

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE  
**THAT WAS THE WEEK THAT WAS**



Monday, June 8th

Front Page Headline, Bloomberg News – “The Federal Reserve Bank of New York reports its monthly survey of consumer expectations for inflation revealed a median response for a likely 3% increase in personal consumption expenditures over the next

MONDAY, JUNE 8TH

twelve months. Since May 2014, this preferred Fed measure of inflation has only increased by 0.1% and has been below the Fed target of 2% since May 2012. New York Fed President William Dudley recently commented: “The firming of inflation that I anticipate reflects my expectation that resource utilization will increase and the likelihood that some of the factors which have pulled down the inflation rate, such as lower oil and gas prices and a firmer U.S. dollar, have already stabilized or partially reversed.”

- Canada Mortgage and Housing Corp (CMHC) reports the nation’s housing starts rose to a seasonally adjusted annual pace of 201,705 units in May. Separately, Statistics Canada reported the value of the country’s building permits rose by 11.6% to \$7.8 billion (CAD) in April. In a research note, Randall Bartlett, an economist at the Toronto Dominion Bank, commented: “Looking more broadly at the current quarter, the housing sector continues to demonstrate surprising strength, so we expect it will contribute positively to real gross domestic product (GDP) growth as a result.”
- Destatis, Germany’s federal statistics office, reports the country’s industrial production – adjusted for inflation and seasonal swings – rose by 0.9% in April, while the seasonally adjusted trade surplus widened to 22.3 billion euros (\$24.74 billion U.S.), propelled by strong level of exports. Separately, the German economy ministry reported German manufacturing orders were 1.4% higher in adjusted terms in April, following an upwardly re-

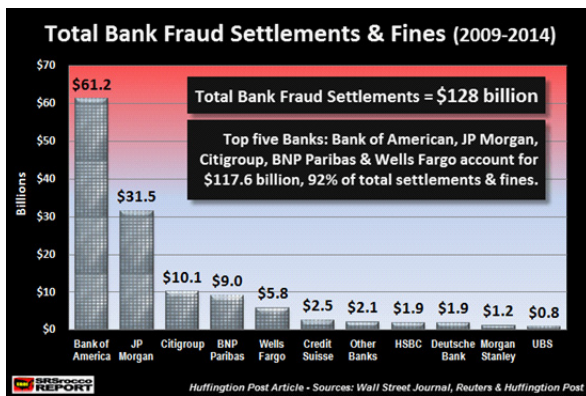
vised increase of 1.1% in March, previously reported as a gain of 0.9%. In a press release, Bundesbank President Jens Weidmann observed: “Domestic economic activity is benefitting from the favourable labour market situation and the substantial wage increases. Though foreign trade is currently being hampered by dampening global dynamics, it is simultaneously being buoyed by the euro’s depreciation and the strengthening recovery in the euro area.”



Assembly line production of a Porsche Macan in Germany. Photo source: Reuters

- Front Page Headline, SRSrocco Report – “Major Bank Fraud Adds Up to a Lot of Silver. The amount of fraud occurring in the major banks throughout the world is staggering to say the least. Ironically, the only market which isn’t manipulated is the silver market, so they say. To make it seem as though the regulators are on the ball, many of the major banks have been found

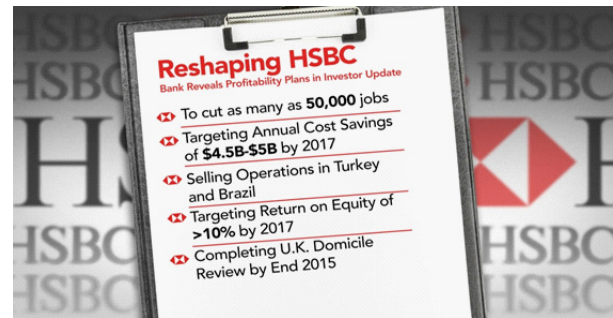
guilty of committing one fraud or another, paying large fines and agreeing to huge settlements. The most recent settlement by the criminal bankers was a cool \$5.6 billion (U.S.) for rigging the foreign currency markets for their own financial benefit. The banks responsible for this sort of illicit behavior come from a list of typically seedy characters: Citigroup, Barclays, JP Morgan, RBS and UBS. One can read all about it in the Wall Street Journal article. Even though \$5.6 billion (U.S.) is a hefty figure, when one adds up the total fines and settlements paid by the banking industry since 2009, it represents a serious amount of fiat currency. How much? Well, if one examines the chart below, it should afford a fairly clear picture.



According to a recent article in the Huffington Post, the major American and European banks have paid at least \$128 billion (U.S.) in fines and settlements to regulators since 2009. As one can ascertain, Bank of America gets the first place prize for paying a staggering \$61.2 billion (U.S.) in fines, while JP Morgan ranks second at \$31.5 billion (U.S.) and Citigroup taking the third spot at \$10.1 billion (U.S.). Scanning across the rest of the chart, one can see the additional fine, upstanding banks that participated in criminal activity and their subsequent fines. Of course, Americans like to boast that the United States is the best country in the world in which to reside, so it is reassuring to know that four of the five top corrupt banks – based on the amount of fines and settlements – are located in the USA. The top five banks accounted for 92% (\$117.6 billion U.S.) of the total \$128 billion (U.S.) in fines.

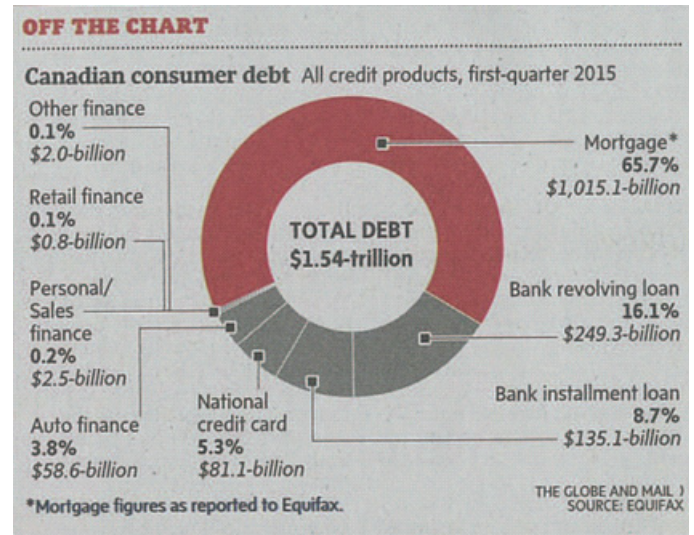
TUESDAY, JUNE 9TH

- Front Page Headline, Bloomberg News – “HSBC Announces Plans for 50,000 Job Layoffs. By means of the sale of businesses in Turkey and Brazil as well as direct layoffs, Europe’s largest bank plans to downsize under a 3-year reorganization plan in a bid to restore investor confidence.



Source: Bloomberg News

- Credit monitoring firm Equifax Inc. reports Canadian consumer debt rose by 6.9% in the 1st. quarter to \$1.54 trillion (CAD), citing higher levels of automobile and installment loans. While the average debt level held by Canadians, excluding mortgages, rose by 2.7% to \$20,910 (CAD), the national 90-days or longer delinquency rate remained low at 1.12%.



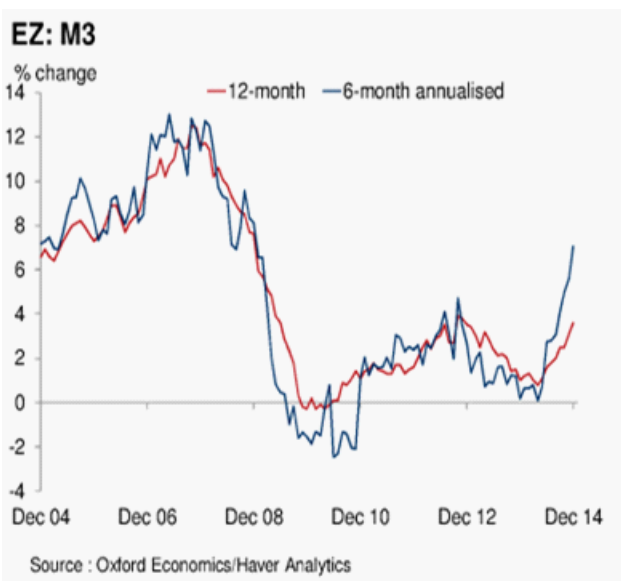
WEDNESDAY, JUNE 10TH

- Front Page Headline, Daily Telegraph U.K. – “The Global Deflation Strategy in Sovereign Debt Unwinds with a Vengeance. International Business Editor Ambrose Evans-Pritchard writes: The yield on German 10-year bunds blew through 1% today, spearheading a violent repricing of outstanding sovereign debt issues across the globe ... Paper losses over the past three months have reached \$1.2 trillion (U.S.). Benchmark 10-year yields have soared by 175 basis points in Indonesia, 160 in South Africa, 150 in Turkey, 130 in Mexico and 80 in Australia. The epicenter is in the euro zone as the quantitative easing strategy goes horribly wrong. While the German 10-year bund yield is 100 basis points higher since March, French, Italian and Spanish comparable sovereign bond yields have moved

up in lockstep. Meanwhile, the yield on 10-year U.S. Treasurys has risen by about 40 basis points recently and is now fast approaching 2.40%.



Data collected by Gabriel Stein at Oxford Economics reveals that narrow M1 money supply in the euro zone has been growing at the rate of 16.2% annualized over the last six months. One does not have to be a monetarist expert to recognize the glaring anomaly. Meanwhile, the broader M3 money supply has been increasing at an 8.4% rate on the same measure, a pace not seen since 2008.



Economic historians will one day ask how it was possible for 2 trillion euros of euro zone sovereign bonds – a third of the government bond market – to be trading at negative yields in the early spring of 2015, even as the inflation hammer was already coming down with crushing force. Mr. Stein elaborated: 'It was the greater fool theory! Traders and investors always thought there would be some other sucker coming along to buy at an even higher price. Now, the market is returning to sanity.'

THURSDAY, JUNE 11TH

- In its latest financial accounts report, the Federal Reserve states net worth for U.S. households and non-profit groups increased by \$1.63 trillion (U.S.) in the 1st. quarter to \$84.9 trillion (U.S.), citing gains in stock portfolio valuations and higher property values mainly fortified household balance sheets. Dana Saporta, an economist at credit Suisse Securities in New York, commented: 'Now that real estate assets are increasing in value, household net worth is broadening out. Indeed, the overall economic recovery is becoming deeper.'
- The Labor Department reports U.S. initial claims for state unemployment benefits increased by 2,000 to 276,000 in the week ended June 6th. while continuing claims were higher by 61,000 to 2.27 million in the week ended May 30th. Joshua Shapiro, an economist at Maria Fiorini Ramirez Inc. in New York, observed: 'Since layoffs remain low, the labor market is in reasonably good shape.'
- The Commerce Department reports U.S. retail sales rose by 1.2% in May, citing broadly based gains at automobile dealers, clothing retailers and department stores; following a modest 0.2% increase in April.
- In its semi-annual Financial System Review (FSR), the Bank of Canada warned: "The most important domestic financial system risk continues to be a broadly based decline in Canadian employment and incomes, particularly in oil producing regions, that significantly reduces the ability of household to service their debt, leading to a widespread correction in house prices." At a press conference, Bank of Canada Governor Stephen Poloz elaborated: "We judge that the vulnerability associated with household indebtedness is edging higher and the overall risk to financial stability in Canada is slightly higher than it was at the time of our December FSR."



Bank of Canada Governor Stephen Poloz.  
Photo source: Globe and Mail

- Front Page Headline, ZeroHedge – “Bankers Should Be Punished for Financial Crimes: Fischer. We doubt we need to explain the virtually infinite circularity contained in this quote from Stanley Fischer, the Vice Chair of the U.S. Federal Reserve. Suffice to say, that for the Fed to admit that the U.S. judicial system is broken and that not a single banker has gone to prison following years of abuse, nearly one third of \$1 trillion (U.S.) in legal settlements and charges by American commercial banks, many of which have now been found to have criminally manipulated markets – of which none more so than JP Morgan, whose CEO Jamie Dimon is now a billionaire as a result – and that the Fed has enabled and encouraged all of this with its policies is frankly unconscionable.

Today, the irony goes much higher when another central banker Mark Carney, former Governor of the Bank of Canada and currently Governor of the Bank of England ... recently stated that prison sentences for market manipulating traders and bankers should be extended from seven to ten years. Mr. Carney elaborated: ‘So-termed rolling bad apples or individuals who are fired from financial firms would no longer be hired in another job without their new employer knowing about their history, because real markets are essential to guaranty prosperity. Not markets that collapse when there is a shock from abroad. Not markets which occur in chat rooms. Not markets where no one appears accountable for anything.’ So, not markets which are artificially rigged by \$22 billion (U.S.) in central bank liquidity and which collapse every time the threat that any of this precious liquidity may be taken away? Regarding cracking down on criminal market-rigging banks, perhaps Mr. Carney can begin with Martin Mallett, the former chief currency dealer at the Bank of England, whose role in the foreign exchange rigging scandal was revealed early on and who was fired for serious misconduct just as promptly, before too many questions emerged ... Because we know Mr. Carney is very sincere and quite serious with his gratuitous and wanton statement, we eagerly await for Scotland Yard to appear on Mr. Mallett’s doorstep and cast him into the prison cell next to Navinder Sarao. As for bankers going to prison for ten years instead of seven, let’s begin with less lofty ambitions. How about some banker ... going to prison for ten minutes first.”

- Front Page Headline, GoldMoney – “The Fallacies of Gross Domestic Product. Researcher Alasdair Macleod writes: The common error of confusing economic growth with progress goes largely unnoticed, though it permeates all macroeconomic analysis. There is no better example of this mistake then the fallacies behind the interpretation of GDP. This statistic represents the market value of all final goods and services for a national economy in a given year. As such, it is only an accounting iden-

tity which reflects the quantity of money in the economy. Econometricians who construct GDP have devised a sterile statistic which should not be used to set economic policy. It leads to the common error of assuming that any increase in GDP is desirable. Statistics like GDP tell a story of an economy based upon historical prices, but which are devoid of any qualitative value; when progress, the improvement condition, is what really matters. Transactions reflecting both wealth creation and economically destructive state spending are included in the GDP without differentiation. Far from the government component of GDP being singled out from the total, it is often welcomed as contributing to economic growth. Macroeconomists, with an eye on the negative impact of cuts in government spending, discourage governments from making them. The lack of distinction between wealth-creation and wealth-destruction is basic to their belief that state intervention is beneficial.

More light can be shed on this issue with an example. Imagine an economy with a fixed quantity of money and credit and further assume that foreign trade is in balance with a stable population. Products will succeed, stagnate or fail. People will either receive wage increases, pay cuts, or be encouraged by reality to move from the least successful businesses into more successful businesses. The businesses of yesteryear fade and those of tomorrow evolve. Winners will redeploy resources released from the failures. Annual GDP, the sum total of all production paid for by everyone’s earnings and profits, will therefore be unaltered from the previous year because it is a zero sum, assuming that as a whole people’s money preferences relative to goods do not change. Without the injection of extra money, people are always forced to choose between items because they cannot add to the purchasing power of their income through extra credit created out of thin air; attempting to create demand that otherwise would not exist.

Therefore, progress is marked by improved products and lower prices, because as the volume and quality of production increases, the total money value of them must remain the same. This is true for both final products and for investment in the higher orders of production. Importantly, however, GDP growth is nil. Now we must consider what happens in the case of unsound money; that is to say money and credit which can be expanded by the will of the state and the banks it licenses. Over a period of time, this new money is absorbed into the economy, reflected in new transactions that otherwise would not have occurred. The value of transactions attributable to the expansion of money and credit is likely to be a multiple of the new money introduced, as it passes from the original beneficiaries to later receivers. If we assume this is a single expansion of the quantity of money,

these new transactions will only be a temporary feature. The prices of goods purchased with the new money rise to compensate for a time lag. Having initially expanded, real GDP would then contract as the temporal lag between stimulus and price effect is fully unwound. With all transactions fully accounted for, real GDP finishes unchanged, always assuming there has been no change in consumer preferences between money and goods.

The dubious benefit of stimulating demand by increasing the quantity of money and credit has been only temporary. Changes in GDP described above reflect not economic progress, but the absorption of the extra quantity of money and credit deployed. If the matter stopped there, the damage to a properly functioning economy would be limited, but monetary inflation also triggers a transfer of wealth from the majority of people to a small rich minority. This happens because price increases spread from where the new money is first deployed – typically via the banks and financial markets – leaving the majority of people to face higher prices with no offsetting monetary benefit. Therefore, there is a secondary impact which is the apparent benefit of increasing the quantity of money followed by a decline in demand for goods and services because of the wealth-transfer effect, i.e. the opposite of the intended result. The economy as a whole ends up worse off than if no monetary stimulus had occurred. This is why extreme monetary inflation is always accompanied by economic collapse.

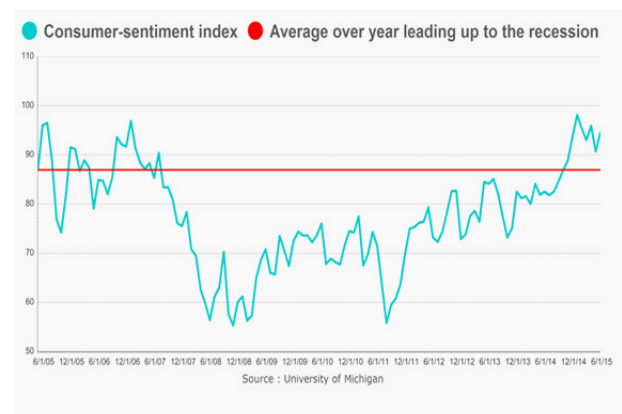
In the foregoing example, the effect of a single injection of additional money and credit was considered, but once embarked upon it almost always continues at a compounding pace. Macroeconomists note only the initial benefits and when they fade, as described above, they clamor for more. Over time, the result is that weak monetary policies lead to the continual currency debasement with which we are familiar today, together with the soaring debt levels, which are the counterpart of expanding bank credit. As the currency buys less, more is required in order to achieve the same initial effect. That changes in money and credit do not equate accurately to changes in GDP in practice, is partly due to econometricians selecting which activities to include in the GDP. They interpose an artificial distinction between categories of spending with the intention of isolating spending on new goods and services deemed to be consumption. This is an error, because these economists are forced into making a subjective judgment which is bound to be at odds with reality. In practice, a consumer can only be described in the broadest terms.

Consumers may spend money buying assets such as housing, art or stocks. There is no difference between spending on these

and on anything else, because they all have a valid purpose in the mind of the consumer. In addition, there are unrecorded transactions on the black market, or not recorded from small businesses, as well as transactions in second-hand goods which are specifically excluded on the grounds that the purpose of GDP is to record new production only. Therefore, much economic activity is excluded from the GDP calculation with the complication that money will flow between the econometrician's version of GDP to the wider transaction universe, undermining all the macroeconomists' attempts to link an increase in prices to an increase in the quantities of money and credit. In conclusion, GDP has nothing to do with economic progress. It is a flawed statistic that imperfectly summarizes the money value of selected transactions over a given period. The fact that it is usually positive is a reflection of the temporal difference between monetary inflation and the lagging effect on prices, but has nothing to do with economic progress."

#### FRIDAY, JUNE 12TH

- The Reuters / University of Michigan group reports their consumer confidence index rose to a preliminary reading of 94.6 in June, following a final level of 90.7 in May. In a research note, Bricklin Dwyer, an economist at BNP Paribas, commented: 'The gain in the Michigan consumer confidence index from already elevated levels suggests that there could be more good news on the spending front in the coming months.'



- The Labor Department reports the U.S. producer price index (PPI) for final demand, which measures prices that businesses receive for their goods and services, rose by a seasonally adjusted 0.5% in May. Core prices, which exclude the volatile food and energy categories, rose by a more modest 0.1%. In a research note, Ian Shepherdson, chief economist at Pantheon Macroeconomics, observed: 'It's clear that underlying price pressures at the producer level, at least for goods, remain very low; thanks to slow wage gains, weak materials prices and the

continuing strong U.S. dollar.’

CLOSING LEVELS FOR FRIDAY, JUNE 12TH.		WEEKLY CHANGE
Dow Jones Industrial Average	17,898.84	+ 49.38 points
Spot Gold Bullion	\$1,179.20 (U.S.)	+ \$11.10 per troy oz.
Spot Silver	\$15.93 (U.S.)	– \$0.16 per troy oz.
S&P / TSX Composite	14,741.15	– 216.01 points
10 – Year U.S. Treasury Yield	2.39%	– 2 basis points
Canadian Dollar	81.23 cents (U.S.)	+ 0.84 cent
U.S. Dollar Index Future	94.972	– 1.373 cents
WTI Crude Oil Futures	59.96 (U.S.)	+ \$0.83 per barrel
DJIA / Gold Ratio	15.179	– 0.102 point
Gold / Silver Ratio	74.02	+ 1.42 points

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