LONGWAVE group

UNDERSTANDING THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

THAT WAS THE WEEK THAT WAS

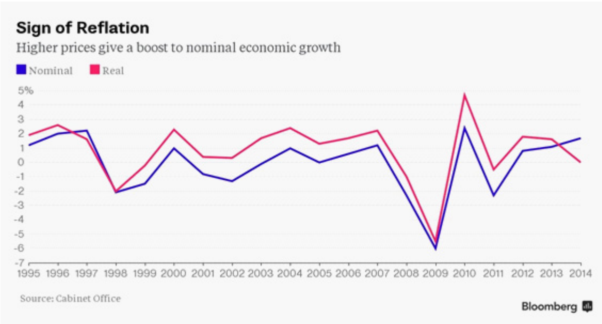
Monday, February 16th

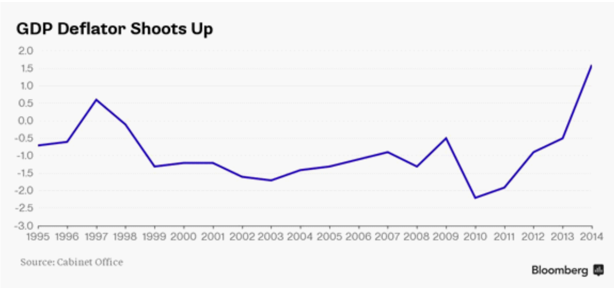
The Cabinet Office reports Japan's gross domestic product (GDP) expanded by an annualized 2.2%, on a seasonally adjusted basis, in the 4th.quarter of 2014, following two consecutive quarters of contraction; while the GDP deflator – a broad measure of

MONDAY, FEBRUARY 16TH

Holidays: Presidents' Day in U.S. /Family Day in Ontario

prices in the economy – increased by 2.3%.





Takeshi Minami, chief economist at the Norinchukin Research Institute, noted: "These are somewhat disappointing figures. The economic situation remains weak and corporations are clearly postponing investments."

TUESDAY, FEBRUARY 17TH

- The New York Federal Reserve reports its Empire State manufacturing index declined to a reading of 7.8 in February from a level of 10 in January. Any reading above zero indicates improving conditions. The index survey covers New York State, northern Connecticut and northern New Jersey.

- The Canadian Real Estate Association (CREA) reports the nation's existing home sales fell by 3.1% in January, following a decline of 5.8% in December.

- Statistics Canada reports foreign investors reduced their holdings of Canadian securities by $13.5 billion (CAD) in December, the biggest decline since June 2013. Foreign investors sold $8.5 billion (CAD) of Government of Canada bonds and corporate issues. The balance of the divestments were almost equally split between provincial government bonds, government guaranteed bonds and private placement corporate bonds.

- The National Association of Home Builders (NAHB) reports its U.S. builder confidence index for new single family homes declined to a seasonally adjusted reading of 55 in February from a level of 57 in January. A reading over 50 indicates a majority of builders regard conditions as generally positive. David Crowe, the trade group's chief economist, commented: 'Solid job growth, affordable home prices and historically low mortgage rates should help unleash growing pent-up demand and keep the housing market moving forward in the year ahead.'

A new house advertised for sale in Lake Forest, California Photo: Bloomberg News

- Front Page Headline, Daily Telegraph U.K. – "Greek Crisis Talks Collapse Amid Acrimony. International Business Editor Ambrose Evans Pritchard writes: 'Greece is on a collision course with the euro zone's creditor powers after emergency talks ended in acrimony on Monday night, triggering the most serious political crisis since the launch of the euro. The leftist Syriza government reacted with fury to euro zone demands that it must stick to the country's discredited austerity plan, describing the draft text as 'absurd and unacceptable.' Yanis Varoufakis, the Greek finance minister, stated: 'Eurogroup finance ministers have ignored a deal already agreed upon with the European Commission (EC) for a four month delay and a new contract for economic growth, returning again to old demands. The only way to solve Greece is to treat us as equals, not a debt colony. I expect European Union (EU) authorities will soon withdraw their latest ultimatum.' The talks were halted following four hours of stormy exchanges risking a traumatic showdown which could precipitate the biggest default in world history and force Greece out of the euro by the end of February. Mr. Varoufakis insisted: 'Mr. Syzira has won a landslide victory vowing to overthrow the EU/IMF troika memorandum and cannot betray Greek democracy. It would be an act of subterfuge to promise our partners that we would complete a program that we were elected to challenge."

WEDNESDAY, FEBRUARY 18TH

- The Federal Reserve reports U.S. industrial production rose by a seasonally adjusted 0.2% in January, while manufacturing output also increased by 0.2%. Capacity utilization held steady at 79.4%.

- The Commerce Department reports U.S. housing starts declined by 2% to an annual pace of 1.07 million units in January, citing winter snowstorms in some areas of the Northeast and Midwest hindered builder activity, following an upwardly revised 1.09 million units in December. Meanwhile, building permits for new construction declined slightly to an annual pace of 1.05 million units from December's upwardly revised level of 1.06 million.

- The Labor Department reports the U.S. producer price index (PPI) declined by 0.8% in January following an unprecedented drop in energy costs. In particular, gasoline prices fell by 24%, the biggest drop since 2008.

- Front Page Headlines, Globe and Mail – "Canada Targets Russian Interests with New Sanctions. The Canadian government announces it is imposing sanctions against the top Russian oil firm NK Rosneft OAO and the chairman of conglomerate Rostec, among others, in response to the actions of Russian-backed militants in Ukraine. Acting in co-ordination with the European Union (EU) and the United States, Ottawa stated it is imposing sanctions against 37 Russian and Ukrainian individuals; as well as 17 Russian and Ukrainian entities. The list includes both Kremlin military officials and politicians."

- Front Page Headline, Globe and Mail – FOMC Minutes Confirm Support for Stable Fed Funds Rate. According to the minutes of the January 27th. – 28th. Federal Open Market Committee (FOMC) policy meeting: 'Many participants indicated that their assessment of the balance of risks associated with the timing of the beginning of policy normalization had inclined them toward maintaining the Federal Funds Rate at its effective 0% - 0.25% lower range for a longer period of time. While considering risks to be nearly balanced, the committee noted a strong dollar, international flash points from Greece to Ukraine and slow domestic wage growth as strengthening the case for maintaining the status quo."

- Statistics Canada reports the nation's wholesale trade increased by 2.5% to $55.4 billion (CAD) in December from $54.1 billion (CAD) in November, citing widespread gains across the sectors, led by the motor vehicle and parts segment. Higher sales were achieved in six out of seven subsectors, accounting for 80% of total wholesale trade.

- The Mannheim-based Center for European Economic Research (ZEW) reports its latest business survey of analysts and institutional investors pushed its investor confidence index to a reading of 53 in February, following a level of 48.4 in January and its highest reading in 12 months.

- Front Page Headline, Gold-Eagle – "Gold and Russia. Researcher Alasdair Macleod writes: In late November, I wrote an article suggesting it could be in Russia's interest to put the rouble on a gold exchange standard. The salient points were the Russians could easily make it stick, inflation would be tamed and importantly Russia would divorce herself from the currency war being waged against her by her NATO enemies.

The immediate consequence of such a move would almost certainly drive gold prices higher, if only because gold bullion banks would be forced to reconsider their short positions, in the knowledge that Russia would probably become a more aggressive buyer to build her reserves. If one understands Austrian economic theory, this move would be very good for Russia, but would be judged reckless by mainstream macroeconomists. So, it is obviously a prerequisite that President Vladimir Putin's advisors would have to lean strongly towards strong money theories, if they were to advise in favour of such a move. Whether or not this is the case we do not know. The only thing we can do is look at the evidence and attempt to see things from Putin's point of view.

Mr. Putin is an old-fashioned mercantilist, tolerating mild dissent to preserve the appearance of democracy, but ruthless with anyone who gets in his way. He rules Russia like a business, always seeking the commercial advantage in alliances. For this reason, some time ago he decided that Russia's future lay as a dominant partner with China in a Eurasian super-state, so the Shanghai Cooperation Organization (SCO) was founded in 2001. It's a natural: Russia has the resources and China has the manufacturing. The SCO will encompass half the world's population under its control when India joins and will heavily influence another billion Asians. Even Turkey, a NATO member and previously an applicant to join the European Union (EU), intends to join the SCO instead. The West pushed Putin in this direction, by refusing to engage with him after the Litvinenko affair in London and by financing unrest in Georgia and Ukraine. These activities have only served to heighten Russia's sense of insecurity and renewed her determination to secure her borders. An important feature of the SCO is that China, Russia and most of the other members have been buying gold. China has been buying since at least 1983, but for Russia this constitutes a relatively new activity, having lost her official reserves at the time of the Russian financial crisis 1n 1998. Nevertheless, she has been buying aggressively so that she has more than tripled her holdings since 2005 to 1,207 metric tonnes, now the world's fifth largest stockpile. Importantly, during the recent rouble crisis, Russia continued buying gold at a time when she might have been expected to preserve her U.S. dollar reserves.

Circumstantial evidence perhaps, but Russia's gold policy clearly tells us that Mr. Putin's advisors favour the yellow metal. Of course, the reasons may not be economic, but strategic. What if Putin's intelligence services have evidence of the lack of gold in western central bank vaults? What if the Central Bank of Russia's gold dealers are setting a trap for the heart of the West's financial system and can break the bullion banks when they please? Both of these are possible and they may be fundamental to Russia's defence strategy, given the war being waged is more financial than military. We can only speculate, but there is an overriding aspect of the future that Mr. Putin is almost certainly considering: i.e. his legacy. If this matters to him, he will want Russia not only to survive, but also for her to be top-dog, with him as the architect. He has almost certainly been made aware of MacKinder's Heartland Theory: 'He who rules Eastern Europe commands the Heartland; who rules the Heartland commands the World-Island; who rules the World-Island controls the World.' Nor, is this mumbo-jumbo; Mackinder's point was that the World-Island, the inter-linked continents of Europe, Asia and Africa is the largest, most populous and resource rich of all possible land combinations. Russia's partnership with China through the SCO substantially achieves this particularly since China now also controls Sub-Saharan Africa.

When Mr. Putin has secured Russia's borders, he will need to deal with organized crime, eliminating it as much as possible. He must change the way he does business and enhance private property rights. With her low taxes, Russia will then be an attractive place in which to do business. Finally, Mr. Putin must secure the rouble from the increasingly inevitable collapse of the global fiat currency system. Ultimately, this is the importance of gold for Russia and the fact that she has been acquiring it aggressively, suggests Mr. Putin knows it. Remember, Putin is not like a western politician driven from one trivial crisis to another and wholly reliant upon a central bank to handle financial matters. Elvira Nabiullina, the governor of Russia's central bank, was previously Putin's personal economic advisor and is almost certainly his personal appointee. Through her, we can assume Mr. Putin controls the Central Bank of Russia.

Given that Mr. Putin is actively considering a move towards some sort of rouble-gold convertibility, it all comes down to timing. Ideally, Russia would probably like to add further to its gold reserves, although we don't know how much non-monetary gold that Russia owns. It is quite possible that Russia owns additional gold to the 1,207 metric tonnes declared to date. If so, a first step would be to declare the full position, which may trigger a similar declaration from China, there being no point in China continuing to conceal Russia's true position. Actually, the more gold that is in Russia's possession, the more likely it will want to announce its intentions sooner rather than later. To a large extent, timing will be up to NATO. If NATO escalates its involvement in Ukraine, with or without more financial sanctions, Russia might respond to stabilize the rouble by announcing a gold standard. The good news for us lesser mortals in the West is that at least a financial war is better than a nuclear war; that is, unless it becomes one." See also, Ian's Investment Insights – The Implications of the Pending Collapse of Fiat Paper Money, January 30, 2015.

THURSDAY, FEBRUARY 19TH

- The Labor Department reports U.S. initial claims for state unemployment benefits declined by 21,000 to a seasonally adjusted 283,000 in the week ended February 14th. while continuing claims increased by 58,000 to 2.44 million in the week ended February 7th.

Source: Business Insider

- The Philadelphia Federal Reserve reports its Current General Activity Index for the region's manufacturing sector fell to a reading of 5.2 in February from a level of 6.3 in January; the third consecutive monthly decline.

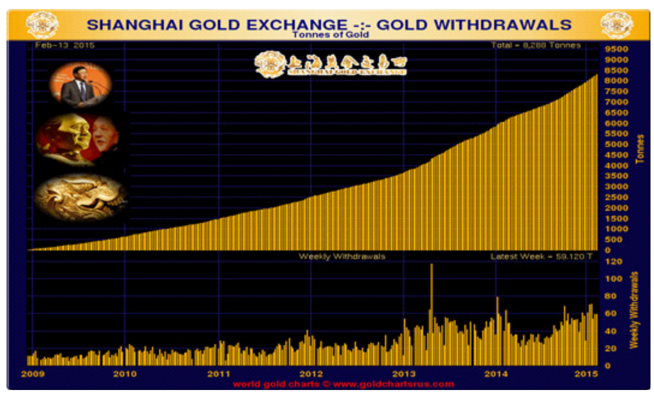
- The New York-based Conference Board reports its index of leading economic indicators (LEI) rose by 0.2% to a reading of 121.1 in January, following an increase of 0.4% in December. Ataman Ozyildirim, an economist at the Conference Board, observed: "While the LEI suggests some positive activity in the short-term, the lack of strong momentum in residential construction along with a weak outlook in new orders for manufacturing, pose a downside risk for the domestic economy." An LEI base reading of 100 was established in 2010.

FRIDAY, FEBRUARY 20TH

- Markit Economics reports its U.S. purchasing managers' index (PMI) for the manufacturing sector rose slightly to a preliminary reading of 54.3 in February from a level of 53.9 In January; citing new orders slowed to the weakest rate in just over a year and there was almost a stagnation of exports. Chris Williamson, chief economist at Markit, commented: "This PMI survey adds to the sense that while still expanding at a solid pace, the U.S. economy has entered a slower growth phase." This preliminary estimate is typically based upon approximately 85% - 90% of total survey responses each month and any reading above 50 indicates improving conditions.

- Statistics Canada reports the nation's retail sales totaled $42.1 billion (CAD) on a seasonally adjusted basis in December, down by 2% from November and representing the biggest one month decline since 2010. Statscan cited: "While sharply lower gasoline prices were a factor – gas station sales fell by 7.4% – the overall sales drop was broadly based, with 9 of 11 sectors recording declines."

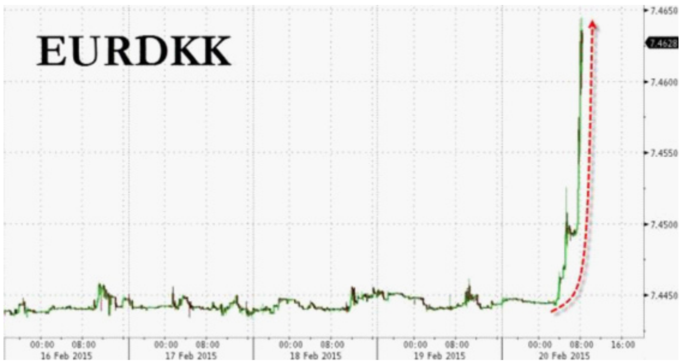
- Front Page Headline, Mineweb – "China's Gold Demand Surges by 17% Year-To-Date. Shanghai Gold Exchange (SGE) withdrawals have reached 374 metric tonnes in the first six weeks of the year; a record level leading to the 10-day Chinese New Year holiday which commenced yesterday. China, along with India, leads the world in gold demand and this Chinese New Year is no exception. Official 'Year of The Ram' gold coins sold out days ago.



Since another 59 metric tonnes of gold was withdrawn from the SGE last week, Chinese demand has already risen by 32% to 374 metric tonnes on a year-over-year basis … Despite the SGE's closure for the New Year holiday, it is gold in the pipeline from the West to China and other points East which should be setting the volume pattern and this will still be substantial. With good reason, gold analysts believe that Chinese demand for gold will now subside perhaps to the beginning of Q3, as it did last year, once the New Year gift giving has passed. Thus, once gold market activity resumes in ten days' time, SGE withdrawals will be followed particularly closely by those looking to try and assess the likely level of overall Chinese demand for gold in 2015. While China's economy is seen as slowing down considerably, it is not considered to be in recession, so there has still been a continuing accumulation of wealth in general, as well as by those seen as entering the middle classes who have embraced the gold buying culture …

As more and more Chinese citizens move up the socioeconomic ladder over the next five years, China's middle class is expected to grow from 300 million to 500 million; nearly 200 million more people than the entire population of the United States. This should help boost gold bullion and jewelry sales in China."

- Front Page Headline, Silver Arrow Partners – "Danish Central Bank Willing to Use Capital Controls to Defend DKK Peg. This remark emanating from Hans Jorgen Whitta-Jacobsen, chairman of Denmark's Economic Council, has sparked the biggest decline in the Danish krone against the euro since 2001."



Source: Silver Arrow Partners

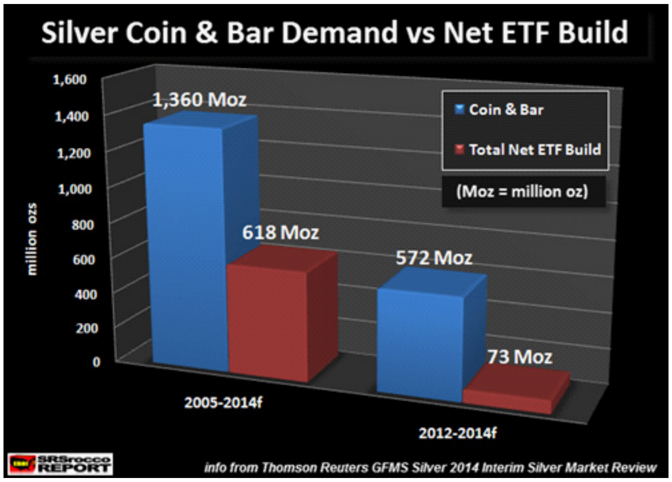
- Front Page Headline, Gold Money – "Update of the Global Economic Outlook. Researcher Alasdair Macleod writes: On January 9th. I wrote an article suggesting that 2015 would unfold as the year of the economic slump. The article's title ended with a question mark, but today we are closer to removing it in favour of an exclamation mark. During recent weeks, it has become clear that key economic blocs are heading for a slump including, but not limited to China, the euro zone and Japan (allowing for the distortions of her aggressive money printing). Together, they account for nearly 40% of global gross domestic product (GDP). We know this because of the collapse in commodity prices, which is reflected in a global shift in preference to the U.S. dollar. For the avoidance of doubt, money should be regarded as a good and each currency as a different good. When this point is grasped, the context of the dollar's rise against both commodities and other currencies becomes clear. Since both commodities and currencies are priced in dollars, so banks, consumers and businesses are preferring to hold U.S. dollars.

  Modern macroeconomics fails to adequately explain the importance of these developments. A quick look at the index in Keynes' General Theory makes no mention in changes in preference for money versus other goods. It lists and defines liquidity preference which is a different topic. Once one accepts money as a good, supply and demand will always balance as predicted in Say's Law, otherwise known as the Law of the Markets. Something has spooked consumers in markets around the world into spending less on other goods and to increase their holdings of U.S. dollars. The explanation can only be that prices for all other goods have been too high relative to dollars, so they were destined to fall. There can be no clearer signal that there is a slump occurring in global economic activity.

  The largest supplier of physical goods exports is China. Demand by other countries for China's goods is declining, confirmed by the Baltic Dry Index which is plunging to new lows. This slowdown in economic activity could easily burst the bubble of bank credit, which is in danger of collapsing under the massive burden of bad debts. December's slowdown in new loan demand coupled with declining trade flows can only be temporarily resolved by China devaluing the renminbi, thereby lowering her export prices. The breathing space this gives China is only as long as it takes for her manufacturing costs to increase, in order to reflect the devaluation. If it occurs, a renminbi devaluation would quickly put more downward pressure on prices for local manufacturers in her export markets.

  Turning to China's trading partners; we see the euro zone's economy – ex-Germany – beginning to contract, which is panicking the European Central Bank (ECB) into money printing in a desperate attempt to maintain too high prices. Japan has been doing this for some time and is laboring under a mountain of debt which makes even Greece look responsible. The signals are clear: the world has already entered a downturn in economic activity. Therefore, we can expect accelerated money printing and the imposition of additional negative interest rates in a forlorn attempt to avert economic reality."

- Front Page Headline, SRSRocco – "Investors Overwhelmingly Prefer Physical Silver. According to the Thomson Reuters GFMS 2014 Interim Silver Market Report, since 2005 precious metals investors have purchased a staggering 1.36 billion ounces of silver bars and coins. This is a huge amount when one considers that annual demand was a lowly 30 million oz. (Moz) in 2001. All that changed during the U.S. financial crisis of 2008 when silver bar and coin demand soared to 187 Moz from 51 Moz in 2007. From the chart below one can see how much greater physical silver demand has been over paper silver.



Over the past three years, precious metals investors purchased an estimated 572 Moz of physical silver bars and coins, compared with a paltry 73 Moz of net ETF purchases … It is our belief that the current global financial and economic system is unsustainable. Precious metals investors have concluded that paper is not a wise investment. So, when the U.S. dollar finally goes down in history as another failed fiat currency, wealth will be tabulated on the basis of how many physical ounces of silver one holds."

CLOSING LEVELS FOR FRIDAY, FEBRUARY 20TH.		WEEKLY CHANGE
Dow Jones Industrial Average	18, 140.44	+ 121.09 points
Spot Gold Bullion	$1,204.90 (U.S.)	– $22.20 per troy oz.
Spot Silver	$16.22 (U.S.)	– $1.11 per troy oz.
S&P / TSX Composite	15,172.24	– 92.57 points
10 –Year U.S. Treasury Yield	2.11%	+ 6 basis points
Canadian Dollar	79.71 cents (U.S.)	– 0.54 cent
U.S. Dollar Index Future	94.341	+ 0.156 cent
WTI Crude Oil Futures	$50.81 (U.S.)	– $1.97 per barrel
DJIA / Gold Ratio	15.056	+ 0.371 point
Gold / Silver Ratio	74.285	+ 3.475 points

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