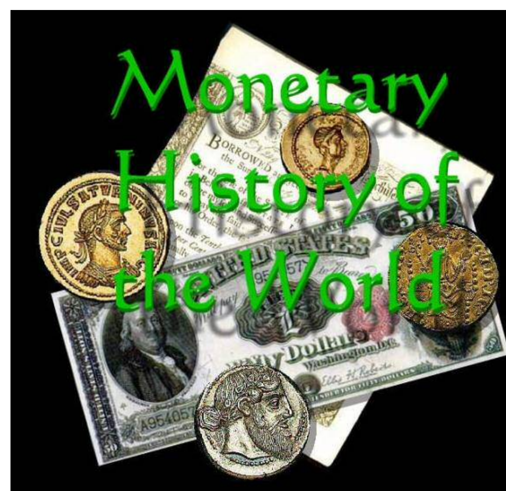
Yet after 2011.45, the model has worked well even on the minor turning points. The first minor target was 2012.05 (January 18th, 2012). We can see that this was the week where the Dow decisively broke out to the upside start the new uptrend post 2011.45. The next target was 2012.43 (June 6th, 2012). This provided the precise low on the test of support. Understanding that **TIME** is incredibly important has become paramount. This model is precise. It is not based upon human opinion that is highly volatile. Anything that requires interpretation to forecast such as Elliot Wave is highly dependent upon opinion. The same can be said of technical analysis where the one is trying to interpret the future pattern based upon previous patterns – head & shoulders, etc.

The numbers are the numbers. This does not involve Guru Status or personal opinion. The true critical factor is data. TIME becomes possible to ascertain ONLY when there is a sufficient database available. Long Term Capital Management began in 1994 at the bottom of the Economic Confidence Model and collapsed as soon as it turned in July 20th, 1998. They lasted just 4.3 years and their model lacked the historical depth to be able to test what happens even during a major collapse as was the case in Russia.



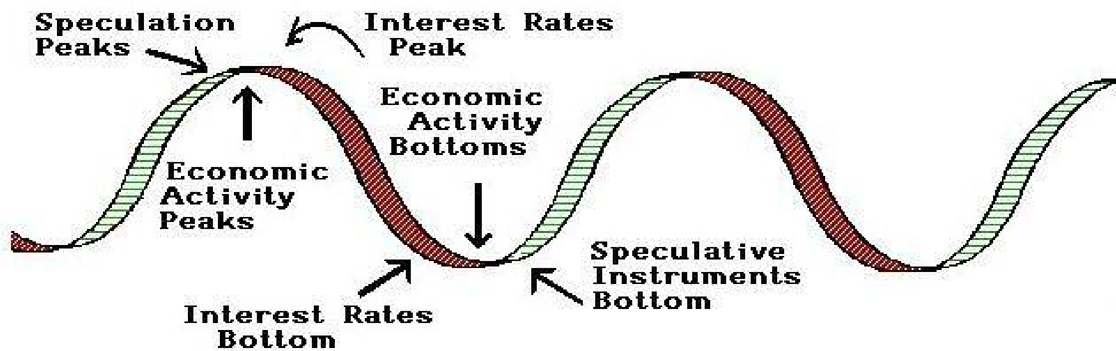
One of the most significant advantages of gathering historical information on the rise and fall of nations throughout history has been the discovery of the true nature of the world economy and its interactions with mankind. There have been numerous shifts and changes in the world economy from even prehistoric times. Weather has had a tremendous impact in causing migrations of mankind that eventually spread humans around the globe. The rise and fall of empires, nations, and city states have caused the financial capital of the world to move from city to city, region to region, empire to empire, and continent to continent. The bottom line - Nothing lasts forever.

We have reconstructed the Monetary History of the world. This has provided us with a database that is unsurpassed no less even unapproached. Illustrated here is the fate of Rome illustrated. The importance of creating such a database is to establish the fundamental principles about how the economy moves. Real science requires observation – not opinion. The collapse of Rome was rapid taking place in just 13 years.



Business Cycle

Based on Average Intensity



The observations of the Business Cycle have been greatly biased by the New Deal where there is an assumption of power by the goverenment and an understanding of what they are actually doing. This has led to the misconception of interest rates where it is assumed that a rise in interest rates is not bearish, whereas during the Roaring '20s, a rise in interest rates indicated rising demand for money and that meant a bull market. Interest Rates always declined during a recession because there was no demand for money while banks typically demand full collateral for loans compare to boom times when they just want to lend regardless of credit.

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This movement of the **Business Cycle** has been the subject of manipulation and the attempts by man to even eliminate it. Never has man been satisfied with observing and learning how to live with the **Business Cycle**. Every time he has sought to control what he cannot even comprehend. There are four seasons to weather and this is part of the **Business Cycle** as well for indeed inflation can be driven by the rise and fall of agriculture as just one component. In the Bible there is the story of Joseph who told the Pharaoh there would be seven years of plenty and seven years of drought. The moral to that story – understand the cycle, live with it, and adapt to it to survive. Consequently, famine has also dramatically altered the course of nations and has been a major contributor toward the migrations of man around the globe. Up until the 1950s, agriculture accounted for 70% of the US economy falling to 40% by 1900. While the United States employs less than 3% of the work force in agriculture, many other developing nations are in that category of 70%+ agrarian.

Man's quest to eliminate the **Business Cycle** rather than live with it is engrained even within politics. The familiar banter is vote for me and I will bring change. The current elections in the United States are really just a race between Pepsi and Coke – there really is not much difference once you strip the "social" issues aside. After Gay Rights and Abortion, there is no substance. Nobody stands up with a plan explaining **HOW** they will create jobs. They provide lip-service because there is nothing they can do, nor do they understand what to do.

Paul Volcker, former chairman of the Federal Reserve, addressed this very issue of manipulating the **Business Cycle**. He explained that the idea after Keynes was this ***"New Economics"*** where it was presumed that government could play God and eliminate the **Business Cycle** at will. He explained that this idea had failed and was self-evident when he delivered this bold realization in 1979 in what he called the Rediscovery of the **Business Cycle**.

> ***"The Rediscovery of the Business Cycle – is a sign of the times. Not much more than a decade ago, in what now seems a more innocent age, the 'New Economics' had become orthodoxy. Its basic tenet, repeated in similar words in speech after speech, in article after article, was described by one of its leaders as 'the conviction that business cycles were not inevitable, that government policy could and should keep the economy close to a path of steady real growth at a constant target rate of unemployment.'***
>
> ***"Of course, some minor fluctuations in economic activity were not ruled out. But the impression was conveyed that they were more the consequence of misguided political judgments, of practical men beguiled by the mythology of the old orthodoxy of balanced budgets, and of occasional errors in forecasting than of deficiency in our basic knowledge of how the economy worked, or in the adequacy of the tools of policy. The avant-garde of the profession began to look elsewhere – to problems of welfare economics and income distribution – for new challenges.***

"Of course, the handling of the economic consequences of the Vietnam War was an obvious blot on the record – but that, after all, reflected more political than economic judgments. By the early 1970s, the persistence of inflationary pressures, even in the face of mild recession, began to flash some danger signals; the responses of the economy to the twisting of the dials of monetary and fiscal policy no longer seemed quite so predictable. But it was not until the events of 1974 and 1975, when a recession sprung on an unsuspecting world with an intensity unmatched in the post-World War II period, that the lessons of the 'New Economics' were seriously challenged."

The Interventionists

Karl Heinrich Marx
(1818-1883)

John Maynard Keynes
(1883-1946)

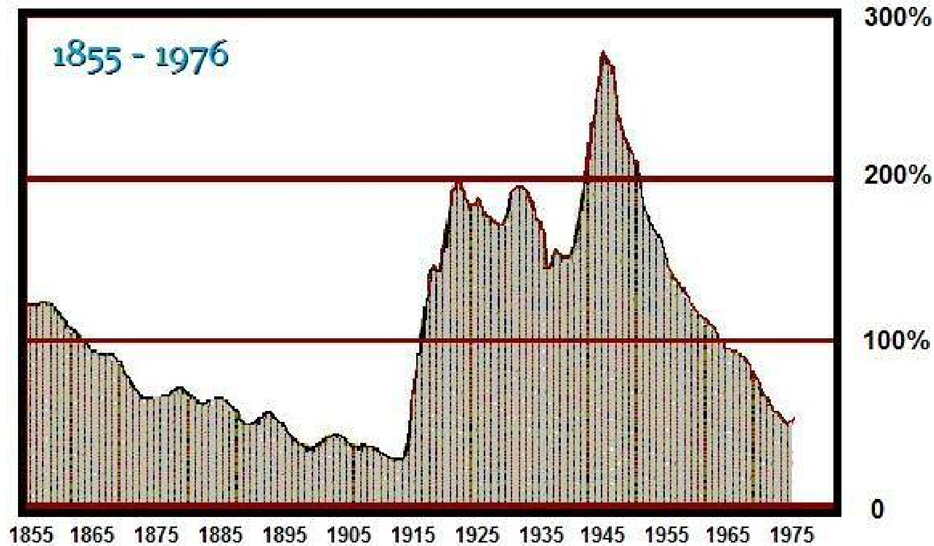
That idea first emerged with Karl Marx who advocated the denial of personal property from the individual to eliminate greed and exploitation of the worker. Marx attributed all value to labor and ignored ingenuity, creation, and the free spirit of man. While his idea may have been noble from a humanitarian perspective, they have nonetheless proved absurd and unworkable. Marx took the power from the people and handed it in a form of a golden scepter of authority to government. Unfortunately, Marx did not fully comprehend human nature. John Maynard Keynes was not much better. He still adopted the Marxist philosophy at its core that government was capable to unbiased management of the affairs of men. In the aftermath, this idea that government is capable of altering the direction of society by regulation has still proved totally worthless. Whatever the policy governments have followed postwar, followed society has only led to massive debt structures that threaten to bring down Western Civilization as it has destroyed every empire, nation, and city state since the dawn of society with no exception.

THE RISE OF ASIA

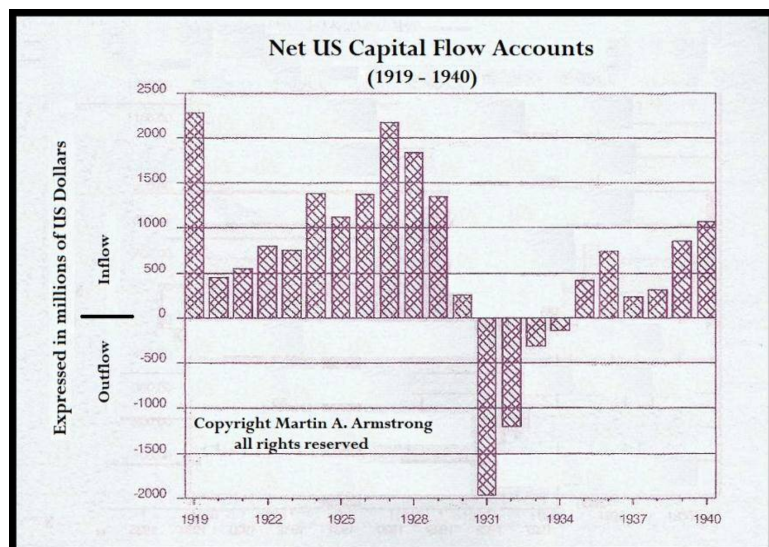
The Financial Capital of the World in modern times had migrated from Italy to Germany and then to Amsterdam as a result of the Serial Spanish Sovereign Defaults. Spain became a serial defaulter beginning in 1557 followed by 1570, 1575, 1596, 1607, and 1647 ending in a 3rd world status. The Spanish Inquisition chased the Jews out of Spain and they too their expertise to Holland where insurance and banking began. It was the Dutch William of Orange who married Mary of England and became the King of England. It was William who brought with him the Dutch way of doing things and this aided the transfer of that title of the Financial Capital of the World to Britain starting in 1689.

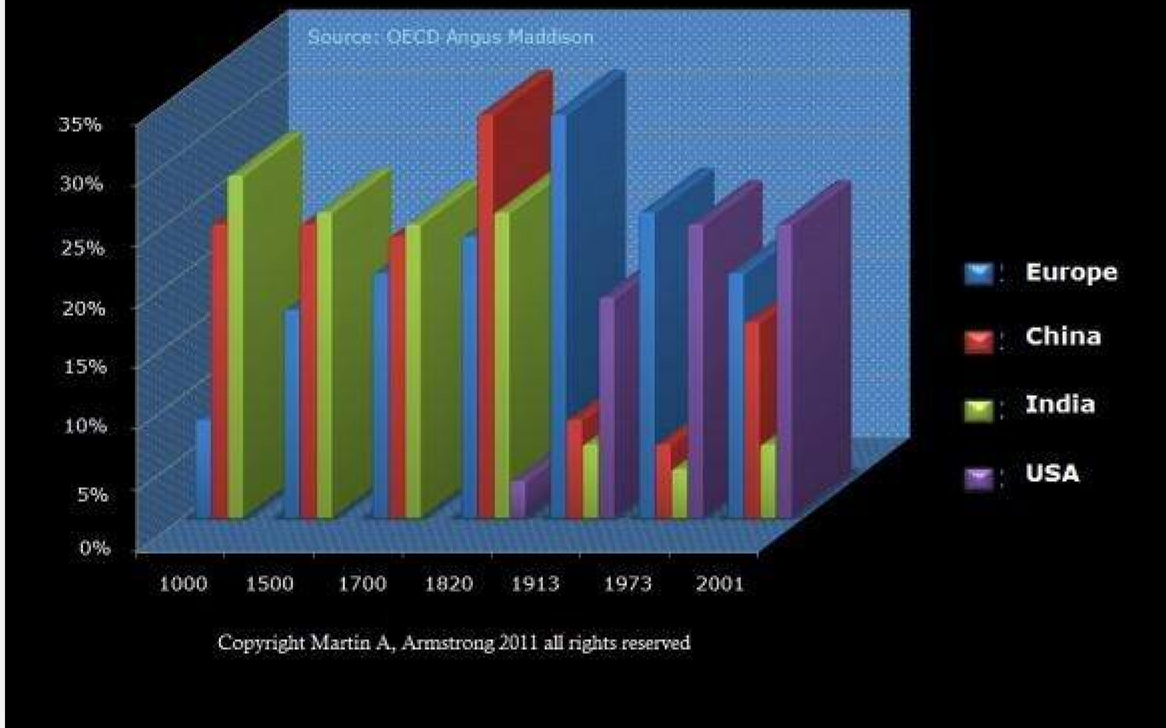
Britain retained that title until World War I as it peaked in 1914. The United States had been the emerging market and was virtually bankrupt in 1896 when J.P. Morgan had to lend it $100 million in gold. This led to the popular dislike of Morgan as many saw him as bigger than government.

J.P. Morgan - Bigger than Uncle Sam



The United States has succumbed to the very same patterns that marked the decline and fall of Rome. Here is the chart of the British debt. We can see how it skyrocketed with World War I and again with World War II. It has **ALWAYS** been debt that destroys a empire, nation, or city state. Typically, once the debt spiral takes place, the nation becomes vulnerable to invasion for it can no longer afford a defense. It was the political instability within Europe that caused World War I and that marked the peak in the British Empire – 1914. From that point onward, international capital flowed to the United States and that created the Roaring '20s as capital concentrated in the US similar to had it had performed in 1989 going into Japan. There were massive capital inflows as the United States became the next boom as an emerging market.





The greatest hidden secret from traditional economic theory is that a cycle actually exists and cannot be eliminated. Asia rose to the ***Financial Capital of the World*** after the fall of Rome and Constantinople in 1453. Asia became rich on the exportation of spices and silk. From the earliest times, we know that there was even diplomatic relations between Rome and China around 180AD. After the fall of Rome and then Constantinople, the ***Financial Capital of the World*** moved to India. After that, Indian religion infiltrated China and the ***Financial Capital of the World*** moved to China. This is why there was such a great interest to get to India and China from Europe that made the voyage of Columbus even a fundable venture capital deal on the part of Ferdinand and Isabella of Spain.

The cycle behind the migration of the ***Financial Capital of the World*** extends back in time even before recorded history. The driving force was largely weather and the ability to produce a livelihood. This drove mankind to actually populate the earth in search of the perfect land. It was about 6700 BC when the earliest city began to appear known by the name ***Catal Huyuk*** located in Turkey that covered about 30 acres. The buildings were mud and brick construction, but inside there appeared plastered walls. No doubt, this was the latest modern invention that illustrates two important developments. First, this confirms the birth of an urban trade skill and secondly, homes were found with paintings on the walls suggesting the flourishing development of art as a trade. This tends to be a luxury and therefore it is one of the last skills to develop within urban life reflecting good economic times.

It is important to understand that this cycle began with the migration of man around the world. Therefore, we see the sequence of empires emerge from the Sumerian, Babylonian, Greek, and then Roman. Once this sequence is complete, then we see the rise of India and then China. Where the Silk Road funneled wealth to Asia through trade, the roles were reversed as illustrated by Marco Polo and the voyage of Columbus.

World at a Glance

Ranked according to size of GDP

	GDP Bil$	GDP Growth	Interest Rate	Inflation	Unemployment
United States	14256	2.8	0.25	2.1	8.9
Euro Zone	12456	0.3	1	2.4	9.9
Japan	5068	-0.3	0	0	4.9
China	4909	9.8	6.06	4.9	4.1
Germany	3347	0.4	1	2	7.4
France	2649	0.3	1	1.7	9.6
United Kingdom	2175	-0.6	0.5	4	8
Italy	2113	0.1	1	2.4	8.6
Brazil	1572	0.7	11.75	6.01	6.1
Spain	1460	0.2	1	3.6	20.33
Canada	1336	0.8	1	2.2	7.8
India	1296	8.2	5.75	9.3	8
Russia	1231	2.7	8	9.5	7.4

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Asia has been following that same path of development. The ***1997 Asian Currency Crisis*** was painful, but this is what put Asia on the map beyond Japan. That event brought Asia to the attention of international capital, despite the fact that this was a very difficult period for Asia as a whole. Nonetheless, as we can see from the global comparison, the countries with the strongest growth are Asian followed by India. This is the new trend demonstrating that the cycle of migration of the Financial Capital of the World is alive and well. The debt structure in the United States and in Europe has been set on an exponential advance thanks to the need to bailout the banks after the 2007 debacle. We are looking at a massive shift in capital from the West to Asia in spite of the Draconian tax increases and the aggressive quest to hunt down Americans offshore and confiscate their wealth.

In the West, we are facing a real Global Meltdown that is brewing far beyond anything that is being traditionally covered in the general press, academia, and analytical circles. Modern man is as arrogant as his historical ancestors who always believed that somehow they were different. Debt today threatens to wipe out the entire social safety net including funded pensions. Greece was just the tip of the iceberg. Governments are imploding around the globe and there is no comprehension of what in truly unfolding.

It is the **Sovereign Debt Crisis** that is rippling through the global economy which is profoundly affecting everything we see from investment to simply surviving our own future and trading decisions. Governments everywhere are clueless. They seek only to maintain power and pray at the foot of their bed that they will wake up and everything will be back as it was. They try to create fake bailouts while never fixing the problems. We are on the verge of such a profound event, that the outcome will not be hyperinflation, but catastrophic deflation as government become more Draconian and seek to confiscate all wealth.

The United States is hunting down Americans on a global scale assuming that any account outside the United States is to hide money not for international business causing a complete reversal in world trade as the velocity of money declines. Where in the 1930s it was protectionism that shrunk the economy, today the United States is destroying itself and employment potential for the youth. In Switzerland, the record fine for speeding is 300,000SF as fines are determined according to one's net worth. Japan is also turning against its own people doubling the sales tax as its national debt will exceed $12 trillion dollars next year – not far behind the USA. Spain is in a really dire financial position. Capital is pouring out of the country equivalent to more than 50% of the annual GDP as wealth has taken flight fearing the worst lies ahead. Unemployment among the youth in Spain has exceeded 50% as civil unrest rises in the face of stupid economic policies that are driving the global economy to the brink of collapse and possibly war. Once Spain goes, there goes the EU. The Spanish banking system is on the verge of systemic complete failure. So much capital has been fleeing Spain the ECB is now pouring in on average, more than €300 billion on a monthly basis to meet liquidity needs. Since the total Spanish banking system is about €3 trillion in size, the financial crisis brewing is amounting to almost 10% of total banking assets on a monthly basis. This is simply unsustainable. Civil unrest is breakout out against austerity throughout Southern Europe and this contagion will soon affect the United States by 2014.

Governments worldwide are in crisis. There is a great disparity between the state and local governments where the latter cannot manufacture money at will as the sovereign national governments. This is a predominant source of deflation as bondholders demand higher taxes and austerity be imposed at the sovereign government levels to prevent hyperinflation and the devaluation of bond holdings. Of course bondholders will lose everything as they always do

historically. Nonetheless, in the immediate term, they will demand their pound of flesh and government will respond by extracting that from the people destroying the global economy in the process.

In France, the dramatic rise to 75% taxation imposed upon the rich is leading to massive capital flight. The French left-wing newspaper the ***Libération*** carried a headline when France's richest man, Bernard Arnault abandoned France for Belgium and the newspaper insulted him with the headline "***Casse-toi riche con!***" (Get lost, rich asshole). In the United States, Obama chastised the "rich" saying they created noting on their own and they owed everything to the state and the people. This rising tide against anyone who has more money than the next guy is threatening the collapse of Western Society and all democratic ideals. Governments everywhere are pointing to the "rich" to blame for their own fiscal irresponsibility. They are targeting even the gold dealers making it illegal to deal in cash trying to assault the growing underground economy.

Venetian "*Mouth of Truth*"

History repeats because the passions of man never change. Here is the Venetian "Mouth of Truth" that marked the end of Venetian civilization. Anyone could slip an accusation into this slot and the person names would then by charged, investigated, and even tortured. It was presumed that whatever allegation that was made was true. Worst still, you did not have to reveal your name to make the allegation. Today, tax authorities in Europe and American have reinstituted this practice. Report someone with money they are hiding and you will be rewarded with a finder's fee.

Local governments are in dire fiscal condition worldwide. The City of Philadelphia has chased out the "rich" and those left behind are the unproductive with their hands out demanding more. Governments are turning to property taxes that are not tied to income. Even in Greece they are now retroactively collecting property taxes from 2008. Regardless what you have in income, you owe taxes on the property irrespective of your current employment or income.

The city of Scranton, Pennsylvania reduced all government wages to minimum wage. In Spain, Catalonia, Spain's most indebted region, announced it could no longer pay subsides in July to hospitals, old age homes and other social services.

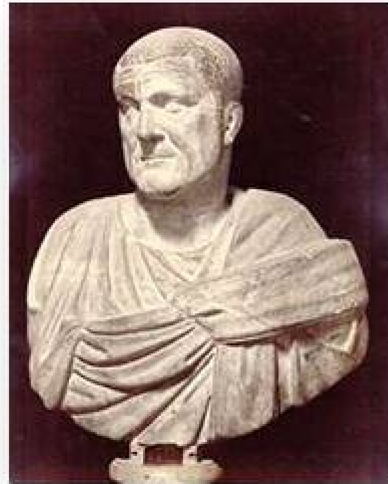
In South America, Argentina is also in economic decline thanks to debt and there too we see local governments imploding. Normally, the provincial cities receive funding from the provincial governments. However, this has dried up in some areas turning cities into cash-strapped debtors who cannot pay their bills or even their own employees. They have turned to trying a raffle to determine which civil servants will receive their pay first. Employees will queue up to get paid and when the money runs out, those in the end of the line are out of luck. The first draw for the raffle took place on Friday, July 20th. Only 23 of the town's 92 employees received their pay.

The mainstream press is simply not covering these issues. National governments continue to suppress free elections and free speech. In Spain, watch this one closely. Right now 6 out of 17 Spanish regional provinces are is serious budgetary crises. Since the federal Spanish government is itself in bankruptcy, there will be no white knight on the horizon.

Capital is fleeing everywhere, as it rightly should. Governments are in hot pursuit determined to destroy Western Civilization as they try to confiscate every scrap of wealth from the private sector as if this will somehow miraculously save the world and maintain the power. The only outcome is revolution or total dictatorial forms of government subordinating all human rights to the pleasure of the bureaucracy. Capital outflows from Spain have been more than €41.3 billion ($50.7 billion) in May, quadrupled compared to the outflow one year ago according to figures released by the Spanish central bank. For the first five months of 2012, a total capital outflow has been about €163.

This massive capital outflow is the same pattern we saw when our computer forecast the collapse of Russia that created the Long-Term Capital Management debacle in September 1998. This capital outflow is stripping banks of deposits and was the reason behind the banking conglomerate, Bankia, having requested a bailout in May. The Spanish government's response has been to try to punish capital leaving.

Governments are out of control around the globe. This is the worst possible outcome we face globally. The United States has lowered the $10,000 reporting on the movement of cash to $3,000 at the bank level. All this hatred of the rich simply causes capital to flee and when it cannot flee, it simply hoards. Either way, this is how the economy implodes. It is how Rome collapsed. The first emperor to start this process was Maximinus I (235-238AD) who simply declared that all wealth in the Roman Empire belonged to him. He too instituted a network of spies and paid rewards for the confiscation of wealth. He created the crime of "CONSPIRACY" meaning you do not even have to attempt to do something. All you have to do to be guilty is think about something. Virtually every crime in the United States at the federal level is "CONSPIRACY" today for it relieves the government of having to prove you actually did something. Maximinus prosecuted one Senator and then prosecuted 4,000 others he claimed "conspired" with him confiscating all their estates.



Maximinus I (235-238AD)

This is the same pattern that **ALWAYS** precedes the decline and fall of empire, nations, and city states. This is the trend that is going to cause a worldwide economic implosion of untold proportion. They are now trying to criminalize natural human behavior of protection one's economic self-interest. This only causes the economy to spiral down as capital seeks to merely hoard. Governments simply take no responsibility for their own actions. This is similar to a landlord renting you an apartment and saying that at any time he can raise the rent because he needs more money because he spent too much money having a good time.

The individual is always screwed. In Iceland, mortgages are adjusted according to the currency fluctuations. If you borrow 1 million Icelandic króna and the currency declines by 50%, you now owe 2 million. Banks have transferred the risk to the average person. People now owe more than what they paid for the house while wages do not fluctuate in such a manner.

The European crisis is spiraling down a debt vortex and the politicians simply refuse to reform. Germany is being dragged down the rabbit hole for the Debt to GDP ratio is up to 90% thanks to all these EU bailouts. In reality, Moody's has put the Germany on a negative watch and it could lose its AAA credit rating as was the case with France last year. The IMF is simply dead in the water.

The ***Sovereign Debt Crisis*** is brewing. We will present the only possible solution at the at the World Economic Conference along with how to shelter your net worth and survive what could become the fall of Western Society because governments everywhere simply refuse to live within their means and stop this crazy borrowing with no intention of ever paying anything back.

All of this political posturing as politicians blame the rich to try to escape their our complete fiscal mismanagement, they are laying the seeds for political unrest. There is a real danger that society goes into a total meltdown. The more aggressive governments become, the more capital will hoard. There may come the day when the mobs storm the bankers and the rich. "Black Friday" took place during the Panic of 1869 when they had to send in troops to suppress the crowds that were hanging the bankers on the street. We must realize, history repeats because the passions of man never change.