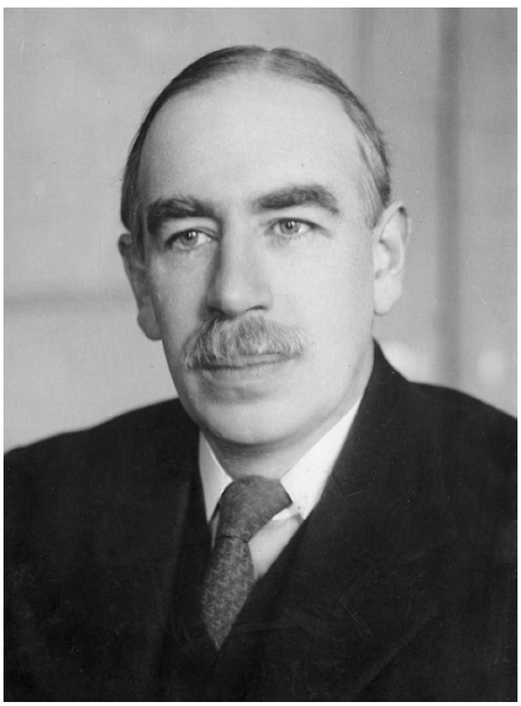
The Four Blind Mice At the Cliff March 15, 2016

Doug Wakefield

“They Keynesian economists urge adoption of a “managed currency” and various forms of government intervention in the economic life of its fellow citizens. The idea is that government should supply an economic wisdom that private enterprise lacks or is unable to use. But even these economists see the uneconomic results of the government intervention which they advocate....Can government ever supply private enterprise with an economic wisdom which it would otherwise lack?” – **Away From Freedom** (1952) Vervon Orval Watts, pg 70



“Lenin is said to have declared that the best way to destroy the Capitalist System was to debauch the currency. By a continuing process of inflation, governments can confiscate secretly and unobserved, an important part of the wealth of their citizens....As the inflation proceeds and the real value of the currency fluctuates wildly from month to month, all permanent relations between debtors and creditors, which form the ultimate foundation of capitalism, become so utterly disordered as to be almost meaningless; and the process of wealth-getting degenerates into a gamble and a lottery.” – **The Economic Consequences of Peace** (1919) John Maynard Keynes, pg 235 & 236

Do you think of the markets you have your money in as having degenerated into a gamble and a lottery? Has the constant stream of comments on centrally planning not only our economic life but the need for constant intervention into global markets and the world’s currencies left you with a feeling that the world of 2016 has come a long way from the world of even 1986?

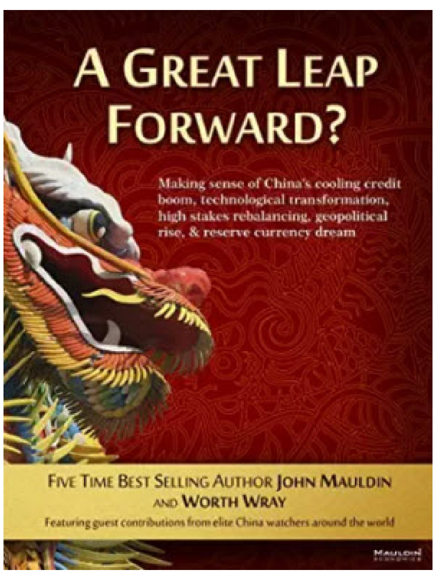
In Ludwig Von Mises’ work, **The Theory of Money and Credit**, published the year before the Federal Reserve was established in 1913, he stated “if one wants to avoid the occurrence of economic crisis, one must avoid the expansion of credit that creates the boom and inevitably leads into the slump”.

So simple, and yet ignored for decades. With each debt fueled boom, came a larger bust, and a need for more intervention by central bankers (the state) in order to make sure the latest bust could be stalled a little longer so that public at large eventually ignored such terms as bust, crash, and collapse as merely marketing terms used by “sensationalists”.

Yet today, March 15th, we are watching as the four most powerful central banks in world - the People’s Bank of China, the European Central Bank, the Bank of Japan, and the Federal Reserve – coming to grips with the reality that “assisting” an illusion of permabull has its limits.

In this short article, I will share a few thoughts and charts which I believe reveal we are at a major roadblock for central bankers and global markets. Since all we are left with is a global casino anymore, monitoring “the game” has never been more crucial.

**Booms Built Reserves, Busts Liquidate Them**




In **A Great Leap Forward?, Making Sense of China’s Cooling Credit Boom** (2015) John Mauldin and a collection of individuals from the private sector with extensive knowledge of the China economic story, make it painfully clear that what fueled the boom is now bringing enormous challenges to the leaders and people of China....and thus the world.

One statistic that boggles the mind, is that China’s total debt stock tripled between the years 2000 to 2007, and more than quadrupled between 2007 to 2014 as the private and government sectors added more than $26 trillion in NEW debt.

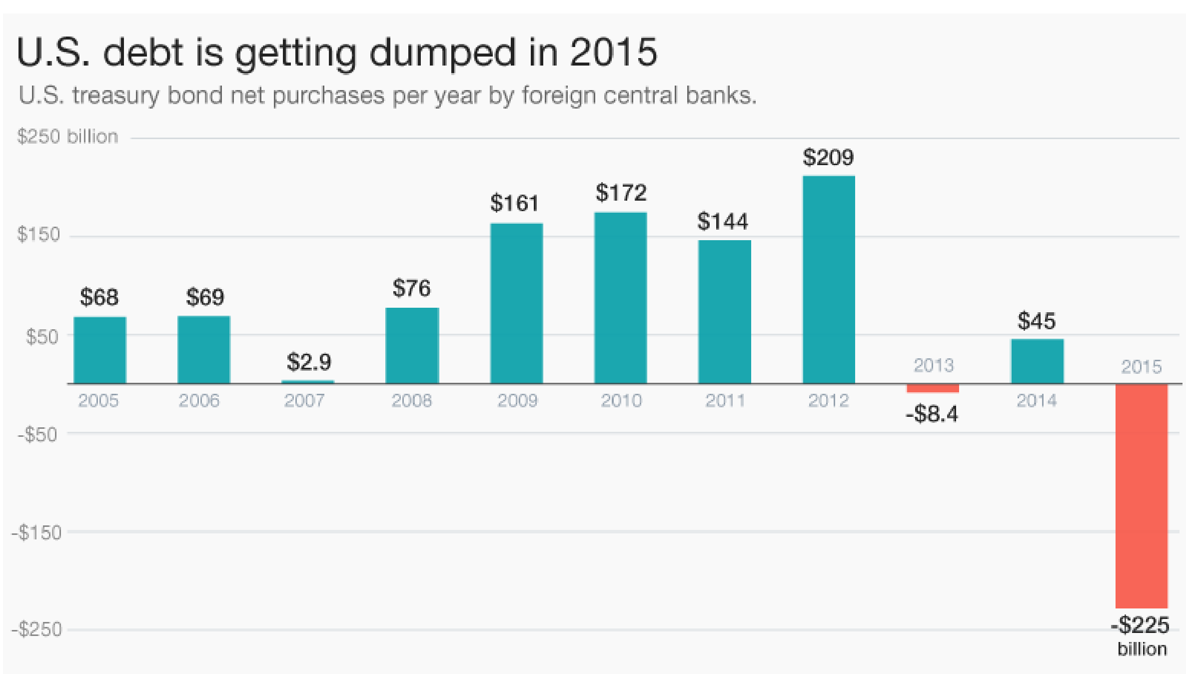
So if we compare headlines in 2009 with those in 2016, and follow the simple premise that Mises left the world over a century ago, we can understand that what we could have all predicted where this saga would bring us as we came to the end of the Great Recession in 2008. Quantitative Easing and zero or negative interest rates could never produce permanent solutions, only a method to create an even larger boom followed by a larger bust. Eventually the public would start to catch on, and cash would become king instead of focusing on never “missing out” on the next “risk on” rally.

WB Official: China a ‘Bright Spot’ in 2009 World Economy, China Daily, April 21 ‘09

China to buy more U.S. debt, CNN, March 24, ‘09

China leads global U.S. debt dump, CNN Money, Feb 17, ‘16

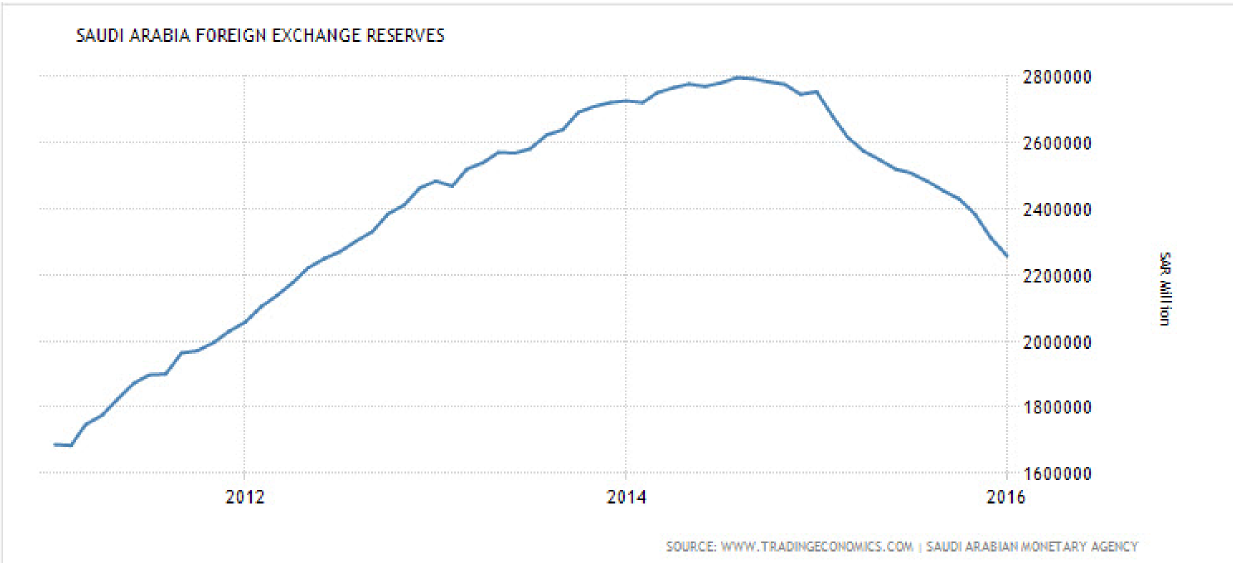
The recent CNN article points out the China sold $18 billion in US Treasury debt in December alone, and that all central banks alone sold off a net $225 billion last year, the largest amount in any year since the data became available in 1978.



So consider this. As China expanded their debt at skyrocketing speeds coming out of the 2008 credit collapse, they used this new “money” to then purchase assets and build up the nation’s reserves. However, for a nation to quadruple its debt load in 7 years, it is clearly not on a sustainable path. So as it became time for China to sell US Treasuries as part of its reserves in order to deal with its own problems at home, we can see that its reserves started falling and falling sharply.

This is no different from an individual or business that builds up reserves, and then has to use those reserves to deal with problems that have arisen.


We can see that China is not the only nation running through its reserves. Even with the price of a barrel of oil rallying recently into the upper 30s, this is still a long way from the profits oil producing nations were seeing during early 2014. Without that income to build reserves, reserves must be depleted.....and like China, rapidly.

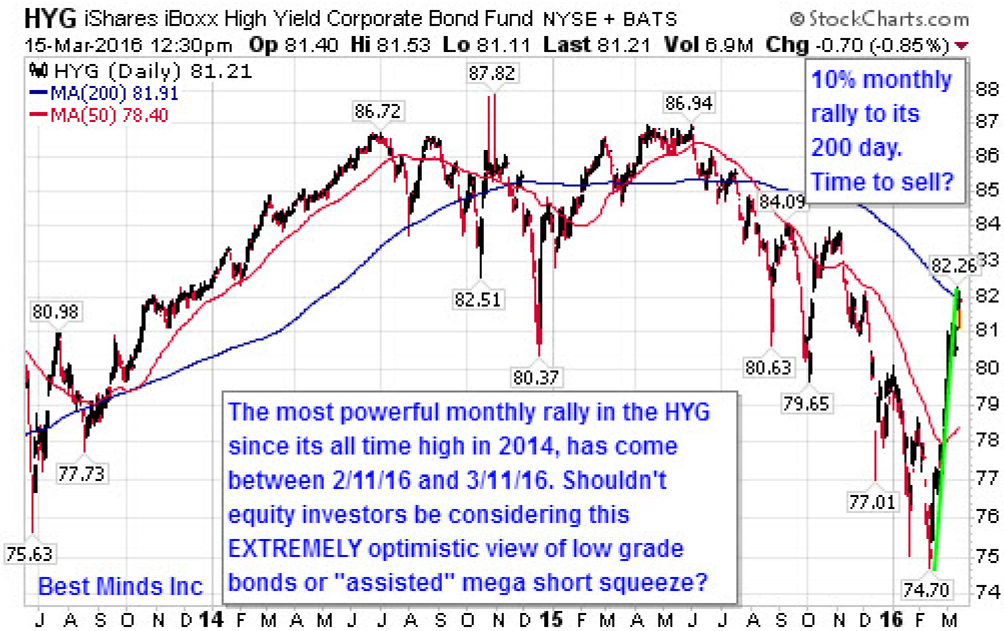



With world markets and national economies being more dependent on each other than ever before, it should also be clear that as China, Saudi, and other central banks sell US Treasuries from their reserves, so also is the US facing a big problem continuing to run hundreds of billions in deficits annually.

In the near term, if stocks and junk bonds are sold off, this could provide capital flowing into US Treasuries, pushing down yields again as a flight from risk on to risk off takes place again as we go into Q2. However, this, like all central planning, is not a long term solution. Only a huge reduction in spending by the governments worldwide, can begin to alleviate the pressure caused by coming to a point where Keynesian socialist policies have created the illusion among the public of “free money”, and our financial markets more akin to blackjack and roulette tables than havens of long term investment capital.

## Keeping a Short Term Mindset

As capital moves between bond markets, foreign reserves, currencies, and the global economy, we must also monitor the technical picture across global markets to understand where pressure points could cause short term “assisted” rallies to stall, and the reality of the bust hit investors hard.





We must also watch how currencies react to the four most powerful central banks in the world. On Thursday, March 10th. Draghi announced that the ECB was expanding its asset purchases starting April 1st, and lowered its interest rates on deposits at the ECB to negative 0.4%. On Tuesday. Kurado announced that the Bank of Japan would hold its rates on deposites at negative 0.1%. Both announcements were greeted with a flight into the euro and into the yen.

We also know before the Federal Reserve's latest press release that over $250 billion is being parked at the Federal Reserve by foreign central banks who are earning a POSITIVE 0.5% interest rate on their deposits. With the ECB and BoJ CHARGING interest on the world's largest depositors, and the Federal Reserve PAYING them interest, is there any doubt that central planners can see they have created a royal mess.


As Foreign Central Banks Quietly Park $250 Billion in Cash At the Fed, A Mystery Emerges, Zero Hedge, Feb 22 '16

Does this distorted global picture really produce an image of stability? Does it not seem to suggest that money will leave dollar backed assets and flow back into the nations of the world that have their own Keynesian socialists experiements to deal with at home?



At this stage in this global bust, denying gravity and history is very foolish.

*"Four blind mice. Four blind mice. See how they scheme. See how they plan. They all seek rallies to give men life, To keep stocks from falling, creating strife, Did you ever see such a sight in your life, as four blind mice."*

### Be a Contrarian, Remember Your History

If you are reading this article, you are already aware of the trillions that have been lost in the last 10 months. It is very clear to anyone paying attention to "the game", that the number of critical pressure points continues to rise.

Click here to start the next six months reading the paid research found in The Investor's Mind newsletters and ongoing brief market emails as we continue through this highly volatile year.

### On a Personal Note

Check out the posts at my personal blog, Living2024. The latest post is A Global Currency: Peace or Pain.


Doug Wakefield

President

Best Minds Inc. a Registered Investment Advisor

1104 Indian Ridge

Denton, Texas 76205

http://www.bestmindsinc.com/

doug@bestmindsinc.com

Phone - (940) 591 - 3000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