Volume 47 | Issue 1 . January 18, 2013

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THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

ECONOMIC WINTER

Economic Outlook for 2013

Introduction

I know that Longwave Analytics is considered to be just like the boy who cried wolf so many times that when the wolf actually did appear and the boy again cried wolf, no one believed him and the wolf killed the flock of sheep. The moral of the fable is that if you lie too frequently, when you do tell the truth no one will believe you anyway. Of course, we are not lying when we tell you how dire things really are. The truth is it is the Government and the Federal Reserve that are lying. They are lying in an effort to convince you that they have everything under control. They are lying when they present you with their numbers, like GDP and unemployment. They are manipulating markets, like the stock, bond and gold market; the stock and bond markets to the upside and the gold market to the downside. They have protected the lying, cheating bankers from imprisonment for perpetrating massive fraud which has led to abject misery for millions of people in many countries. We believe that in 2013 these lies will be exposed and the whole fraudulent structure will come crashing down.

Why 2013? This Long Wave winter is now well beyond its ‘best by date’. The worst of the previous Long Wave winter lasted only three and a half years, between September 1929 and March 1933. Between those months 10,000 US banks failed, US unemployment reached a peak of 25%, the GDP collapsed by 45% and the Dow Jones Industrials Average lost 90% of its value.

This winter started in January 2000, when the DJIA peaked at 11,750 points. As of January 14, 2013 we will have been 13 years into winter. During that time less than 500 US banks have failed; official unemployment numbers are 7.7%, whereas John Williams who monitors official government statistics on his website Shadow Government Statistics estimates total US unemployment is currently at 22.2%; official GDP is plus 2% and the DJIA is 14% higher than its onset of winter price peak in 2000. Thus, from this point on things can only get worse and that’s a lot worse.

Another reason for our belief that 2013 is going to be a dismal year is because central banks have run out of road down which to kick the can. We have demonstrated to you several times that once a fiat money system starts to collapse, governments create huge amounts of new money in an effort to get the economy going again, all to no avail. What this panic money printing does is destroy what remains of confidence in paper money which in turn, instigates a flight to gold and silver. The flight to the precious metals has been building over several years and is now coming to the stage where the precious metals are being accepted as alternative money.

The Outlook for Gold and Silver

I trust you know that the indices of the general stock markets always move in the opposite direction to the price of gold over the longer term. This is best depicted in the Dow Jones industrial Average/Gold price ratio which is posted on our website and updated daily. What is most interesting is that this ratio reaches extreme highs or extreme lows around the changes of the Long Wave seasons. We know that share prices always perform very well during the Long Wave spring, which signifies the re-birth of the economy and during the Long Wave autumn, which always has been the season of speculative excess. It is at the end of spring and autumn that the ratio reaches a significant high. During the Long Wave summer, which has always been the inflationary season, stocks perform poorly and the price of gold rises much higher. In the winter the stock bear market is every bit as bad as the previous autumn bull market was good and the huge demand for gold pushes prices significantly higher. The Dow/Gold ratio reaches extreme lows at the conclusion of summer and winter.

The point that I am trying to make here is that as at December 31, 2012, the ratio was at 7.75; it took the price of 7.75 ounces of gold to buy the value of the Dow Jones industrial Average. Although this ratio has fallen significantly from its autumn ending peak of 43.75, it is nowhere near the extreme low that we should expect at the end of winter, which given past lows would be a 1/1 ratio, although I expect something closer to .25 to 1 (Dow 1,000/ Gold $4,000). To this end we should be comfortable knowing that the price of gold has much more room to move to the upside.

At the close on December 31, 2012 the spot gold price was $1,673.50 (U.S.) which was up almost 8% on the price at the start of the year. It is our belief that the gold price will move significantly higher during 2013. We have several reasons for making this pronouncement.

1. The year 2013 is likely to be an economic and financial disaster as has been discussed elsewhere in this report. The demand for physical gold thrives in such extreme unsettled times.

2. Given this huge projected demand for gold, it is likely 'the powers that be' will lose their control over the gold price. If you don't believe that governments and particularly the US government are actively controlling the price of gold, then you should read GATA's excellent work in proving gold price suppression over many years. (www.lemetropolecafe.com). It stands to reason why governments would want to control the price of gold; they want you to believe in their bogus fiat currencies. Once they lose control of the gold price, this will add impetus to the rising price of gold.

3. 2013 might well be the year in which the entire world monetary system collapses into a pile of worthless paper. The ramifications of such are frightening to contemplate and we will give further discussion to this later in this paper. However, such a debacle would result in a massive flight to gold and to a lesser extent silver. The demand for gold would come from governments and wealthy individuals, whereas silver would be the choice of the less wealthy individuals.

4. In the midst of this frantic desire to own gold, more and more governments will want to take control of their gold and repatriate it from the vaults of foreign central banks. This will likely expose the fraud perpetrated by these central banks, the principal custodians of various governments' gold, because it will be evident that there is only a fraction of gold remaining in their care. Most will have been loaned out, sold or perhaps stolen.

Thus, you have the perfect storm developing to drive the price of gold to unimaginable levels.

As for silver, we simply don't see it enjoying the historical status that gold enjoys as money sans pareil. In Great Britain, gold replaced silver as the monetary standard in 1717 under Sir Isaac Newton's tenure as Master of the Mint. During the 19th Century gold became the international monetary standard. At the outbreak of the First World War gold's international monetary role was broken. After the war a modified gold standard system was re-introduced. That system collapsed between 1931 and 1933 at the onset of the depression. At Bretton Woods in 1944 gold was re-introduced as a monetary instrument backing the dollar at $35.00 (U.S.) per ounce. That relationship was severed by President Nixon in August 1971 and since that time the entire world as been subjected to a floating fiat currency system which is the cause of the current crises. Nevertheless, gold not silver has been the mainstay of the international monetary system, with a few small interludes, from 1717 to 1971. Most central banks still hoard gold as a backing to their fiat currencies. In recent years several central banks, notably those of China and Russia have been substantially increasing their position in gold. Central bank gold purchases in 2012 amounted to 500 tons. Thus, it might be argued that gold has been a monetary lynchpin for almost three hundred years. We don't see silver breaking gold's historical monetary tradition.

Silver will play a monetary role in the coming economic, financial and monetary catastrophe, but one that will be in a subordinate position to gold. Silver plays an important industrial role. We see industrial demand for the metal being significantly reduced as the winter worldwide economic depression intensifies.

Several influential and very respectable analysts, including my friend Eric Sprott, believe that silver will outperform gold in the coming decade. They believe that the gold/silver price ratio could fall to as low as 16/1. At present the gold/silver price ratio is close to 50/1 and it is our belief that the value of the ratio will not be significantly changed from its current level during the coming crisis.

In the following chart, the gold/silver price ratio is depicted from 1971, which is the year that President Nixon took the dollar off gold. From that time on, the price of gold supposedly has operated in a free market. The silver price, on the other hand, has been subject to the laws of supply and demand since the middle of the nineteenth century. The study of this chart, therefore, allows us to view the price action of the two metals relative to each other when each has been operating according to the laws of supply and demand. After 1982, the price ratio has stayed most of the time above the geometric mean of 51.46, and as we have already written, we don't see the ratio dropping significantly below that mean.

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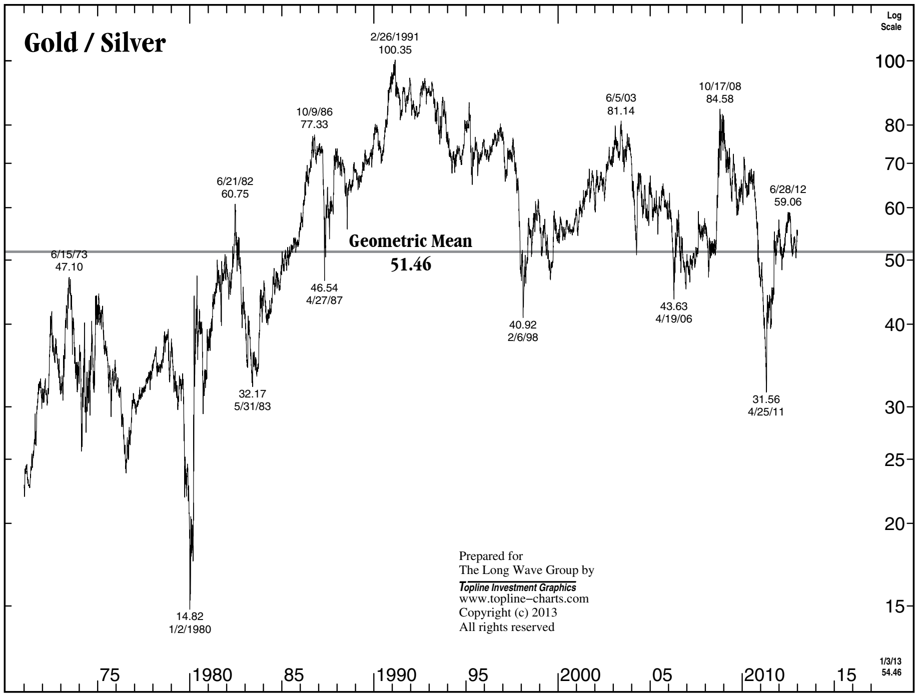


Stock Market Outlook

Our outlook for the stock markets in 2013 and in particular the US stock market, hasn't changed since our November 5th publication of **"Ian's Investment Insights"**, which you are encouraged to read.

What you should understand about this outlook is that directly in front of us lies a catastrophic stock bear market. Robert Prechter writes that the stock market situation is 'terminal.' Dr. Robert McHugh writes "This is a major Topping Formation that is the Multi-Century Top. This is a Broadening Top, Megaphone Top pattern. These patterns are reliable and appear at tops. This one is huge, as it should be the conclusion of a multi-century rally. We call it the Jaws of Death pattern." Dr. McHugh believes that the pattern will be complete once the DJIA reaches between 14,500 and 15,000 points.

Can it do that? Of course it can. Anything is possible in the markets and given the amount of government price support, and the front-running and insider trading that this support encourages, stock prices can rise to levels that are far beyond where they should be given the real state of the economy. But in the end all that doesn't matter because all the lying and cheating cannot maintain prices at inflated levels once the collapse begins as between 2000 - 2002 and 2007 - 2009. If you want to understand how corruptly the game is played I encourage you to read Octopus: Sam Israel, The Secret Market and Wall Street's Wildest Con by Guy Lawson

From our perspective, it is difficult to envisage such a move, but there's no telling what kind of market manipulation the Federal Reserve and its cohort bankers can undertake to raise stock prices to such unfathomable levels.

During the October 1929 stock market crash, the bankers led by J.P. Morgan intervened only once to try and stem the tide of selling that gripped the market following the crash in prices on October 23rd and the continuation of that crash the following day,Thursday October 24th. Following that meeting early in the afternoon, Richard Whitney, who was the Acting President of the New York Stock Excahange and also Morgan's floor trader appeared on the floor and began placing buy orders for up top 20 different stocks. "This was it the bankers, obviously, had moved in. The effect was electric. Fear vanished and gave way to concern lest the new advance be missed. Prices boomed upward" Galbraith, J. K. The Great Crash1929.

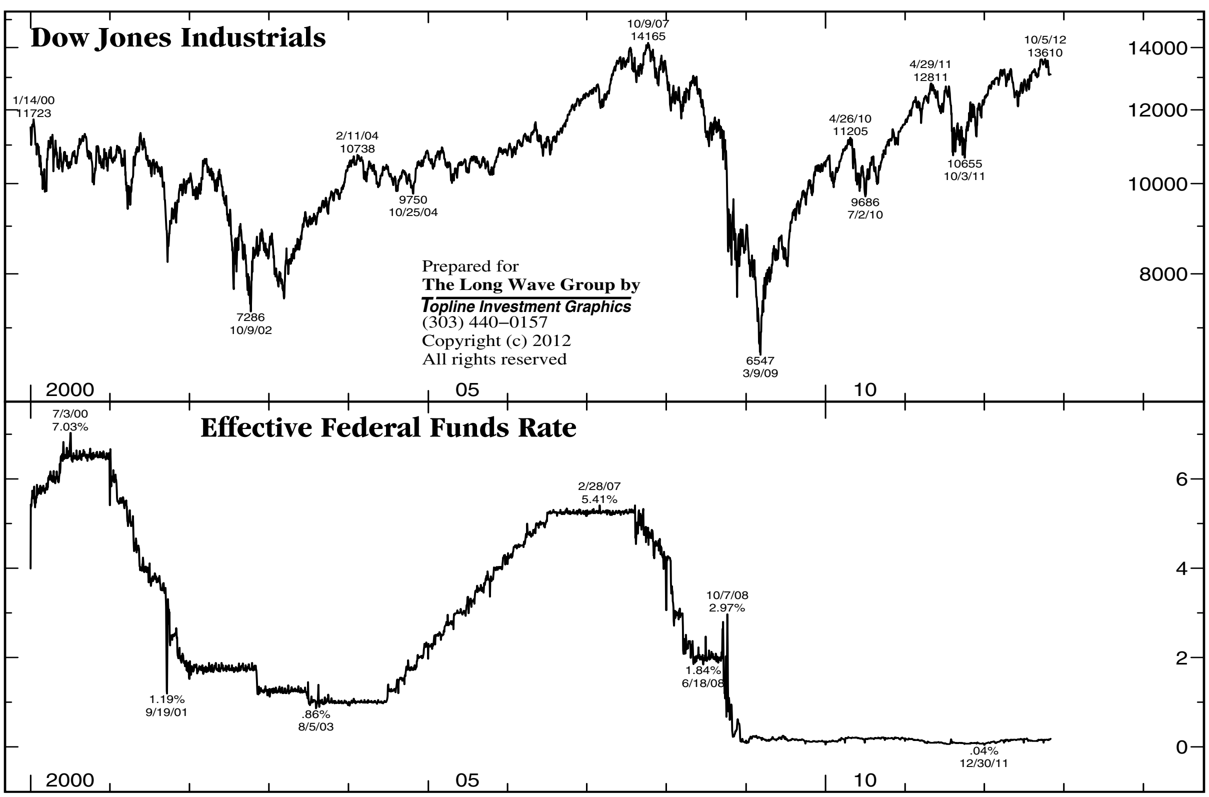
Three trading days later stocks were again met with a wave of panic selling and the bankers wisley stood aside allowing the natural course of events to take place. Hence, the third winter bear market as bad as it was, lasted less than three years and was over by July 8th, 1932.

The current winter bear market as evidenced by the Dow Jones Industrials Average has now been ongoing since January 14, 2000 (13 years), when the DJIA peaked at 11,750 points. That peak was followed by a decline to 7,286 by October 2002. To combat that fall and in an effort to reignite confidence, Alan Greenspan the Federal Reserve Chairman cut the Federal funds rate to just over 1% from the 7% rate it had been at the stock market peak in 2000. This achieved the desired effect, the stock market resumed its upward trend and rising consumer confidence was reflected in an orgy of real estate buying. As stock prices recovered and the real estate market boomed, the Federal Reserve slowly began to increase the Federal funds rate to the point that by mid 2006 it was set above 5%.

By October 2007 the Dow made a new high at 14,200 points. From that level, stock prices collapsed into March 2009 below the October 2002 low. Once again the Federal Reserve responded by lowering the Federal funds rate, ultimately to a level essentially at zero. At the same time using all kinds of nomenclature for money printing, such as TARP and Quantitative Easing, the Central Bank flooded the banks with money, of which most has been used for speculation, principally in the stock market. As a result of these actions by the Federal Reserve the stock market has recovered from the dark days of early March 2009 to the point where the DJIA sits 13% higher than the 11,750 point peak at the onset of the winter bear market and within striking distance of its all time high of 14,200 points.

Certainly, early 2013 stock price action would support Dr. McHugh's hypothesis that the 'Jaws of Death' will complete with the Dow meaningfully above 14,200 points and negate my theory that the the price peak was made in October 2012 when the Dow reached 13,662 points. Regardless, 2013 will very likely be a horrible year for not only U.S. stocks, but also stock markets around the world.

Once the stock deluge recommences, the Federal Reserve will be powerless to intervene as it has done consistently on any index break since the 2000 peak. With interest rates at zero and monetary stimulus totalling $1 trillion (U.S.) per annum, the Federal Reserve has no more ammunition to shoot at the enemy of declining stock prices.



Imagine what will be the repercussions of the coming hemorrhage in stock prices . . .

- Huge loss of wealth. The current value of all US traded stocks is approximately $15.2 trillion (U.S.) (Wilshire 5000 Index). A 90% drop in stock prices a la 1929-1932 would drop the total value of US equities to only $1.5 trillion.
- Pension and retirement plan destruction.
- Economic collapse. In the third Long Wave winter U.S. GDP dropped by 45% into 1933.
- Staggeringly high unemployment. U.S. unemployment reached 25% in the previous depression. It is likely to go considerably higher than that during this depression simply because overall debt is significantly higher than it was prior to the onset of the 1930’s depression.
- Debt implosion leading to extensive bank failures and the collapse of credit.
- Major civil unrest.

Euro Currency Crises

The world monetary crisis, currently most evident in the euro, has been ongoing for at least four years. Confidence in all major currencies is on the wane, as evidenced by the rising values in gold and silver.

Mario Draghi, President of the European Central Bank has promised to do whatever it takes to keep the euro alive and at this point in time he has succeeded, but at great cost to many people. In the United States and Great Britain the Federal Reserve and the Bank of England having been buying copious amounts of their national debt to bolster the dollar and the pound and maintain their respective national debt interest rates at historically low levels.

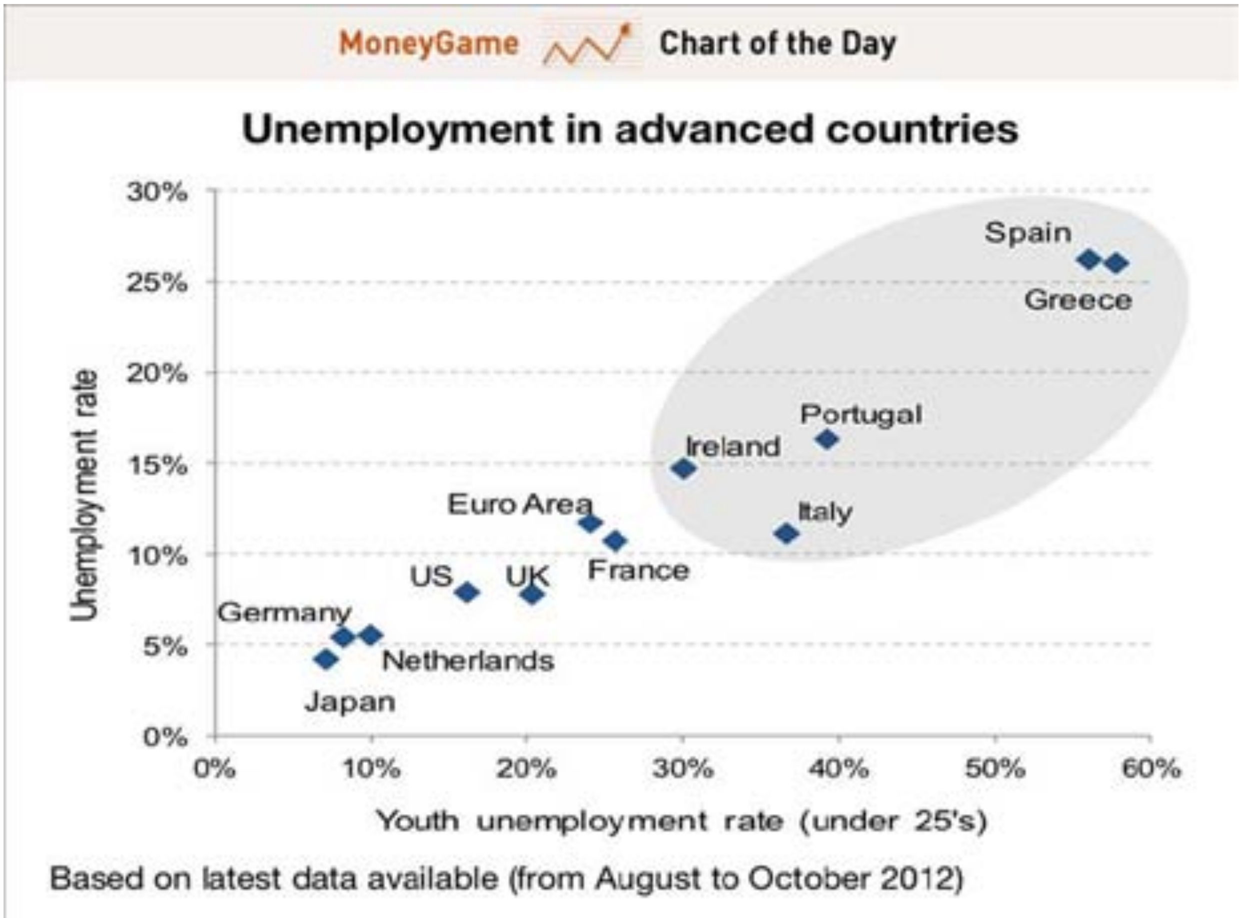
People have been fleeing and taking their money out of crisis countries like Greece, Spain, Italy and France into countries considered to be more stable such as Germany, Switzerland, Great Britain and in some notable cases Russia. I have been told by a Canadian banker that an increasing number of U.S. citizens have been transferring money out of their U.S. banks into Canadian ones. The number of U.S. citizens renouncing their US citizenship although still quite small, it is projected that about 2000 did so in 2012, but that number has increased by two and a half times since 2008.

The European Central Bank and some of the key European countries led by Germany are desperately trying to keep the euro from disintegrating because thay know that such an event would lead to a collapse of the worldwide banking system. They are fighting a rearguard action, because it now appears that the monetary crisis has spread from the periphery countries to the core, in this case France.

Commenting on a Washington Post story headlined “European leaders hail breakthrough in debt crisis.” Washington Post, January 5, 2013, Sage10 wrote-” The Euro Zone is just entering a new phase in its economic crisis. Economies are weakening. France elected an idiot socialist as their Prez, who promptly killed investment in France by raising income tax rates to the highest in the Euro Zone. France not Spain, Greece, or Portugal is the real sick man of Europe that will end the Euro and provoke a huge economic crisis. We are not immune. Our four largest banks control most of the USA’s private assets, and they are exposed to risk, since they hold a lot of European bank debt....not to mention 227 trillion....yes, trillion....3.3 times entire world GDP in worthless derivatives. Meanwhile, the U.S. debt continues skyward at $1 trillion (U.S.) on the barbie every year. Recovery? I’d be genuinely surprised, if we don’t have a worl-wide monetary system collase by the end of 2013.” And so would we.

Europe

As recently reported in the Daily Telegraph U.K., the primary cause of Europe's economic woes is a north-south incompatibility crisis; the result of fusing together misaligned economies into a single currency. **At Longwave Analytics, we do not believe the democracies of southern Europe can withstand a prolonged state of depression, with no light at the end of the tunnel.** Eurostat has reported the euro zone unemployment rate rose to a record 11.8% as 18.8 million people were without jobs in November. Moreover, the overall unemployment rate for 15 to 25 year-olds in the euro zone was 24.4%, up from 21.6% in October. Indeed, in Greece, youth unemployment now stands at almost 58%, while in Spain it's almost 57% and in Italy it's 37%. In terms of raw numbers, almost 5.8 million young people are unable to find work in the 27-member European Union, with more than 3.7 million of them in the euro zone. Clearly, a lost generation is being moulded throughout southern Europe, threatening further social unrest and turmoil.



In Spain, the General Workers' Union announced that nationalized lender Banco de Valencia, recently absorbed by La Caixa – Spain's largest retail bank – is about to lay off 890 workers, more than half of its work force. As reported in the Times of London, Spain's financial sector is expected to shed as many as 12,000 employees this year, as smaller savings banks are taken over by larger lenders. Banco Santander, which recently took over Banesto, is expected to cut up to 3,000 employees as part of a restructuring plan which will involve closing 700 branches. Bankia, the country's fourth-largest lender which was nationalized last May is expected to sack 6,000 workers. Novagalicia Banco, another nationalized lender, has proposed shedding 2,508 jobs and closing 315 branches by 2015. Catalunya Banc, yet another nationalized lender, is expected to be sold early this year in a move that will probably mean additional job losses. The banking sector is despised by many Spaniards because it has received billions of euros of public funds to bail out four lenders while public services – such as health and education – have been slashed by the centre-right government of Mariano Rajoy, which is determined to reduce the country's deficit.

Spanish Prime Minister Mariano Rajoy Source: Associated Press

However, Spain has been quietly tapping the country's richest pension fund – the Social Security Reserve Fund – as a buyer of last resort for Spanish government bond issues, raising serious concerns about the Fund's role as guarantor of future pension commitments. Now, however, the scarcely noticed funding spree, executed amid a prolonged economic crisis, is about to end because the Fund is reaching its limit. So, the Spanish Treasury has announced plans to issue a record 121.3 billion euros ($158.53 billion U.S.) of government bonds this year, 7.6% more than in 2012. This figure includes 23 billion euros for the country's semiautonomous regions, most of which have lost access to financial markets. This week, the Treasury will auction 4 billion to 5 billion euros of bonds, split between a new 2-year bond and a reopening of 2018 and 2026 maturities.

Italy, which like Spain saw its outstanding bond yields rise to unsustainably high levels when the euro zone crisis deepened last summer, will also launch its first 2013 bond auction this week, as the country heads toward February elections, that are widely seen as a referendum on the country's austerity program. Italy plans to auction 410 billion in bonds and treasury bills in 2013, down from about 470 billion euros in 2012. Since the European Central Bank (ECB) has promised to buy Spanish and Italian bonds in the secondary market, should those countries seek an international bailout; the yield on Spain's 10-year bonds were at a 10-month low last week at 5%, while Italy's equivalent yield was at 4.22%, the lowest since 2010. **Given the state of Spain's economy, replete with growing unemployment and a contracting gross domestic product, we cannot see the country avoiding an international financial bailout in 2013**.

As reported in the Wall Street Journal: Once the vibrant commercial heart of Athens, the capital's central Omonia Square now is ringed by shuttered hotels, vacant shops and haunted by drug dealers, addicts and prostitutes; making it a national symbol of despair and social collapse. The square, whose name means harmony in Greek, and the neighbourhoods which stretch around it have been ravaged by the country's depression, a flood of illegal immigrants and austerity measures which have severely undercut the government's ability to cope. The depth of the urban disintegration there reveals the complexity of the problems Greece faces, as the country enters into a sixth year of economic contraction, plus it is a warning to other crisis-hit European countries about how swift the fall can be when a tipping point is reached. With police struggling to control the chaos, street battles have erupted between groups of ultra-nationalists – who carry out attacks against immigrants and wreck their shops and market stalls in the neighbourhoods around the square – and anarchists who say they are fighting fascism and want to protect foreigners. In the case of Omonia Square and surrounding areas, a massive inflow of illegal migrants desperate to get into the European Union has collided with a lack of jobs in Greece's moribund economy and diminished public and charitable resources to help them. **We are hard-pressed to see Greece retaining its European Union membership throughout 2013.**

As far as Germany is concerned, about 80% of the German electorate think Chancellor Merkel is doing a competent job. If the German election, scheduled for September of this year, were held today, 40% would vote for Merkel's Christian Democrats, leading the Social Democrats by 10%. Our question remains: Will the German electorate continue to support Ms. Merkel and her party in September, if in the meantime weak sister countries of the Mediterranean periphery either exit the euro zone, or require additional financial bailouts?

Japan

Japan's sovereign debt has recently reached a new milestone by crossing the one quadrillion yen mark, which is one thousand trillion, or 1,000,000,000,000,000 yen; representing about 220% of the nation's gross domestic product (GDP). Today, as noted by the Privateer, Japan's population has one of the longest life expectancies in the world, with well in excess of 20% of the population over the age of 65. Since immigration is all but non-existent, the revenue base to support the gargantuan level of government debt is falling inexorably. The current population of Japan is 127.7 million people. Japanese government researchers have concluded should Japan's current birth rate continue at present levels or diminish further, the population of the country will decline by two-thirds over the next century. By any scale of measurement these are scary figures.

Undaunted, Japan's newly elected Prime Minister Shinzo Abe has announced his government will soon draft a package of emergency stimulus measures, intended to bolster the nation's long-stagnant economy. "The stimulus will be the first step in our economic revitalization program." Japan's Yomiuri newspaper reports the government's stimulus package will total 10.3 trillion yen ($116 billion U.S.), with half the funds being allocated towards public works projects and overall creating 600,000 new jobs. Moreover, through the combination of government and private sector spending, the stimulus measures could expand to more than 20 trillion yen.

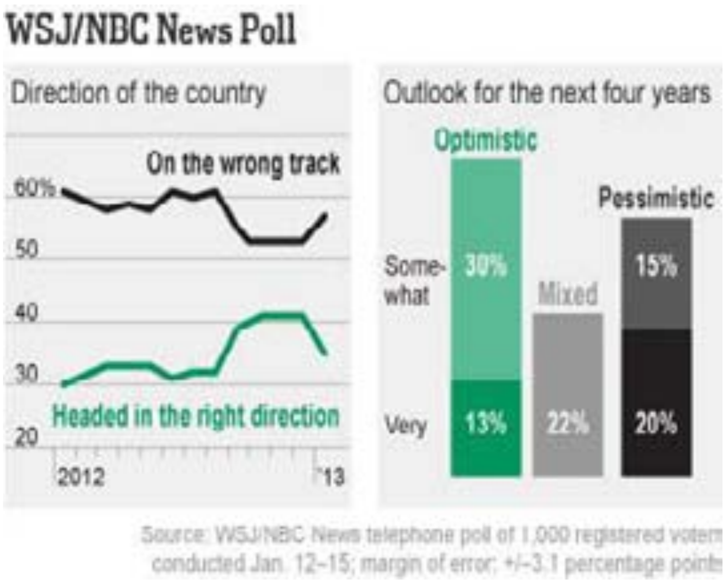
An outline of the stimulus package approved by the government includes a call for the government and the Bank of Japan to create a mechanism to strengthen cooperation to swiftly overcome deflation. It also said the government will "continue to keep a close eye on movements in the foreign exchange market and respond appropriately." It also stated the government would invest in infrastructure for disaster prevention following the March 2011 earthquake and tsunami. The plan calls for stimulating private sector investment to promote economic growth, supporting research plans in various fields and investing in renewable energy. Kyodo News reported the government is considering issuing 5 trillion yen of new construction bonds, bringing total new debt for fiscal 2013 to about 50 trillion yen. Moreover, Japanese Finance Minister Taro Aso has unveiled plans to purchase bonds from the European Stabilization Mechanism (ESM) using foreign exchange reserves to fund the initiative: "Stabilizing Europe's financial crisis will eventually contribute to the stability of other currencies including the yen, so we plan to keep purchasing ESM bonds."

Japan is now drowning in such an ocean of debt, it is difficult to see how the country will ever be able extricate itself; the above-mentioned new stimulus, notwithstanding. Given the country's demographic challenges and the mountain range of outstanding government debt, it is only a matter of time before a wholesale rollback of the currency will be required. Japan is set upon a journey down a river of no return.

The United States of America

Although the United States has recently averted the fiscal cliff as a result of a political compromise on various taxation measures, many fundamental problems remain seared in the nation's fabric which will spell deep trouble in the months and years ahead. One of the most serious impediments within the American system of government lies at the very feet of the country's elected representatives in Washington. Mistrust, partisan politics and an outlandishly ridiculous lobbyist system are rendering the U.S. Congress and Presidential Administration into a state of dysfunction and serious political gridlock. The entire calendar year of 2012 was wasted on an expensive election campaign that solved nothing by a basic return to the status quo. Political debate seems to be regarded as an anachronism, while mutual vilification of one's political opponent seems to be applauded along party lines. As an elected representative of the people, once you begin treating your political opponents like enemies, instead of adversaries, you will morph into a 'dead bear in the water' and as a result, accomplish nothing.

America has reached the stage where, as a result of self-inflicted financial wounds of lobbyist aggrandizement over the decades, the country is sailing into a state of economic stagnation at best. Nowhere to be seen is an elected representative possessing the testicular fortitude, or the sheer courage to tackle the entitlement challenges of Social Security, Medicare, Medicaid or tax code reform. These entitlement programs can no longer be afforded in their current state and are in desperate need of reform. Further delay in the implementation of reforms will only prove to be more costly and unnecessarily time consuming. The definitive question remains, does America possess the political will to tackle entitlement programs which have become no longer affordable?



The next fiscal challenge is looming on the horizon. This is the issue of raising the statutory debt limit, currently at \$16.4 trillion (U.S.), to at least \$18 trillion (U.S.) by the end of February, or risk having America default on its U.S. Treasury debt obligations. The Republicans would attempt to lever the debt ceiling negotiations in favour of sizeable spending cuts, whereas the Democrats would still prefer the combination of higher tax revenues and the closure of taxation loopholes. President Obama has oft stated he will not use the statutory debt ceiling negotiations as a bargaining tool for further spending cuts. So, once again, political gridlock will surely rear its ugly head in America. Whatever the end result, both Fitch Ratings and Moody's Investors Service are likely to join Standard and Poor's by downgrading the U.S. sovereign debt credit rating to 'AA' (High) from 'AAA', which means it will become more expensive for the U.S. Treasury to service America's outstanding debt.

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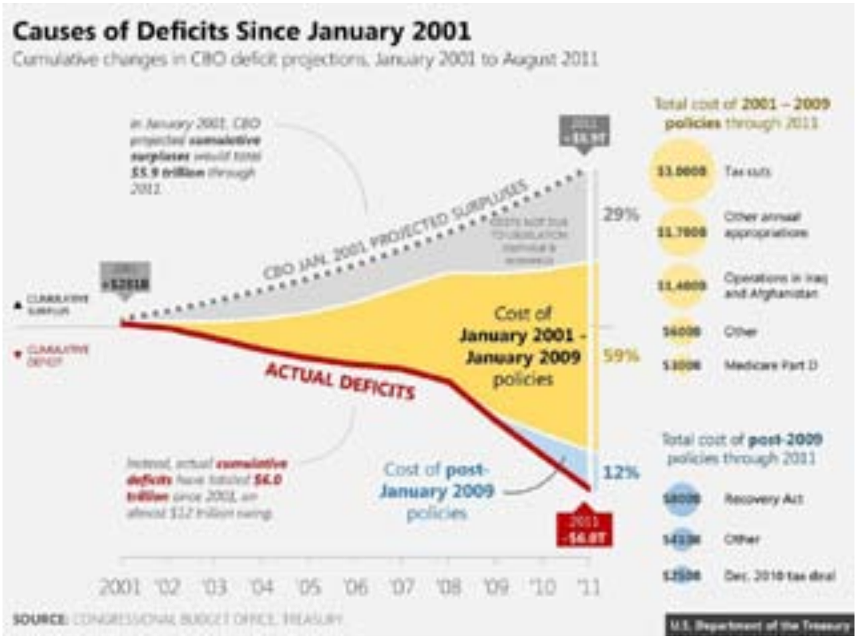
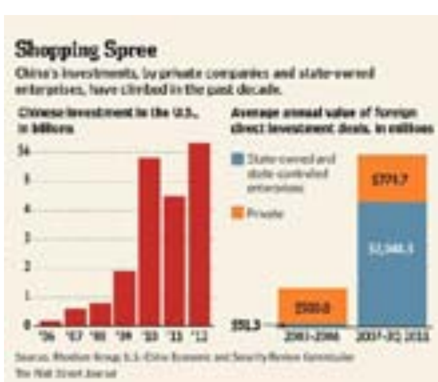


China

China's bank loans as a share of funding in the economy may have fallen to a record low, highlighting the growth of alternative financing channels that have prompted warnings of rising credit risks. New yuan loans probably declined by 14% in December from a year earlier, according to the median projection in a Bloomberg News survey of 37 analysts ahead of data due by January 15th. That would give bank lending a 55% share of aggregate financing for 2012, based upon UBS AG estimates, the least in figures dating back to 2002. The decline underscores the waning ability of official loan data to capture the scale of debt in the world's second largest economy, as borrowers and investors turn to less-regulated, higher return, shadow banking products. The People's Bank of China (PBOC) is putting greater emphasis on aggregate financing and the International Monetary Fund (IMF) states the growth of non-bank credit poses "new challenges to financial stability."

Shi Lei, a Beijing-based analyst at Founder Securities, who has provided research advice to China's securities regulator, commented: "China's economic performance in 2013 will be significantly affected by how seriously Chinese regulators are going to treat non-bank financing. While a hands-off approach will help the economy, a crackdown would be really detrimental for (economic) growth." The PBOC lending figures are among the December data in the coming days that will reveal whether an economic rebound which began in September, accelerated or slowed in December following a seven quarter growth slowdown.



Conclusion

At the onset of the New Year everything appears rosy.

According to most economists the U.S. economy is recovering, despite the fact that official unemployment numbers remain stubbornly high. The fiscal cliff has been averted and the budget limit debate is at least been pushed forward into February, so let's not worry about that until we get there.

"Junk-Bond Prices Point to Return of the Bulls-Investors signal a strong start to 2013"

"The junk-bond market is sending a bullish signal for the global economy in 2013, with investors in U.S. high-yield securities earning higher returns so far this year than those who have bought investment-grade debt."

"High-yield bonds are an acute barometer of risk appetite and increases in their prices have often signalled a turn in sentiment." Financial Times,Tuesday January 15, 2013.

The value of the euro has been rising against the dollar and European leaders are convinced that the worst is behind them.

"After more than three years of global market turmoil, political upheaval and nail-biting summits, European leaders are declaring that the worst of the continent's debt crisis is behind them."

"In New Year's speeches and congrulationary comments, leaders across the region are crediting fresh rounds of painful austerity, a hard-fought new role for the European Central Bank and steps towards a deeper integration with acheiving a breakthrough."

"Borrowing costs for troubled nations, they note, have come down steadily from last year's dangerously high levels, pulling a string of countries back from the brink of imminent fiancial collapse and defying naysayers who predicted a quick breakup of the euro zone last year." The Washington Post, January 5, 2013.

As has been the case for some years now the industrialized world is hoping that China can take up the slack and acording to Chinese statistics the economy is indeed regaining its vigour after seven quarters of slowing growth.

We are very suspicious of official Chinese data, much as we are of U.S. data. From our perspective it seems unlikely that there can be any meaningful economic recovery in China given the hoplessness of the European economy, where even Germany is experiencing an industrial slowdown. One person commenting on a recent CNBC article regarding the Global Economy wrote,"Only naive persons believe communist people and the communist party. They are lying from the top of the communist party to the bottom people."

"As the Chinese economy continues to sputter, prominent corporate executives in China and Western economies say there is evidence that local and provincial officials are falsifying economic statistics to disguise the true depths of the troubles."

"Indeed, China officilas in all cities and provinces are also overstating economic output, corporate revenue, corporate profits and tax receipts, the corporate executives and economists said. The officials do so by urging businesses to keep separate sets of books, showing improving business results and tax payments that do not exist. China's broad measures of economic growth are man-made and therefore unreliable." Sounds a lot like the good old Soviet days. But never mind China, when the world's economies explode, China's economic numbers will become irrelevant.

In Japan Mr. Abe, the Prime Minister recently introduced a supplementary budget, which includes a major stimulus programme. Mr. Abe believes that the stimulus will raise GDP by 2.5% and create some 600,000 jobs.

Most stock market pundits are of the opinion that stock prices will continue higher. A headline in the Financial Times-"Billions pumped into global equities" The story then noted, "Investors this week poured the most money into equity funds in more than five years, as global shares surged and a comprimise deal on the U.S. fiscal cliff boosted confidence."

"Net inflows into equity funds monitored by EPFR, the funds research company, hit $22.2 billion (U.S.) in the week to January 9 - the highest since September 2007 (You may remember that the following month October 2007 was the stock market peak when the DJIA reached 14,200 points) and the second highest since comparable data began in 1996." Financial Times, Saturday January 12, 2013.

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For the most part, it would appear that world leaders and indeed people in general are optimistic about our future as we begin 2013. However, we believe that such confidence in the future is misplaced. Indeed, being contrarian by nature we are of the opinion that once the general level of confidence reaches a relatively high level it is a good indicator that the economy and the financial markets are about to turn down.

Our very pessimistic outlook for stock markets during 2013, which is corroborated by both Dr. McHugh and Robert Prechter, is signalling some kind of financial or monetary catastrophe, perhaps more acute than that which occured in 2008. Governments and central banks have been fighting to hold back the ravages of the Long Wave winter for thirteen years we believe that they have now run out of time.

We end this 2013 outlook with a quote from Money Week, which is Britain's largest financial publication. While the quotation is directed at the situation in the United Kingdom, it is our belief that it is a relevant summation attributable to all industrialized nations-"We believe the outcome of this problem is inevitable.....and the recession, joblessness and instability you see right now is only the first stage of it. Many people think the slump we're in now is as bad as it will get."

"But the truth is, it's only the start. In fact you will certainly see the consequences of this deep-rooted problem unfold across the cities, towns and villages of Britain.No one will escape the fallout."

"In all recorded history no country has ever recovered from the financial postion we find ourselves in today. No government has ever been able to reverse this trend. No emergency action has ever come close to a solution.The inescapable problem has only ever had one outcome: financial collapse."

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"Those who cannot remember the past are condemned to repeat it." Santayana