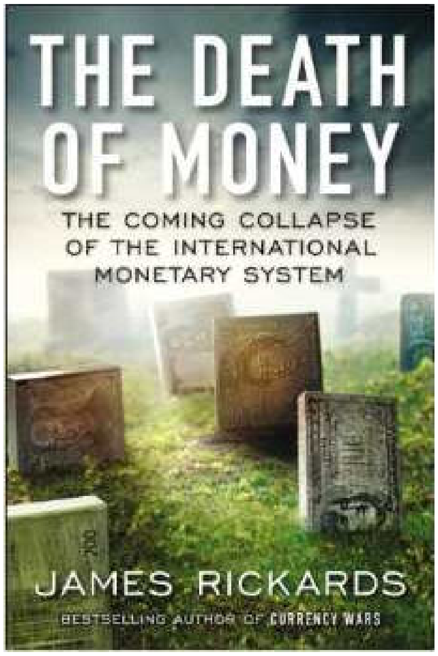
Two Worlds Collide: Financial & Political Manipulation Accepted
May 8, 2014
Doug Wakefield

"Federal Reserve policy is at a crossroads facing unpleasant paths in all directions. Monetary policy around the world has reached the point where the contradictions embedded in years of market manipulation have left no choices that do not involve either contraction or catastrophic risk. Further monetary easing may precipitate a loss of confidence in money; policy tightening will restate the collapse in asset values that began in 2007. Only structural change in the U.S. economy, something outside the Fed's purview, can break this stalemate." (1) [The Death of Money: The Coming Collapse of the International Monetary System (2014) James Rickards]



At first glance, we are prone to look at the title of this book and the graveyard image on the front cover, and label Rickard as an individual who belongs with the "end of the world" camp. We would like to dismiss his comments. Out of sight, out of mind. Besides, if we have lived through "years of market manipulation" that had brought us to a point where our financial markets and economic system were facing "catastrophic risk" or a "collapse in asset values", we would see people everywhere discussing these possibilities, and the financial industry placing "warning, hazardous to your financial health" labels on various investment strategies, right?

The problem in even contemplating comments like Rickards' is that none of us really wants to consider their ramification. I don't. You don't. Millions don't.

A change of this magnitude would mean that much of the wealth attained in the last few years was going to be destroyed again, like 2008. Even worse, it would impact the entire world around us that we live in day after day.

The longer nothing has happened in the financial markets to support the idea of "collapse in asset values", the easier it has become to dismiss the very thought that an event the size of 2008 could happen again. When we felt concerned about our own financial situation, we could rest on the fact that every "all time high" headline supported the desire to do nothing. Even as we have watched the Federal Reserve reduce the "free money" down to $45 billion a month [(2)] at the end of April ($85 billion in December 2013), the movements of the Dow seem to support the idea "all is well, don't worry, go back to sleep".

But then we are challenged with the very idea that "years of market manipulation" could be at the root of the "recovery" since 2008. If this is the case, then a centrally planned recovery could have brought us to a point where as a society, we have grown to ACCEPT manipulation and direct intervention into our financial system "for the greater good".

Clearly, when the Federal Reserve announced in September 2012 that it was ramping back up its purchases of high risk mortgage backed securities (3) to $40 billion a month (4), they believed the way Americans "feel" from being wealthy was the most important element in their strategy to return to overall economic growth.

Fed seeking to create wealth, not just cut rates, Yahoo Finance, Sept 14 '12

"The Federal Reserve wasn't just trying to drive down interest rates when it announced a third round of bond purchases Thursday.

It also wants to make people feel wealthier — and more willing to spend.
The idea is for the Fed's $40 billion-a-month in bond purchases to lower interest rates and cause stock and home prices to rise, creating a "wealth effect" that would boost the economy.

And "if people feel that their financial situation is better because their 401(k) looks better or for whatever reason — their house is worth more — they're more willing to go out and spend," Chairman Ben Bernanke told reporters. "That's going to provide the demand that firms need in order to be willing to hire and to invest." (5) [Red text my own]

Has Increasing Our Nation's Debt to Buy High Risk Assets From the Major Banks Helped the Economy?

When we consider the following data from Rickards' book on the increase in gross domestic product, currently the most widely accepted measure of economic growth, one can see that the "more debt, more wealth, feel good" model is facing a crisis. As such, the old adage "perception is reality" becomes critical for public complacency that "things have returned to normal". A continuing stream of "all time highs" is not only needed to give the image of more good times to come, but to also support the idea that we are right at the cusp of growing our way out of the trillions of debt accumulated since 2008.

"Annual GDP growth in the United States touched 4 percent in the fourth quarter of 2009, prompting talk of 'green shoots' amid signs that the economy was bouncing back from the worst recession since the Great Depression. Even when growth fell to a 2.2 percent annual rate by the second quarter of 2010, the optimistic spin continued, with happy talk by Treasury secretary Timothy Geithner of a 'recovery summer' in 2010. Reality slowly sank in. Annual growth was an anemic 1.8 percent in 2011 and was only slightly better at 2.2 percent in 2012. Then, despite predictions from the Fed and private analysts that 2013 would be a turnaround year, growth fell again to 1.1 percent in the first quarter of 2013, although it revived to 4.1 percent in the third quarter."**(6)**

Anyone watching financial trends - sadly a topic millions of Americans seem uninterested in, whether having wealth or not - would have noticed last week, that the GDP for the first quarter of 2014 had come in at a dismal 0.1%.

US Economy Grows Just 0.1% in Last Quarter, The Guardian, Apr 30, '14

No one, whether Federal Reserve staff, investment manager, or millions of Americans in the workplace can look at headlines like the ones below, and believe ALL of this can be dismissed, solely because the Dow has found it impossible to gain footing above its December 31st level for over 4 months into 2014, while at the same time has refused to decline. The REAL economy has NOT benefited from the trillions of additional debt that has been strapped to the nation's already enormous debt load since 2008. **(7)**

US Homeownership Rate Falls to the Lowest Since 1995, Bloomberg, Apr 29, '14

Retail Store Closures Soar in 2014: At Highest Pace Since Lehman Collapse, Zero Hedge, Apr 21 '14

All Signs Point to the Fact that America Has Become Little More than a Servant Economy, Economy in a Crisis, Apr 29 '14

"Since the recession started in December 2007 there are still 1.3 million fewer U.S. jobs than when the recession began."

Flood of Students Demanding Loan Forgiveness Forces Administration Scramble, Zero Hedge, Apr 22 '14

Structural Not Cyclical

Over the last two years, I have found that most individuals understand the fact that "the solution" to the 2008 crisis has been the same solution to the NASDAQ's depression level collapse between 2000-2002. **(8)** Flood the financial system with cheap credit and expect the additional borrowing, whether for consumer and business spending or increased margin loans for more investment leverage in financial markets, and voilà, recovery.

Yes it helps build a war chest of debt owed to the largest global banks in the world who are the only corporations allowed to own stock in the central banks in the world, but for the rest of us, whether your wealth exploded in size from the Ponzi scheme in the last 5 years, or you are working two jobs to make ends meet, the problems we all face is structural, requiring REAL change, not merely kicking the proverbial can down the road and trying to deny that it exist.

I really sometimes hate writing about where this has brought us, since it is much easier to talk about enjoyable and fun things in life. But lying to ourselves about the fact that we have a financial cancer is not going to make the cancer go away, no matter how much we would want to wish it away.

"The economy was in a phase not seen in eighty years. It was neither a recession as technically defined, nor robust recovery as widely expected. It was a depression, exactly as Keynes had defined it, 'a chronic condition of sub-normal activity for a considerable period without any marked tendency either towards recovery or towards complete collapse.' There was no cyclical recovery because the problems in the economy were not cyclical; they were structural. This depression should be expected to continue indefinitely in the absence of structural changes." **(9)**

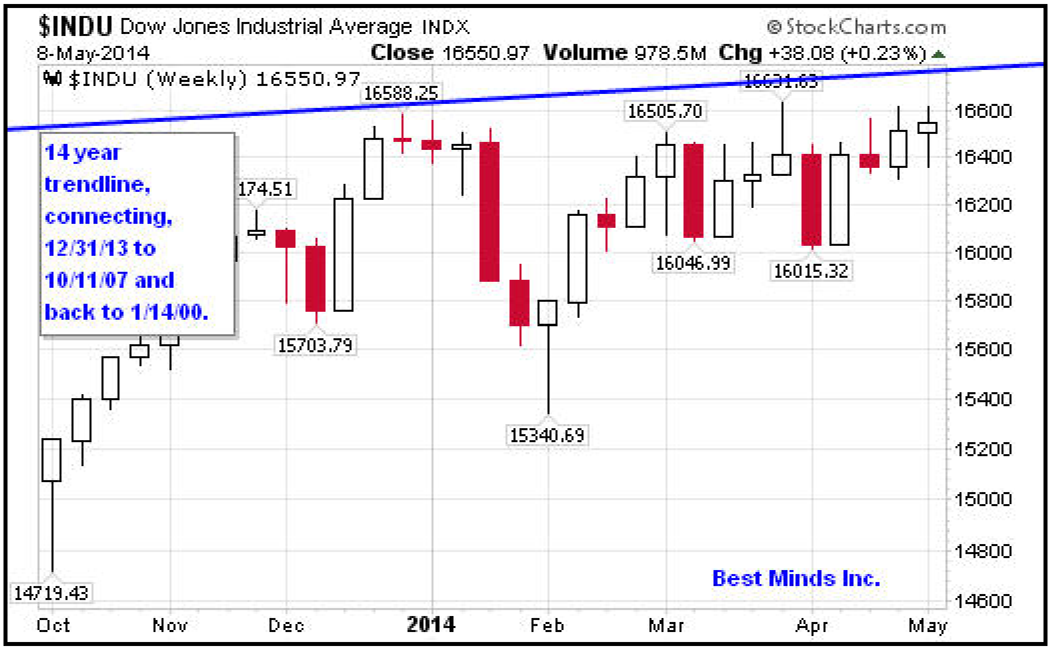
The Clock Ticks Down: Start Your Engines, or Admit Failure

I have already written on the consistent pattern of major stock, bond, and currency markets bouncing at various major moving averages. This certainly cannot be dismissed as merely a theory, since it has proven to be fact for many months now.

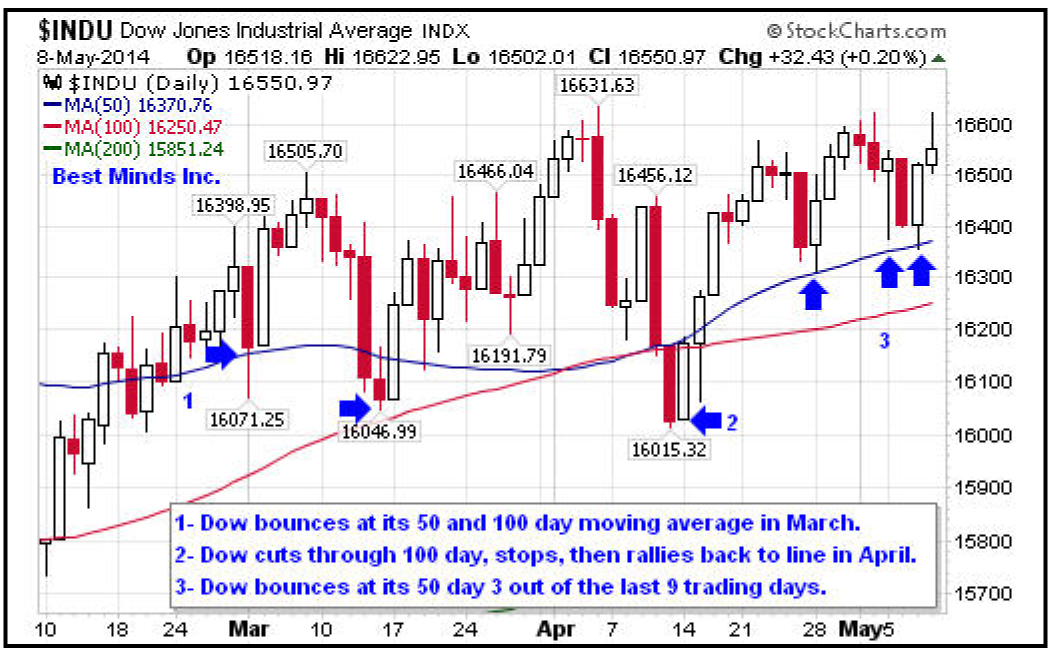
What makes 2014 very different from 2013 is that it is public knowledge that the "free money" from the Federal Reserve has been dwindling quickly. We can also see from the action of US Treasuries, that instead of money *leaving* this asset category because the Federal Reserve started reducing the amount of US Treasuries they were buying after December 2013, money has been *entering* this asset category. Notice, where the 3-year HIGH in US Treasuries took place.

Yes I believe that US Treasuries will have big problems in the future, just like the US dollar. The long-term picture becomes clearer with each passing year to anyone willing to pull their head out of the "we can always be rescued with more debt" sand. However, as money comes out of "all time high" stock and junk bond areas, it must find a home. In my opinion, that home in the next phase from "risk on" assets moving to "risk off" assets, will be areas like gold and US Treasuries.

Yes, I had rather have gold in the long run, but nothing today matches the size of US Treasuries when *the world* looks for a “risk off” area to hide.



As I look at the Dow in relationship to other major stock markets in the world, it looks very tired. When I considered its movements in conjunction with today’s hard turn down in the euro, reaching almost $1.40 this morning as European markets opened, this “never say decline” period seems very close to its end.



Last summer, on July 24, 2013, I released the public article, *The Nirvana Trade*. The "nirvana" trade, was the acceptance of the fact that someone's computers and those of "the herd", had established the fact that every time major US stock market indices came down to their 50, 100, or 200 day moving averages, they MUST start rising. I know from watching other commentators over the last several months that this pattern has been widely noticed.

The pattern has no relationship to poor global economic developments or the rising financial and military tensions between Russia and the EU & US over Ukraine. This was shown in my recent article, *Always Bet on Black*, released on March 19th. The pattern supports the fact that humans and computers, after watching this pattern consistently hit the "bounce back higher" switch, have *presently* come to see these levels as impenetrable.

But with headlines like these, how much longer can the computer gaming world of financial markets remove itself from the continued rising geopolitical and economic tensions between Russia and the West over the Ukraine? We will explore this further in the second part of this article, out next week.

Pro-Russia Group Ignores Putin Call to Delay Referendum, USA Today, May 8

"A council of the self-proclaimed People's Republic of Donetsk voted unanimously on Thursday to hold a referendum on secession from Ukraine on Sunday despite Russian President Vladimir Putin's call for a postponement.

'This is a people's referendum. There already is a civil war underway. The referendum will be the only way stop it,' Denis Pushilin, the self-styled head of the republic told journalists in a Donetsk government building seized by his pro-Russian militia in early April and turned into its make-shift headquarters....

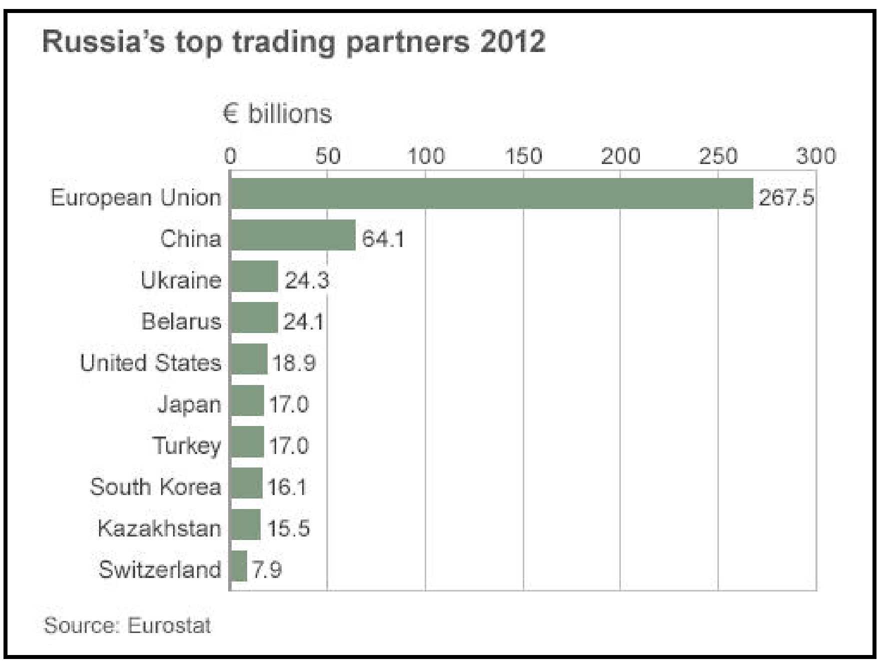
A new report released Thursday by Pew Research shows a majority of Ukrainians — 77% — want their country to remain a single, unified nation."

Russian Strategic Bombers Flying Along California Coast, Breitbart, May 5

"The Associated Press reported Monday that Gen. Herbert Carlisle, Commander of United States Air Forces in the Pacific, acknowledged a significant increase in the activities by Russian long-range strategic aircraft flying along the California coast."

NATO Fighter Jet Presence Triples in Baltic States, Zero Hedge, May 4

"With even the Ukraine authorities no longer denying civil war has broken out, the next two escalation steps are clear: first Russia, whose involvement is now just a matter of time and tactics, and then NATO."



[Source, BBC News, March 4 '14 – Russia's Trade Ties with Europe]

Preparation Time is Running Out

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If you really want to prepare for the next major bull and bear trends – some of which have been unfolding since January – come explore the paid research newsletters and trading reports available with a six month subscription to The Investor's Mind.

Sources:

(1) The Death of Money: The Coming Collapse of the International Monetary System (April 8 '14) James Rickards, pg 243 of 356
(2) Federal Open Market Committee Press Release, April 30, 2014
(3) One of the earliest quarterly derivatives reports, Q4 1996, calls mortgage backed securities, "high risk mortgage securities". Neil Barofsky was appointed as Special Inspector General of the Troubled Asset Relief Program in early 2009. His comments regarding the basis of "the rescue" from the 2008 crisis reveal the same "high risk" terminology in his book, **Bailout: An Insiders Account of How Washington Abandoned Main Street While Rescuing Wall Street** (July 2012): "The initial TARP proposal, made by Paulson, was for the money to be used to buy large quantities of the 'troubled' or 'toxic' mortgages and mortgage-related bonds that were clogging so many banks' balance sheets; hence the name Troubled Asset Relief Program. The sharp decline in the value of those assets, starting in 2007, was what had precipitated the crisis, and the argument was that the banks could not be stabilized until large quantities of them were taken off their books."[pg 25 of 270 in Kindle Edition].
(4) Once the original "rescue" by the Federal Reserve, of creating debt out of thin air to purchase over $1 trillion of these high risk financial instruments off the books of the major banks was completed in March 2010, why was the public not WARNED that to start up purchasing an additional $40 billion a month of these financial instruments, would eventually lead the Fed into a corner, finding it all but impossible to sell something the major banks had been getting rid of by selling them to the Federal Reserve since the 2008 crisis? On September 13, 2012, the Federal Reserve's balance sheet revealed they were holding $843 billion in mortgage-backed securities. The

most recent release on May 1st shows a total of $1,632 billion, an app. 100% increase since Sept 2012.

(5) Article quoted in *Powder Kegs and Photo Ops*, Sept 19 '12

(6) The Death of Money, Rickards, pg 244 of 356

(7) The chart to the right was posted on the Weekly page of the Best Minds Inc website on 2/25/14. Since that time, 4/4/14 marks the highest level of the Wilshire 5,000 at $20, 257 billion, the US Treasury reporting that our national debt reached $17, 555 billion on that same day, thus the ratio of stock wealth to national debt on April 4, 2014, reached a ratio of 1.15: 1. Notice where this ratio stood at the January 2000 top and October 2007 top.

Stock Wealth Versus US National Debt:
Our net worth declines as we are told, "More debt leads to recovery"

Date	14-Jan-00	10-Oct-02	11-Oct-07	6-Mar-09	24-Feb-14
Stock Wealth	$14,991	$7,274	$15,938	$6,772	$19,924
Nat'l Debt	$5,719	$6,240	$9,042	$10,951	$17,411
Ratio	2.62:1	1.16:1	1.76:1	0.62:1	1.14:1

** Dates are Major Tops and Bottoms since Jan 2000, with the current "all time high" in 2014*
** Public Stock Wealth is based on the market cap of the Wilshire 5000*
** US National Debt comes from the US Treasury*
** amounts in billions* — *Best Minds Inc - Feb 25, 2014*

(8) From the top in 1929 to the bottom in 1932, the Dow plunged 89%. From the top in March 2000 to the bottom in October 2002, the NASDAQ 100 plunged 83%.

(9) The Death of Money, Rickards, pg 244 of 356

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