Monday July 13th, 2015

LONGWAVE group

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

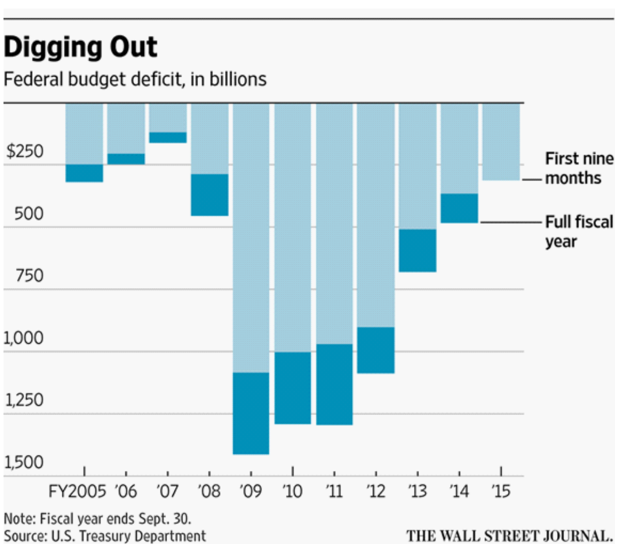
THAT WAS THE WEEK THAT WAS

Monday, July 13th

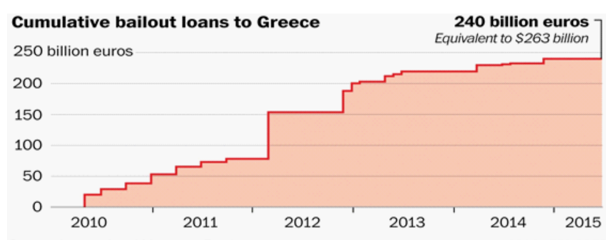
The U.S. Department of the Treasury reports the federal government posted a surplus of $52 billion (U.S.) in June, which is $19 billion (U.S.) lower than the surplus recorded in the same period of 2014. For the fiscal year to date – i.e. October 1, 2014 to June 30,

MONDAY, JULY 13TH

2015 – the federal government's deficit is $313 billion (U.S.), which is $52 billion (U.S.) lower than the same period a year ago.



- Front Page Headline, Washington Post – European Leaders Agree to Greek Rescue Plan. In order to keep his country in the euro zone, Greek Prime Minister Alexis Tsipras has acquiesced to a challenging ultimatum from European leaders. In exchange for a $96 billion (U.S.) rescue – Greece's third in five years – Mr. Tsipras has agreed to press the Greek parliament for swift passage of a package of reforms by Wednesday, thereby remaining within the European Monetary Union (EMU). Mr. Tsipras agreed to far more than simple austerity, pledging to even stage what may amount to a fire sale of Greek utilities, even plots of lands on its islands, to help repay its huge debt load … Now Mr. Tsipras faces a tough and humbling battle to enable the 300-seat parliament's ratification of the rescue agreement. Every point is a potential political battle, including creditor-demanded overhauls to the Greek tax and pensions systems. Without an official blessing from parliament, the promised lifelines could be withdrawn and Greece would be hurled into a full-scale financial crisis.



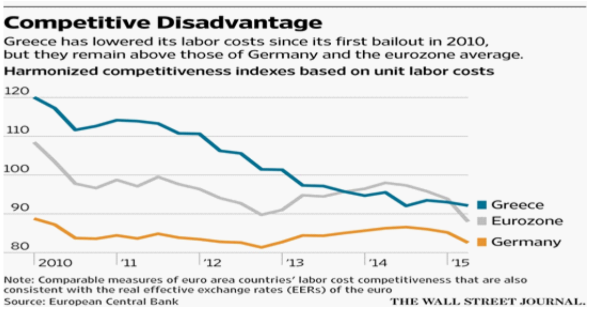
In a comment to the media as he left Brussels, Mr. Tsipras stated: 'Today's agreement maintains liquidity and offers hope of economic recovery. We know the agreement will be difficult to implement and may be recessionary.' European Council President Donald Tusk proffered: 'While there are strict conditions to be met, the agreement gives Greece a chance to get back on track with the support of European partners."

- Front Page Headline, Daily Telegraph U.K. – "EMU Treating Greece Like A Hostile Occupied State. International Business Editor Ambrose Evans-Pritchard warns: The cruel capitulation forced upon Greece after 31 hours on the diplomatic rack offers no conceivable way out of the country's perpetual crisis. The terms are harsher than a full order of magnitude of those already rejected by Greek voters in a landslide referendum a week ago, therefore they can never command democratic assent … European Monetary Union inspectors can veto legislation and the emasculation of the Greek parliament has slipped into the text. All that is missing is a unit of EMU gendarmes. Such terms are unenforceable. The European creditors have sought to nail down the new memorandum by transferring 50 billion euros of Greek assets to 'an independent fund which will monetize the assets via privatizations and other means.' In part, it will be used to pay off debts. This fund will be under EU supervision. The cosmetic niceties of sovereignty will be preserved by letting the Greek authorities manage its day-to-day affairs. Nobody is fooled.

  In other words, they are seizing Greece's few remaining jewels at source. This is not really different from the International Committee for Greek Debt Management in 1898 imposed on Greece after the country went bankrupt following a disastrous Balkan war. A six-power league of bondholders, led by British bankers, impounded customs duties in the Port of Piraeus and seized revenues from stamp duty, tobacco, salt, kerosene and all the way down to playing cards. However, at least there was no humbug about solidarity and helping Greece on that occasion. In a telephone conversation this morning, former Greek Finance Minister Varoufakis said of the new agreement: 'It's the Versailles Treaty for the present age.' Under the new terms, Greece must tighten fiscal policy by about 2% of GDP by next year. This could push the country into a debt deflation spiral and into the next downward leg of its six-year depression. Moreover, this will likely cause the government to miss the budget targets yet again – probably by a large margin – in an exact repeat of a self-defeating policy which caused Greek debt dynamics to spin out of control in the last two Troika loan packages. As the International Monetary Fund (IMF) acknowledged in its famous mea culpa, if one misjudges the fiscal multiplier and force austerity beyond the therapeutic dose, one makes matters worse. The debt to GDP ratio increases despite the spending cuts … The text states that in addition to pension cuts and tax increases, there should be 'quasi-automatic spending cuts in case of deviations from ambitious primary surplus targets.' In other words, they will be forced to implement pro-cyclical contractionary policies. The fiscal slippage which acted as a slight cushion over the last five years will not be tolerated this time around. Also, let us not forget that these primary surpluses never made any sense in the first place. They were not drawn up on the basis of macroeconomic analysis. They were written into prior agreements because that is what would be needed – ceteris paribus – to pretend that debt is sustainable, therefore the IMF could then sign off on the accords. What a charade.

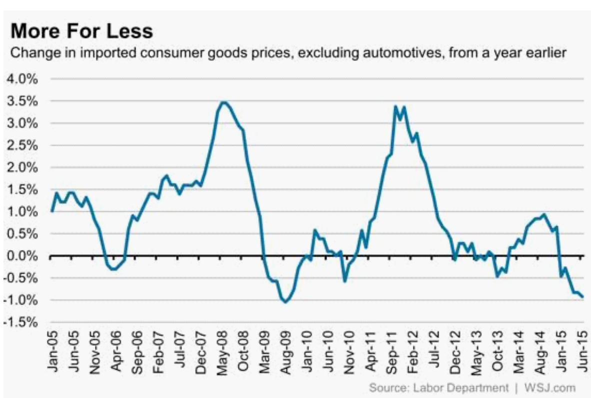
  Nobel economist Paul Krugman notes: 'The EMU demands are madness on every level. What we've learned these past couple of weeks is that being a member of the euro zone means that the creditors can destroy your economy if you step out of line. This has no bearing at all on the underlying economics of austerity. This goes beyond harshness into pure vindictiveness, complete destruction of national sovereignty with no hope of relief. Presumably, it is meant to be an offer which Greece cannot accept, but even so, it's a grotesque betrayal of everything the European Union was supposed to stand for.' Yes, while Syriza has blinked, there are many chapters in this sorry saga yet to come. The Greek banks are on the verge of collapse. There is neither enough cash left to cover ATM withdrawals of 60 billion euros each day through this week, nor to cover weekly payments of 120 euros to pensioners and the unemployed, that is to say, the tiny fraction of the jobless who receive anything at all.

  Capital controls have led to an economic standstill. Almost nothing is coming into the country. Companies are running down their last inventories of raw materials and vital imports. Hundreds of factories, mills and processing plants have already reduced shifts and are preparing to close down operations as soon as this week. Late tourist bookings have crashed by 30%. Syriza faced a serious risk that the country would be depleted of imported food stocks by the end of the month, with calamitous consequences at the peak of the tourist season. So yes, faced with the full horror of what is occurring, they recoiled. There is no doubt that Syriza sold the Greek people a false prospectus with its incompatible promises both to tear up the Troika Memorandum and to keep Greece in the euro zone. They have learned a horrible lesson. Yet, that is only half the story. We have also watched the EMU creditor powers bring a country to its knees by cutting off the emergency liquidity assistance (ELA) to its banking system. Let there be no doubt, it was the decision by the European Central Bank (ECB) to freeze ELA at 89 billion euros two weeks ago which precipitated the final crisis and broke Syriza's will to resist. The lines of authority on this episode are blurred. Personally, I do not blame ECB President Mario Draghi for this abuse of power. Rather, it was in essence a political decision by the Euro group. However one dresses it up, the fact remains that the ECB is by its acts dictating a political statement and serving as the enforcement arm of the European creditors, rather than upholding European Union treaty law.



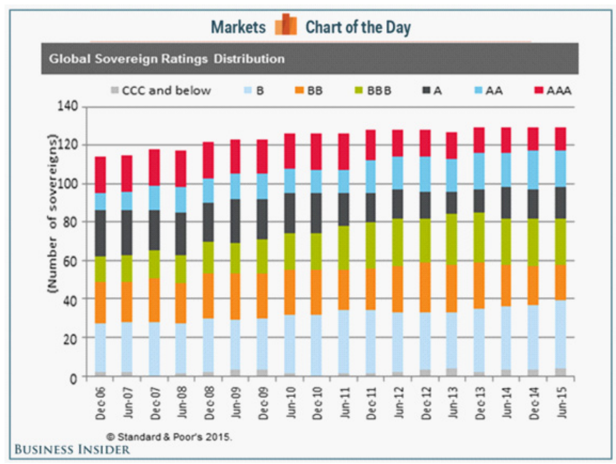
TUESDAY, JULY 14TH

- The Commerce Department reports U.S. retail sales declined by 0.3% in June, following a downwardly revised increase of 1% in May. Stephen Stanley, chief economist at Amherst Pierpont Securities in Stamford, Connecticut, commented: "The weakness in the retail sales report is rather broadly based, with particular emphasis in categories that are considered seasonal in nature. It definitely throws cold water on the idea that consumer spending was gathering momentum."



- Front Page Headline, Business Insider – "Global Sovereign Credit Ratings. According to a new report by Standard and Poor's, approximately 55% of all rated sovereign credits are investment grade, i.e. 'BBB' (Low) or above, as at June 30, 2015. Basically, this ratio is largely unchanged from five years ago, although it is lower than the 59% peak as at June 30, 2008. The report stated: 'Overall, global sovereign creditworthiness has declined slightly since the onset of the global financial crisis in 2008. The average long-term sovereign credit rating has fallen by just over one level to between BBB (Low) and BBB; compared with just below BBB (High) in 2008.

- Additionally, negative outlooks still outnumber positive outlooks, which suggest that over the next 12 months downgrades will outnumber upgrades.' Notably, most of the negative outlooks reside in the Middle East, Africa and the Commonwealth of Independent States (CIS) which includes Russia, Belarus, Ukraine and Turkmenistan. Countries sporting S&P's pristine AAA credit rating include Australia, Canada, Denmark, Germany, Lichtenstein, Luxembourg, Norway, Singapore, Switzerland and the U.K. Notably, the U.S. lost its AAA credit rating in August 2011amid persistent political brinkmanship regarding America's statutory debt limit."



- Front Page Headline, New York Times – "Iranian Nuclear Agreement Built on Verification' – U.S. President Obama. Iran and a group of six nations have announced they reached an historic accord to significantly limit Tehran's nuclear ability for more than a decade, in return for removing international oil and financial sanctions. The accord culminates 20 months of negotiations on an agreement President Obama had long been seeking. Following decades of coups, hostage-taking, terrorism and sanctions, whether the agreement portends a new relationship between Iran and the United States remains a bigger question. In an early morning appearance at the White House, President Obama began what promises to be an arduous effort to sell the agreement to Congress and the American public. President Obama made it abundantly clear that he would fight to preserve the agreement from critics in Congress who are beginning a 60-day review. President Obama stated: 'This agreement is not built on trust, it is built on verification. I will veto any legislation which prevents the successful implementation of this agreement."

- Front Page Headline, Daily Telegraph U.K. – "IMF Stuns Europe with a Call for Massive Greek Debt Relief. International Business Editor Ambrose Evans Pritchard writes: The International Monetary Fund has launched a political earthquake in Europe, warning that Greece may need a full moratorium on debt payments for 30 years and perhaps even long-term subsidies in order to claw its way out of depression. In a confidential report, the IMF stated: 'The dramatic deterioration in debt sustainability points to the need for Greek debt relief on a scale that would need to go well beyond what has been under consideration to date.' Greek public debt will spiral to 200% of gross domestic product (GDP) over the next two years, compared to 177% in an earlier report on debt sustainability issued just two weeks ago. The findings are explosive. The document amounts to a warning that the IMF will not participate in any European Monetary Union (EMU) led rescue package for Greece unless Germany and the EMU creditor powers finally agree to sweeping debt relief. This vastly complicates the rescue accord which was agreed by euro zone leaders in marathon talks over last weekend, since Germany insists that the bailout cannot move ahead unless the IMF is involved. The creditors were aware of the IMF's report as early as Sunday, yet chose to sweep it under the rug. Extracts were leaked to Reuters today, forcing the matter into the open. The IMF noted there is no conceivable chance that Greece will be able to tap private capital markets in the foreseeable future, leaving the country entirely dependent upon rescue funding. The IMF claimed that capital controls and the shutdown of the Greek banking system had entirely changed the picture for debt dynamics, an implicit criticism of both the Greek government and EU authorities.

IMF Managing Director Christine Lagarde.
Photo source: Daily Telegraph files.

The decision by the European Central Bank (ECB) to force the closure of the Greek banks two weeks ago by freezing emergency liquidity assistance (ELA), appears to have cost European taxpayers very large sums of money. In its report, the IMF stated: 'Europeans will have to offer either a deep up-front debt haircut, or slash the debt burden by lengthening maturities and possibly lowering interest payments. There would have to be a very dramatic extension of maturities, with grace periods of 30 years on the entire stock of European debt. Debt forgiveness alone would not be sufficient. There would also have to be new assistance and perhaps explicit annual transfers to the Greek budget.' This is the worst nightmare of the northern creditor states … The underlying message of the IMF's report is that Greece is in such deep trouble that it cannot withstand further austerity cuts, but this is difficult to square with the latest demands by EMU creditors … The IMF's report raises as many questions as it answers. Almost no economist would accept the fact that two weeks of capital controls could alone raise Greece's debt ratio by 28 percentage points of GDP a full seven years later.

The backdrop to this sudden shift in position is almost certainly political. It follows an intense push for debt relief by the U.S. Treasury, which is the dominant voice on the IMF Board in Washington … It would appear that powerful voices in global capitals and on the IMF Board have since demanded that the IMF return to the drawing board. Its conclusions validate what Greece's Syriza government has been saying all along. The debt cannot be repaid. Any formula which fails to recognize this merely stores up an even bigger crisis for down the road."

WEDNESDAY, JULY 15TH

- Front Page Headline, Globe and Mail – "Bank of Canada Lowers Bank Rate to 0.50%. Bank of Canada Governor Stephen Poloz announces the central bank is reducing its administered overnight lending interest rate to 0.50% from 0.75%; while lowering the bank's outlook for the country's gross domestic product (GDP) to 1.1% for 2015 from a 1.9% forecast of three months ago. In a statement accompanying the Bank Rate decision, the central bank cited: 'Canada's economy is undergoing a significant and complex adjustment. Additional monetary stimulus is required at this time to help return the economy to full capacity and inflation to sustainably to our target level of 2%.

Bank of Canada Governor Stephen Poloz. Source: Globe and Mail files.

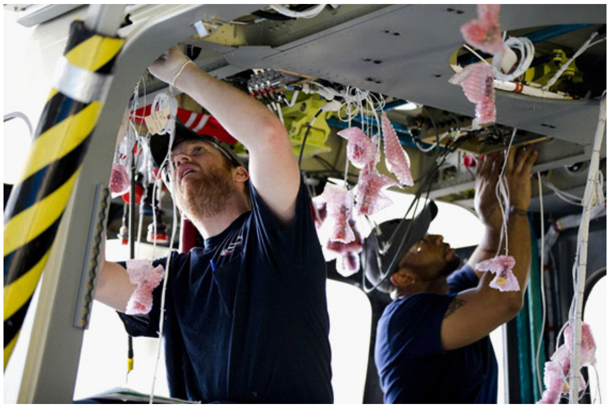
- The Canadian Real Estate Association (CREA) reports the nation's existing home sales declined by 0.8% in June from May, but were 11% higher on a year-over-year basis. In a research note, Robert Kavcic, senior economist at BMO Capital Markets, commented: “Following tough winter weather conditions across many areas of the country, home buyers were very active through the spring and early summer, with record low mortgage rates providing a boost. Overall, while the market didn’t tighten up again in June, it remains considerably tighter than it was a year ago.”

- Statistics Canada reports the nation’s factory sales edged 0.1% higher in May from April, citing higher demand for aerospace, petroleum and coal products, as sales increased in six of twenty-one industries surveyed. In a research note to clients, analysts at CIBC World Markets stated: “The trend in real manufacturing continues to be down compared with levels reached in mid-2014, meaning additional time will be needed for a more competitive exchange rate and a stronger trading partner to the south to influence the desired rotation away from the consumer and the housing market.”

- In her semi-annual testimony to the House Financial Services Committee, U.S. Federal Reserve Board Chairwoman Janet Yellen indicated she was more inclined to raise the administered Federal Funds rate soon and proceed slowly, rather than wait a longer time and move aggressively. In response to a lawmaker’s question, Ms. Yellen stated: “If we wait longer, it certainly could mean that when we commence raising the Federal Funds rate, we might have to do so more rapidly. An advantage to beginning somewhat earlier is that we might have a more gradual rising rate trend. So, I believe a gradual path is a prudent approach.”

U.S. Federal Reserve Chairwoman JanetYellen.
Source: Wall Street Journal

- The Federal Reserve reports U.S. industrial production – a measure of output in the manufacturing, mining and utilities sectors – while rising by a seasonally adjusted 0.3% in June from May, declined at an annual rate of 1.4% in the 2nd. quarter. Manufacturing, the largest component of the index, was flat on the month largely because of a decline in the production of autos and auto parts. Machinery, fabricated metal products and primary metals production both declined by 0.1% as well. Capacity utilization, which measures industrial slack, rose by 0.2% to 78.4%. While capacity utilization has risen by 2.6% over the past 12 months, it still remains 1.7% below its long-term annual average since 1972.



Workers help assemble a helicopter at the Agusta Westland aircraft plant in Philadelphia. Photo source: Associated Press

- The Bureau of Labor Statistics (BLS) reports the U.S. producer price index (PPI) rose by a seasonally adjusted 0.4% in June, citing nearly two-thirds of the increase in the index can be attributed to prices for final demand goods, which rose by 0.7% following an increase of 0.5% in May.

- Front Page Headline, Daily Telegraph U.K. – “Greek MPs Ratify Controversial Austerity Bill to Secure Euro Zone Bailout. Following a tense debate which lasted into the small hours of this morning, the 300 member Greek parliament voted by a majority 0f 229 to 64 against on a raft of tax hikes and pension reforms. There were six abstentions and one MP was absent from the debate.

Greek MPs during the tense debate.
Photo source: Daily Telegraph U.K.

The vote was part of the conditions laid down by Brussels for a third bailout of about 85 billion euros and will prevent Greece from being cast out of the euro zone. Greek Prime Minister Alexis Tsipras said he would probably step down from office if he did not receive the support of more than 121 of his Syriza Party MPs. This morning's vote has left him with the support of 124, a margin that may still leave his fate hanging in the balance and could provoke a vote of confidence in his leadership … Prior to the votes being cast, Mr. Tsipras made a final appeal to parliament for support for the measures, telling fellow MPs that there was no alternative: 'While we don't believe in it, we are forced to adopt it. I didn't want Greek society to be in a worse position than it was five years ago."

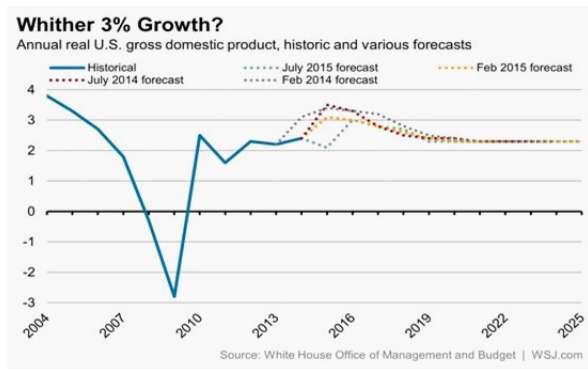
THURSDAY, JULY 16TH

- The Labor Department reports U.S. initial claims for state unemployment benefits declined by 15,000 to 281,000 in the week ended July 11th. from a revised level of 296,000 in the prior week; while continuing claims fell by 112,000 to 2.22 million in the week ended July 4th.

- The National Association of Home Builders (NAHB) reports its index of builder confidence in the market for new single family homes remained at a seasonally adjusted reading of 60 in July, matching a revised June reading of 60 previously reported as a level of 59; its highest point since November 2005. David Crowe, NAHB's chief economist, observed: "July's reading is consistent with recent data showing stronger sales in both the new and existing home markets, as well as continuing job growth. However, home builders still face a number of challenges, including low inventories of lots and shortages of skilled labor."

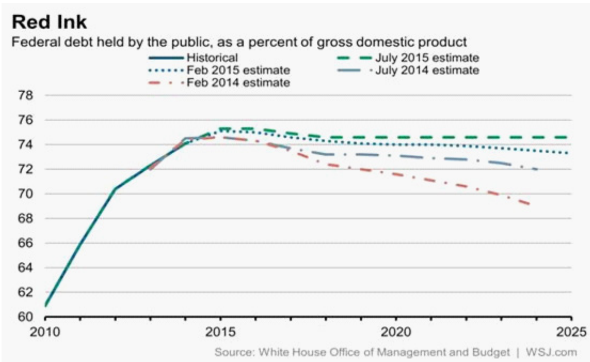
- Front Page Headline, Wall Street Journal – "White House No Longer Projecting a Decline in the U.S. National Debt. When the White House produced its annual budget last year, it projected a steady decline in the nation's debt as a share of economic output over the coming decade. A set of revisions issued this week in a report known as the 'Mid-Session Review' is a brief update to the forecasts unveiled at the beginning of the year by the White House Office of Management and Budget. Firstly, the good news: Over the short-term budget deficits are falling. The Obama administration now forecasts the annual budget deficit will reach $455 billion (U.S.) this year, down 22% from its forecast at the beginning of the year and about 6% below last year's level. That level represents about 2.6% of America's total economic output, down from a forecast of 3.2% earlier this year. Moreover, the administration sees the budget deficit declining by another 6% next year to $429 billion (U.S.), or about 2.3% of gross domestic product (GDP). Secondly, the bad news: Domestic economic growth has continued to underperform expectations. So, because the administration's economists don't foresee economic growth rebounding later to play catch up, revenue which is lost to lower economic growth won't be recouped in the future.

The latest forecast provides somewhat more fodder for the secular stagnation argument advanced by former Treasury Secretary Larry Summers, which notes that developed countries face a stretch of sub-par economic growth due to a mixture of weak demand, an aging population and slower productivity growth. Last Year, the White House budget forecast called for 3.1% GDP growth in 2014 and 3.4% in 2015. Last July, it downwardly revised the 2014 GDP growth forecast following a disappointing first quarter, but it boosted its 2015 GDP forecast to 3.5%. This year, a similar dynamic has unfolded. At the beginning of the year, the White House estimated 3.1% GDP growth for this year, which has now been reduced to 2.1%, after the weak first quarter.



While slower economic growth does produce some savings for the government, such as lower debt servicing costs on new issues of U.S. Treasurys and slightly less costs for some entitlement programs, they don't amount to as much as the lost revenues. The upshot is that even small downward shifts in economic growth make the government's debt burden somewhat steeper. When the White House produced its budget at the beginning of 2014, it estimated that the debt held by the public would fall as a share of economic output from 74% last year to 69% in 2024.

Last July, when the government first downwardly revised its GDP growth forecast, that boosted the debt-to-GDP ratio to 72% for 2024. This February, that figure rose to 73.5% and this week the latest estimate put the debt-to-GDP ratio at 74.6%. In other words, the steady declines envisioned in last year's forecasts have been washed out, primarily on account of the slightly weaker economic growth forecasts.



Wakeup call for U.S. President Obama: According to the U.S. National Debt Clock, America's national debt has recently surpassed $18.3 trillion (U.S.), that's $18,300,000,000,000. See also, Economic Winter, Implications of the Impending Collapse of the Fiat Paper Money System – February 20, 2015."

FRIDAY, JULY 17TH

- The Reuters / University of Michigan group reports its preliminary July reading for its consumer sentiment index declined to a reading of 93.3 from a final level of 96.1 in June. Richard Curtin, director of the Michigan Survey of Consumers noted: "When asked to explain how their finances had changed, 6% more of households surveyed mentioned income gains, while others stated slowly improving finances are anticipated for the year ahead."

- The Commerce Department reports U.S. housing starts rose by 9.8% to an annualized pace of 1.17 million units in June from an upwardly revised rate of 1.07 million units in May. Meanwhile, building permits rose by 7.4% in June to a 1.34 million annualized rate, the highest level since July 2007. Brett Ryan, an economist at Deutsche Bank Securities in New York, noted: "The fundamentals all point to more pronounced activity in the housing market. Given the gains in the labor market, stronger household balance sheets and stable energy prices, this is the perfect environment for housing."

- The Labor Department reports the U.S. consumer price index (CPI) rose by 0.3% in June, following a gain of 0.4% in May. The so-termed core rate, excluding food and energy costs, increased by 0.2% in June and by 1.1% on a year-over-year basis.

- Front Page Headline, GoldMoney – "Credit Deflation and the Price of Gold. Researcher Alasdair Macleod writes: There is a common view in financial markets that credit deflation is bad for gold prices because nowadays gold is regarded as an asset to be sold in the scramble for cash when investors are forced to reduce their debts. Four years ago, when asked by Ron Paul for his opinion on gold, then Federal Reserve Chairman Ben Bernanke replied that gold was not money, rather just another asset, appearing to confirm this view.

Undoubtedly, Mr. Bernanke's view is shared by nearly all other central bankers in the advanced economies and by executives in the banks which have profited handsomely from monetary and credit inflation. However, it is not shared by the majority of ordinary savers around the world who still see it as the ultimate store of value at a time of fiat currency inflation. For them, gold is the money to save, driven out of circulation by inferior currencies. We know this to be true throughout Asia where the bulk of the world's population lives. In addition, even millions of ordinary Americans continue to accumulate silver eagles because they still recognize the monetary attributes of precious metals. Crucially, the assumption in capital markets that gold is no longer money, but just an asset or commodity, has all but destroyed our understanding of its monetary relationships.

Financial analysts fail to appreciate the difference in behavior of sound money compared with that of unsound money during a contraction of bank credit. This can be empirically established by looking at the relationship between gold and the U.S. dollar during the Great Depression, when bank credit contracted substantially following the Wall Street stock market crash and gold was then upwardly revalued by 69% to $35 (U.S.) per troy ounce in 1935. The whole point of unsound money is that it can be devalued relative to sound money as it was at that time, in order to stabilize prices that would otherwise decline; a policy option that is not available to central banks adhering to a gold standard. In the days of a gold exchange standard, the collapse of excessive bank credit was always sudden and vicious in proportion to the previous expansion. Since credit was expanded out of thin air by banks without underlying stocks of gold to cover it, inevitably slumping prices became associated with bank failures and central banks were positioned to insulate commercial banks from this brutal reality. Saving overextended banks always requires the artificial lowering of administered interest rates and the expansion of the money supply, in order to restrain the currency's purchasing power from rising against declining commodities. Therefore, gold remains a store of value for savers because it cannot be devalued in this way by a central bank.

This is becoming relevant again given that the escalating credit problems in China appear to be leading towards a 1929 style stock market crash, which if it follows the well-established playbook, will be followed by an economic slump. Today, China is the world's largest commercial consumer of commodities, just as

America was in the late 1920s and her slowing economy is putting downward pressure on commodity prices, pushing up the purchasing power of money of the other major currencies. Put another way, falling energy and commodity prices in yuan are forcing deflation upon the rest of us. So, even though gold investors have seen its dollar price trade broadly sideways for the last three years, its purchasing power measured against most commodities has actually been rising. More recently, gold has also been an effective store of value against weaker currencies, notably the euro and the yen.

Now that China's credit deflation is beginning to be exported to America through lower commodity prices, there is a growing assumption that the U.S. dollar will strengthen further. This has encouraged hedge funds to sell gold futures in order to capture the dollar's rise. In terms of purchasing power, it is certainly true that the currency has a deflationary element within it. However, if the Federal Reserve refused to expand the supply of dollars in circulation, abandoning commercial banks to face the full force of a credit contraction, the purchasing power of the dollar would rise as if it were sound money. However, the Fed was positioned to do the exact opposite, so it has a clear duty to weaken its currency in this event. Therefore, when the balance of risks swings towards a credit contraction in the U.S., the gold price will rise against the dollar because the Fed through its monetary policy is certain to ensure it does so.

This will also surprise market traders who think that a continuing collapse in Chinese stock markets will force liquidation of gold holdings by the Chinese public. There is little doubt that distressed speculators will come under pressure to sell their gold holdings if any, but this argument ignores the certainty that during a credit contraction government-issued currencies always weaken against gold. So, having acquired substantial quantities of gold for itself and having also ensured it is widely held by its public, the Chinese government is arguably in a more compelling position to encourage a gold revaluation as a means of stabilizing her economy in a credit crisis than America was eighty years ago. It will be China's only option and if the government doesn't implement it, China's middle classes certainly will.

We are already witnessing the People's Bank of China (PBOC) engaging in reflationary policies in order to contain the stock market crash. This is a normal central bank response. Doubtless it will maintain the managed peg against the U.S. dollar, partly because China is committed to building confidence in her own currency as a replacement for the dollar in international settlements; also because currency devaluation would be deemed in the markets as a failure in economic policy. Furthermore, China can expect U.S. monetary policy to do some of its reflationary work for it.

Therefore, instead of devaluing against the dollar, a rise in the yuan gold price is almost certain to occur. Of course, whether or not China revalues her gold reserves remains to be seen, but allowing the gold price to rise fits in with the logic of the relationship between sound and unsound money when a credit contraction threatens to become a serious issue. This simple fact could override all the geostrategic considerations upon which China watchers have tended to focus. A gold revaluation would be presented to the world as bound up with China's domestic economic problems, instead of an act aimed at undermining the dollar's reserve status; a solution which is less confrontational than outright disagreement with Western central banks over gold's role in the international monetary order."

CLOSING LEVELS FOR FRIDAY, JULY17TH.

		WEEKLY CHANGE
Dow Jones Industrial Average	18,086.45	+ 326.04 points
Spot Gold Bullion	$1,131.90 (U.S.)	– $26.00 per troy oz.
Spot Silver	$14.81 (U.S.)	– $0.73 per troy oz.
S&P / TSX Composite	14,642.84	+ 231.77 points
10 – Year U.S. Treasury Yield	2.35%	– 5 basis points
10 – Year Gov't. Canada Yield	1.56%	– 12 basis points
10 –Year Sovereign Yield Spread	79 basis points	+ 7 basis points
Canadian Dollar	77.00 cents (U.S.)	– 1.87 cents
U.S. Dollar Index Future	97.956	+ 2.179 cents
WTI Crude Oil Futures	$50.89 (U.S.)	– $1.85 per barrel
DJIA / Gold Ratio	15.979	+ 0.641 point
Gold / Silver Ratio	76.428	+ 1.917 points

Ian A. Gordon, The Long Wave Analyst www.longwavegroup.com

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