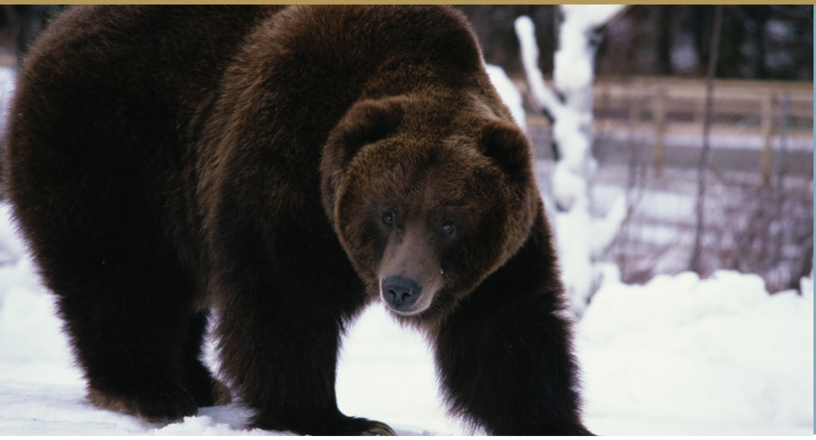
Volume 29 | Issue 1 . July 28, 2011

LONGWAVE group

THE LONGWAVE ECONOMIC AND FINANCIAL CYCLE

WINTER WARNING



The Death of Paper Money

We are now facing the greatest economic crisis the industrial world has ever encountered. This financial crisis is likely to be far greater than any disease or war yet experienced. I have given this matter a great deal of thought before making such an assertion, but I cannot think of any event in history that ever had the ramifications of the current debt crisis, which threatens to engulf the world in a terrifying and massively destructive economic depression. There have been wars and plagues which have resulted in huge losses of human life, but the potential scale of human misery brought about by the collapse of the international debt bubble is likely to be beyond compare. I know that I am frightened, not only for myself and my family, but also for everyone else, because once governments lose control of the debt situation our world will likely turn upside down.

I am sure that many of you will consider me an alarmist. However, my job is to prepare myself, my family, my readers and my friends, for whatever the financial and economic future might hold in store. Alas, what I see in the future, in that vein, is truly frightening.

We are often advised 'to prepare for the worst and hope for the best.' Unfortunately, there's not much 'best' that I can see in this whole debt fiasco, which means that we must definitely prepare for the worst.

What convinces me to make such an alarming prediction is my envisagement that the world's paper monetary system is now in its death throes and there is nothing that can be done to alter the course of its demise. Politicians and central bankers throughout the industrialized world are desperately trying to prolong the life of paper (fiat) money by creating even more of it. How stupid is that? Albert Einstein said, "We cannot solve our problems with the same thinking that we used when we created them." Obviously, our leaders lack even a modicum of the intellectual capacity of an Albert Einstein.

The beginnings of the end of national monetary discipline began with the outbreak of the First World War, when all combatants opted to abandon gold as the backing for their respective currencies. It accelerated during the early years of the depression, when the world monetary system, based on a quasi-gold standard, collapsed. This breakdown enabled countries to print paper currencies without any reference to gold.

A new world monetary system was created at Bretton Woods, New Hampshire in 1944, when the U.S. dollar was made exchangeable into gold at $35.00 (U.S.) per ounce. This exchange privilege was only accorded to countries not individuals. Indeed, American citizens were still banned from owning gold, having lost that privilege by President Roosevelt's edict in 1933.

During the 1960s, the U.S. began to ramp up the printing presses to pay for the Viet Nam war and President Johnson's 'Great Society.' America's trading partners became alarmed by this turn of events and many countries, France in particular, accelerated the pace of their exchange of U.S. dollars for gold. In August 1971, President Nixon responded to the drain on U.S. gold stores by closing the gold window. Thus, the vestiges of a gold based monetary system ended and paper money became the indigenous medium of exchange for every nation.

In the history of the world, this represents the first era that every nation's currency is fiat paper. So, we are in uncharted waters when it comes to knowing what the repercussions of the worldwide collapse of paper money might be. We can surmise that such worldwide currency destruction will have huge and horrible implica-

LONGWAVE group

tions. We can only reference what happened during and after the collapse of a paper money system in a particular country. To that end two paper money experiences in France can provide us with valuable insights into the unfolding process of destruction of the currency and how the French people acted to protect themselves from the calamity.

Our first example is John Law's paper money scheme that he introduced to France in 1716. Typically, at the onset of any paper money system, Law was careful to control the number of paper money notes issued. He stipulated that there was to be at least 25% coin backing for the paper notes that were issued. But the French Regent became an owner in the bank (Banque Royale) and it was he who made the decision regarding the size of the paper issue versus the amount of reserves held.

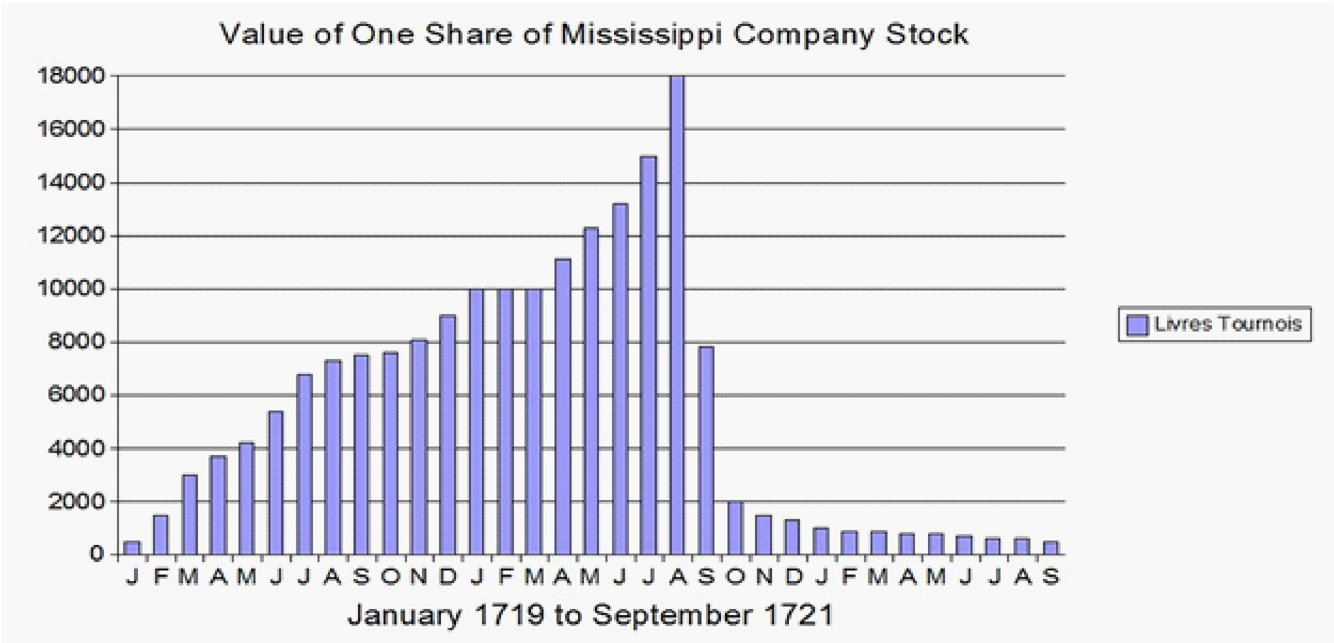
In conjunction with the establishment of the Banque Royal, John Law also established the Mississippi Company, based on the vast Louisiana lands then controlled by France, in which shares were issued to the general public. His company issued more shares with the acquisition of tobacco farming in the colonies, slave trading in Senegal and the right to trade in the East Indies. Soon the Mississippi shares broke through their par price; "aided by a flurry of rumour, the herd instinct took hold."[1] The Banque issued fifty million paper notes to accommodate the new shareholders. The bank continued to print more and more notes and issued more loans to enable people to buy and deal in shares, which just fueled an ever increasing share price value.

"Outside the Mississippi Company office, throughout the summer of 1719, Paris was rapidly engulfed in unprecedented speculation madness. By mid-August the shares that three months earlier had languished at 490 livres were being snapped up at 3,500."[2] By October 1719, the share price of the Mississippi Company had risen to 6,500 livres. As prices continued to rise, more and more speculators, jumped into the market driving prices even higher. By May 1720 the share price had risen above 10,000 livres. The following month it was trading at 13,000 livres and in July at 15,000 livres. In August 1720, Mississippi shares sold for a record price of 18,000 livres. Within 18 months the value of the shares had increased 36 fold.

This new found paper wealth was used to purchase luxury goods of all descriptions. "The age-old symbols of wealth – jewels, expensive clothing, gold, silver, property, and prestigious furnishings – were avidly sought….Goldsmiths and silversmiths, whose businesses had languished in the wake of Louis XIV's financial crisis, now found themselves inundated with orders…The weavers at tapestry workshops in the Gobelins, in the provincial town of Aubusson, and in the Savonnerie carpet factory were deluged with commissions. Porcelain, another eye-catching luxurious status symbol, was imported in vast quantities to fill the tabletops, cabinets, and walls of the elegant salons of the newly rich….Summing up the prevailing mood, the regent's doughty mother wrote, with a note of apprehension, 'It is inconceivable what immense wealth there is in France now. Everybody speaks in millions. I don't understand it at all, but I see clearly that the god Mammon reigns an absolute monarch in Paris."[3]

One of the first to sell his shares was Richard Cantillon a friend of John Law, who sold when the price went above 12,000 livres in August 1720. He "realized that the bull market was based on little more than smoke and mirrors and ever-increasing quantities of paper money. Feeling that a crash was both inevitable and imminent, he cashed in."[4]

By September 1720, prices had collapsed below 8,000 livres in a wave of panic selling. By October, the shares were trading at 2000 livres. Most of the sellers converted their proceeds into coins and either hoarded them or sent them overseas. The Prince de Conti took some 4.5 million livres to the Banque and demanded coins. Law had no alternative but to comply. It was said that the Prince needed three wagons to carry away the coins.



John Law's Banque Royale and the Mississippi Bubble – John E. Sandrock.

By the end of 1720, some 500 million livres in silver and gold had been taken out of France. Merchants began to accept paper only at a discount and in some instances refused to accept it at all, demanding payment in coin (gold and silver). The proliferation of paper money caused prices to rise in all commodities. Property prices rose by three or four times, because many stock sellers chose to convert their paper wealth into land.

Law introduced an edict on January 28, 1721, banning the export of coin. To circumvent this, many people exchanged their money for diamonds and other precious stones, which they hastily sent abroad. Law quickly retaliated by banning the purchase and wearing of diamonds and other precious jewels. But the ban failed to halt the move away from paper. Instead of diamonds and precious stones, investors started buying gold and silver artifacts, like tureens, candelabra, dishes, plates and cutlery. Two weeks later, this route was blocked, by the issuance of new law which banned the manufacture and sale of all gold and silver artifacts, except those used in a religious ceremony. It was not long before prices soared for chalices, crucifixes and candlesticks.

Meanwhile, the run on the Banque's reserves forced Law to introduce more oppressive measures. On February 27, 1721, he issued an edict which banned the possession of more than 500 livres of gold and silver and designated that all payments in excess of 100 livres were to be made in banknotes. All gold and silver in excess of the stipulated amount had to be brought to the Banque and exchanged for paper. Those who failed to comply could expect to be severely punished and informers were encouraged with generous rewards.

The printing presses kept producing paper money. In May 1720, more than 2.6 billion livres were issued. Worried that the whole system was about to crash, John Law decided on a desperate move.

On May 21st. he announced that Missiissippi shares now priced at 9,000 livres would only be worth 5,000 by December. The value of banknotes would also be reduced to half their current value. He argued that it was of fundamental importance to the nation to redress the value of paper notes and coin reserves, upon which France relied for foreign trade.

"In the past five months the long-suffering public had witnessed multiple changes in the value of their currency; their coinage had been outlawed; wearing jewelry had been prohibited, even crucifixes were banned. He had left them only with paper." "The day after the announcement a disaffected mob gravitated to the bank. When they found it closed they began to pelt it with stones. For three days riots erupted in the streets of Paris."[5]

With only 2% of the money in circulation being in gold and silver, Law reasoned that financial stability could only be restored if the amount of paper, shares and money, was reduced and the value of coins was increased. Accordingly, over a period of weeks thousands of livre notes and share certificates were publicly burnt. But confidence in paper had been lost. "Every smoldering bonfire sapped the credibility of paper, and the press for coins grew more insistent."[6]

The public anger against Law and even his family grew more pronounced. Meanwhile, the Regent realized that real economic recovery could not take place as long as the people were determined that Law and his paper money system were untrustworthy and that the parliament, the financiers and the wealthy elite were determined to oppose him. He sought the advice of the bankers and financiers to provide him with the means wherewith his regime might receive desperately needed hard money. Their advice was "a return to the old metallic system of money and the abandonment of paper credit."[7]

On October 10, 1721, the French government, supported by the Regent, declared that as of November 1, France would return to a specie-backed monetary system. Marais's response to this was "Thus ends the system of paper money, which has enriched a thousand beggars and impoverished a hundred thousand honest men."[8] Voltaire cynically remarked that with its demise "Paper money had returned to its intrinsic value, which is zero."

Our second example, also based in France, occurred approximately 70 years after John Law's paper money experiment. You'd think that memories of that calamitous episode would still be reasonably fresh in the minds of the French people in 1789, but apparently not. In that year, France found herself deeply in debt and with an economy in ruins. This problem, or so it seemed to the lawmakers, was caused by a lack of money and before long the idea of introducing paper money as a solution was promulgated again.

The Finance Committee of the General Assembly reported that it was the French people who demanded a new circulating medium of exchange and that paper money provided the best option, because "It will bind the interests of the citizens to the public good."[9] In that regard, it concluded that paper money, carefully guarded, in the amount of four hundred million livres be issued. This money would be available to purchase church lands which the government had decided to confiscate. Not only could the money be used to stimulate the moribund economy, but also, France could repay her debts from the proceeds of the sale of church lands.

It remained for the National Assembly to address the people regarding the advantages of this paper issuance, which was named the 'Assignat.' Part of the proclamation read as follows – "Paper money is without inherent value unless it represents some special property (In this case the church lands). Without representing some special property it is inadmissible in trade to compete with a metallic currency, which has value real and independent of the public action: therefore it is that the paper money which has only the public authority as its basis has always caused ruin where it has been established; that is the reason why the bank notes of 1720, issued by John Law, after having caused terrible evils, have left only frightful memories. Therefore, it is that the National Assembly has not wished to expose you to this danger, but has given this new paper money not only a value derived from the national authority but a value real and immutable, a value which permits it to sustain advantageously a competition with the precious metals themselves… These Assignats, bearing interest (3%) as they do, will soon be considered better than coin now hoarded, and it will bring it out again into circulation."[10]

The initial results of this issue were all that could be desired: a portion of the public debt was repaid; credit was revived; trade increased and the economy improved. But within five months of the issue, the government had spent what it had received from the sale of church lands and was again in financial distress.

Thus, a new issue of Assignats was debated in the Assembly. The great orator, Mirabeau argued vehemently, in favour of a new issue, saying that the most pressing issue was to get the church, now government, lands into the hands of the people. He extolled the value of Assignats, which were convertible into public property and declared that the notes were better secured than if redeemable in specie (gold and silver). He concluded by saying "If gold has been hoarded through timidity or malignity, the issue of paper will show that gold is not necessary, and it will then come forth."[11] On September 29, 1790, the Assembly passed the issuance of a further 800 million Assignats, which unlike the first issue were to bear no interest. It decreed that there was to be further issue of paper money and that as fast as the Assignats were turned in for land they were to be burned. (Fat chance).

This paper money issuance had typically, followed Thomas Gresham's dictum that 'bad money drives out good' and forced small silver and copper money to disappear. Within a short time, the Treasury had received one hundred and sixty million livres in payment for land. That paper money, according to the decree of the Assembly, should have been burnt, but for the most part it was re-issued in smaller notes to compensate for the disappearance of small silver and copper coinage.

Prices began to rise and the call for even more paper money issuance became louder and louder. To that end, following the previous last issue and the determination not to issue any more paper, a new issue of six hundred millions more assignats was approved on June 19, 1791.

"The nation was becoming inebriated with paper money. The good feeling was that of a drunkard just after his draught; and it is noted as a simple historical fact, that as the draughts of paper money came faster the successive periods of good feeling grew shorter."[12] The decline in the purchasing power of the paper money corresponded to the disappearance of gold and silver coinage. "The disappearance of specie was attributable to a natural law, simple and consistent, the superior money had been withdrawn because an inferior currency could be used."[13]

On December 17, 1791 a new issue was ordered, because it was deemed that the circulation of assignats was becoming rarer by the day. The total amount of assignats now in circulation amounted to twenty-one hundred million. The value of a hundred livre note was now worth only 68 livres.

In March 1792, another issue was announced. Then in July 1792, it was reported that the total amount of assignats issued amounted to twenty-four hundred million, which was less than the value of the national (church) lands, which gave the excuse for another issue of 300 million.

This huge release of paper money engineered, as it always does, a speculative fervor that spread throughout France. "A still worse outgrowth was the increase of speculation and gambling. With the plethora of paper currency in 1791 appeared the first evidences of that cancerous disease which always follows large issues of irredeemable currency – a disease more permanently injurious to a nation, than war, pestilence and famine. For at the great metropolitan centers grew a luxurious, speculative stock-gambling body, which, like a malignant tumor absorbed into itself the strength of the nation and sent out its cancerous fibers to the remotest hamlets. At these city centers abundant wealth seemed to be piled up. In the country at large, there grew a dislike of steady labour and contempt for moderate gains and simple living."[14]

By now, the General Assembly didn't even bother setting a limitation on the total amount of issuance, as it had done in the earlier days, because the limit had never been respected anyway; similar to the U.S. debt ceiling which has been raised 102 times since 1917. Issue followed issue at regular intervals so that by December 14, 1792 the official number in circulation amounted to twenty-eight hundred million.

In 1773, the French government confiscated the lands of aristocrats, who had fled the country at the onset of the revolution. These lands were offered for sale, which allowed for the issue of even more assignats. Previously, the issuance of paper money had been made public by decree from the National Assembly, but now they were made in secret and they were made so frequently that four hundred workmen were added to the number already employed printing the money.

The value of the massive amount of assignats in circulation dropped to about a third, evidenced by large price increases in all products, particularly food. While the government looked for a scapegoat, the obvious fact was of course, that it was printing far too much money.

The government ordered price controls under the law of Maximum. This had the effect of depressing manufacturing and more importantly, agriculture. Farmers found it difficult to raise their products at anything like the new price fixed by the law and when they held back selling their crops or livestock, these were frequently taken by force. To detect goods withheld by shopkeepers and farmers a spy system was established with the informer receiving the value of one third of the concealed goods.

In an effort to make the paper money equal to specie, the National Convention decreed that anyone selling gold or silver coin or anyone making any difference in any transaction between paper and specie should be imprisoned in irons for six years and anyone who refused payment in assignats or at a discount should pay a fine of three thousand francs for the first offence and a fine of six thousand francs for the second offence; plus suffer imprisonment for twenty years in irons. By September 1793, the penalty for such offences was death, with confiscation of the perpetrator's property. Informants of such 'criminal' actions were offered a reward. In May 1794, the Convention decreed that the death penalty would be imposed upon anyone convicted of asking in what payment was the transaction to be concluded.

The Finance Minister, Cambon, concluded that the worst enemy of his paper money was gold and silver, so he closed the precious metals exchange. Shortly thereafter, under terrifying penalties, he banned all commerce in precious metals.

Meanwhile, the printing of assignats continued at an ever-increasing pace. Towards the end of 1794 there were seven billion assignats in circulation. By the end of May 1795, the circulation was increased to ten billion and by the end of July, to fourteen billion.

The value of the 25 franc gold Louis acted as a monitor to the activity of the printing presses, much the same as the price of gold is doing today. On August Ist., 1795, this gold coin was worth in paper, 920 francs; on September 1st., 1,200 francs; on November 1st., 2,600 francs; on December 1st., 3,050 francs. In February 1796, the coin's value had risen to 7,200 francs. The last quotation set the value at 15,000 francs. That is, one franc in paper was worth 600 francs in gold.

Prices of all commodities rose in approximate proportion to the increase in the value of gold. For example, the price for a bushel of flour increased 100 times between 1790 and 1795; the price of eggs increased by a little more than ten times over the same period and the cost of a pair of shoes increased forty fold.

In February 1796, the government issued a new paper money, mandats, which it deemed 'as good as gold'. But to no avail, within six months the value of the currency had plummeted to only three percent of their original face value. At the same time as the original issue of mandats, the plates and paper for the printing of assignats were destroyed. By this time, there were throughout France approximately 40 billion livres in circulation. As for the mandats there were 2.5 billion issued.

In February 1797, the government withdrew the legal tender laws pertaining to both assignats and mandats, which became worthless after May of that year. Gold and silver, once again, became the binding French currency.

In May 1799, Napoleon orchestrated a coup d'etat in France, and became First Consul. At that time "the condition of fiscal affairs was appalling. The government was bankrupt and an immense debt was unpaid. The further collection of taxes seemed impossible; the assessments were in hopeless confusion…All the armies had long been unpaid, and the largest loan that could for the moment be effected was for a sum hardly meeting the expenses of the government for a single day. At the first cabinet council Bonaparte announced what he intended to do. He replied, 'I will pay cash (gold and silver coin) or I will pay nothing.' From this time on he conducted all his operations on this basis. He arranged assessments, funded the debt and made payments in cash."[15]

When the European coalition was formed against him, Napoleon was hard pressed financially and it was proposed that he resort to paper money, but he wrote to his minister, “While I live, I will never resort to irredeemable paper.” He never did and France under his leadership commanded all the gold she needed. Some of this gold came from the sale of the huge land mass of Louisiana to the United States in 1803 for $15 million (U.S.) of which $3 million (U.S.) was paid in gold.

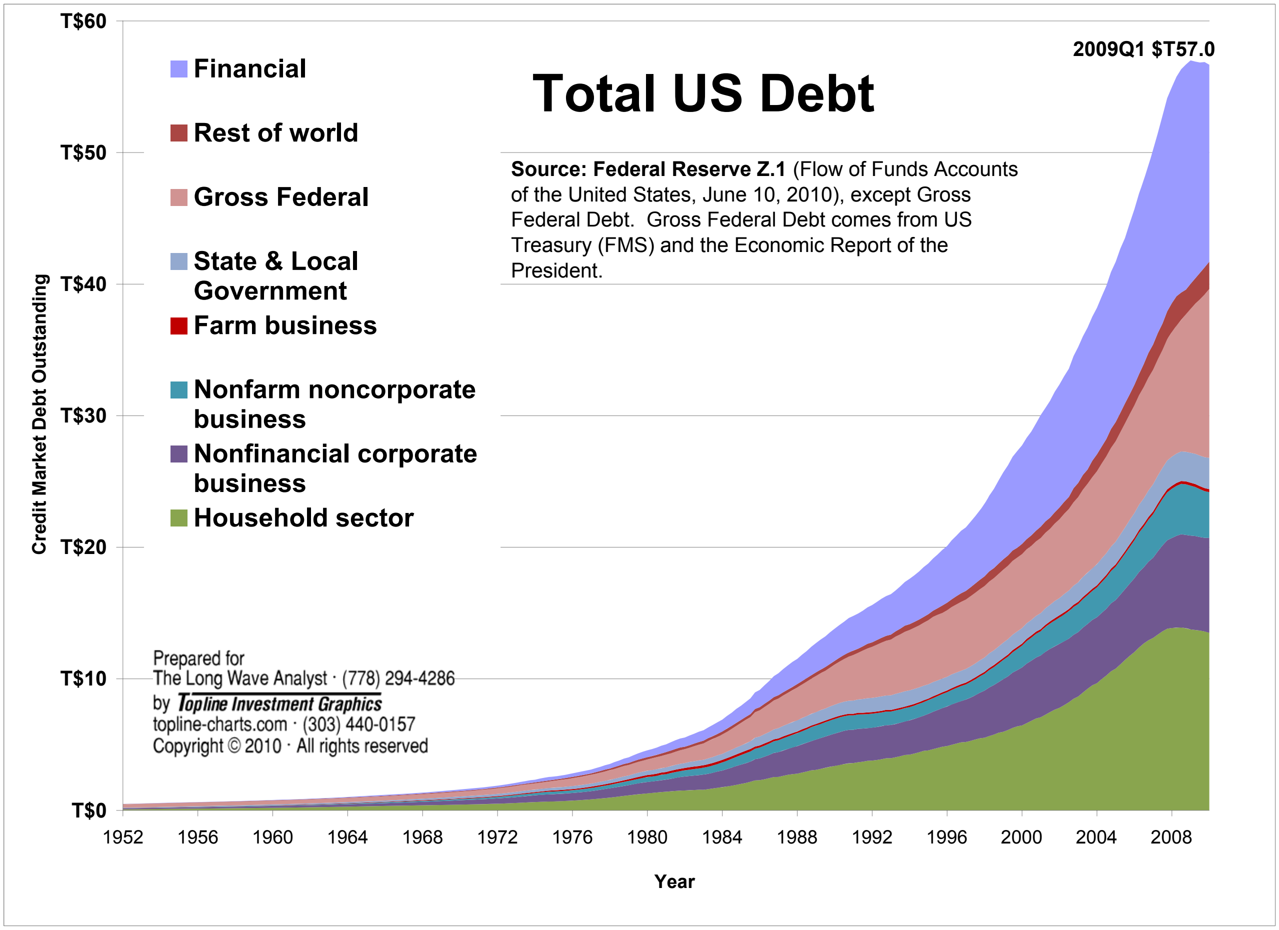
These two French examples clearly demonstrate that paper money always fails as a currency for the simple reason that it’s just too easy for governments to continue printing it at an ever increasing rate, which effectively devalues the currency to a point at which time it becomes worthless. However, these examples also show us that governments hate to abandon their prerogative to print money. They will use all the powerful means at their disposal to retain their privilege to create paper money, and they will continue to do this long after their citizens’ trust in fiat money has been lost.

The problem with the issuance of paper is that it takes more and more of it to keep an economy functioning. Eventually, however, the economy becomes saturated with an overabundance of fiat money. At that point no amount of additional money can keep the economy expanding. Rather, the economy begins to roll over, first into a recession and then into a depression, overwhelmed by massive debt.
Paper money is debt money and the world economies are being devastated by the collapsing debt bubble. Typically, governments are responding by issuing even more paper/ debt in their misguided attempts to reignite their respective economies. It will not work. Paper money is in extremis.

America’s national debt was $437.5 billion (U.S.) at the beginning of 1952, essentially the onset of our current Kondratieff cycle and spring. This debt, much of which had been eradicated in the prior Kondratieff winter was less than 1% of the current total American debt amounting to $57 trillion (U.S.).

A review of the U.S. debt chart shown below shows the exponential rise in debt began in about 1982, which was the beginning of the Kondratieff autumn and always the season during which massive amounts of debt are accumulated. In 1982, America’s total debt was about $5 trillion (U.S.), so it has increased by more than tenfold since then. The other thing to notice is that since 2000, which we have always deemed the onset of the Kondratieff winter, U.S. debt has continued to increase exponentially, more than doubling. This is not the way it is supposed to happen; winter is the season when debt is expunged. That process has been delayed, until now. The debt unraveling, now just beginning in the United States and evidenced by the collapse of consumer debt, particularly mortgage debt and the dire straits in which many states and municipalities are now found, has prostrated the American economy. The U.S. government, aided by the Federal Reserve, in much the same way that the respective French governments at the time of John Law’s paper money and the period of the assignat, is desperately attempting to right the ship by creating massive amounts of new paper money. From the beginning of 2007 to the 1st quarter of 2011, America’s federal debt has increased by $ 5.6 trillion (U.S.). Meanwhile, the Federal Reserve, according to the recent audit undertaken as a result of the ‘Dodd-Frank Wall Street Reform and Consumer Protection Act,’ issued $16.1 trillion (U.S.) in emergency loans in the period between December 2007 and July 2010. We can add another $1.4 trillion (U.S.) to that through two quantitative easings. “This inflationary (money printing) explosion is unprecedented in any era. It represents the biggest ever effort to rescue a debt-based system from the ravages caused by its own debt issuing excesses. It has, at best, provided a ‘remission’ for global paper markets. The cost has been devastating for REAL economies everywhere.” The Privateer – Number 683, Late July Issue. There comes a point in time when the issuance of more paper money cannot revive a dying economy.

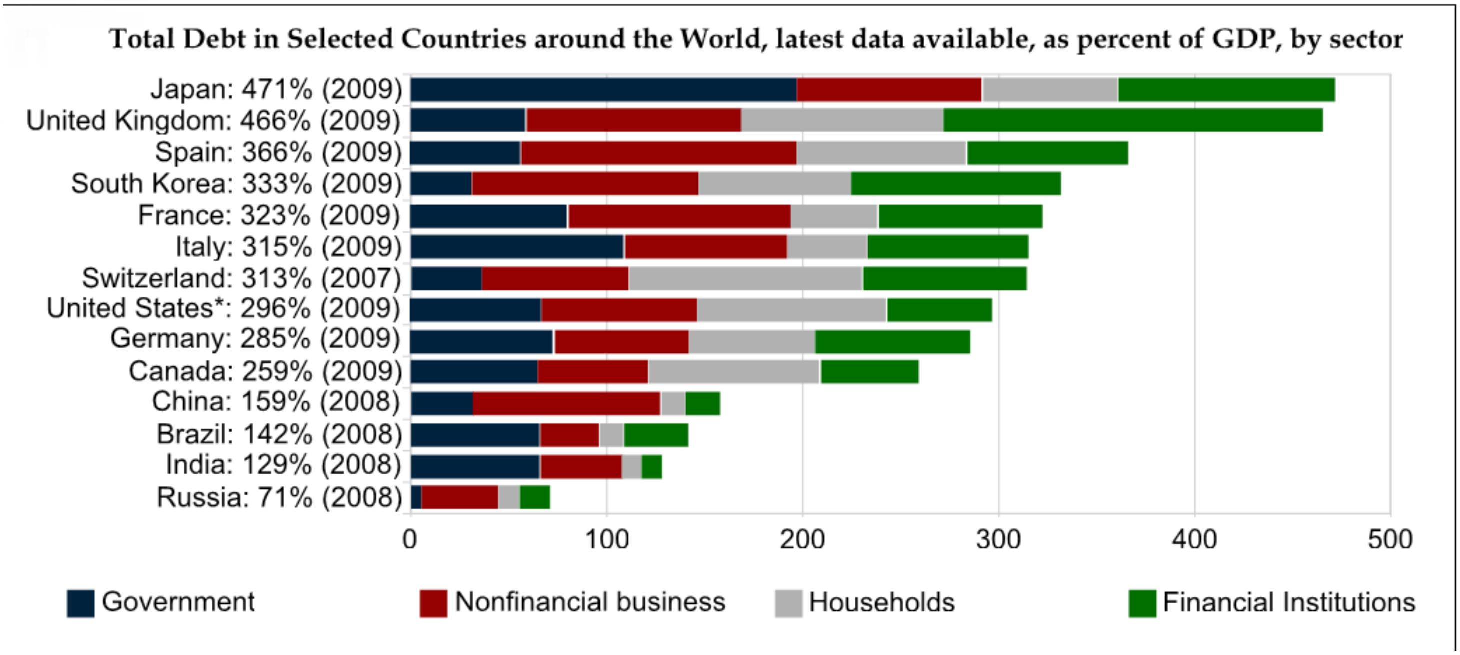
Volume 29 | Issue 1 . July 28, 2011



World debt has almost doubled from $57 trillion (U.S.) in 2000 to $109 trillion (U.S.) in 2010. The paper money printing presses have not been for the exclusive use of the United States. The following chart, which depicts total debt per GDP of several select developed countries, shows the enormity of the debt problem that exists worldwide. Most of the numbers delineated are at least two years in arrears, which likely means that they have increased.

The current debt focus is on Greece and the (U.S.), where the debt limit debate appears to going down to the final hour. So much is made of the necessity for increasing the statutory limit in order to maintain the U.S. 'AAA' credit rating. We consider that a farce. There's no way, other than the credit rating companies are American companies that the U.S. should even now be rated 'AAA'. Simply raising the debt ceiling another two plus trillion dollars doesn't improve the national debt picture at all.

As for Greece, this is the second time in two years that it has been bailed out by its fellow Euro members and almost certainly there'll be another bailout required in the not too distant future. The same is likely true for Ireland and Portugal and then there are the bigger economies of Spain and Italy, where their debt is also being called into question. Does France manage to avoid the debt spiral or even mighty Germany? These debt bailouts are, for the most part being orchestrated by Germany and France, because it is their banks, holding so much bad debt paper on their books, which might be brought down by a European country's bankruptcy.



Source: Global Finance, Tina Aridas www.gfmag.com

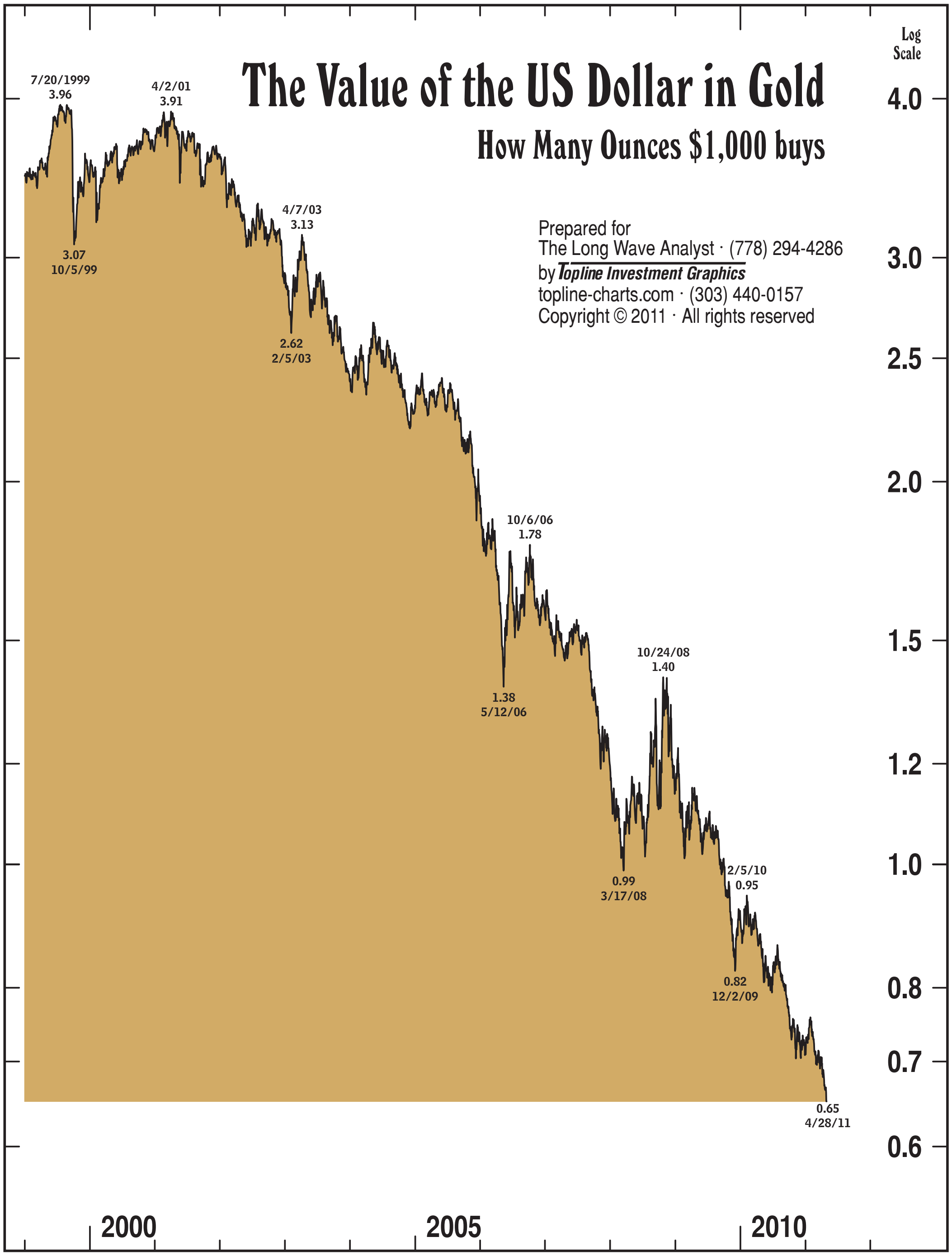
Japan, too, is a debt basket case. The country has been printing copious amounts of Yen to keep the country from falling into an economic depression following the collapse of the Nikkei after 1990.

There you have it, debt, which is the instrument of paper money, is collapsing in almost every industrialized country in the world. Once the collapse is complete it will bring about the failure of paper money.

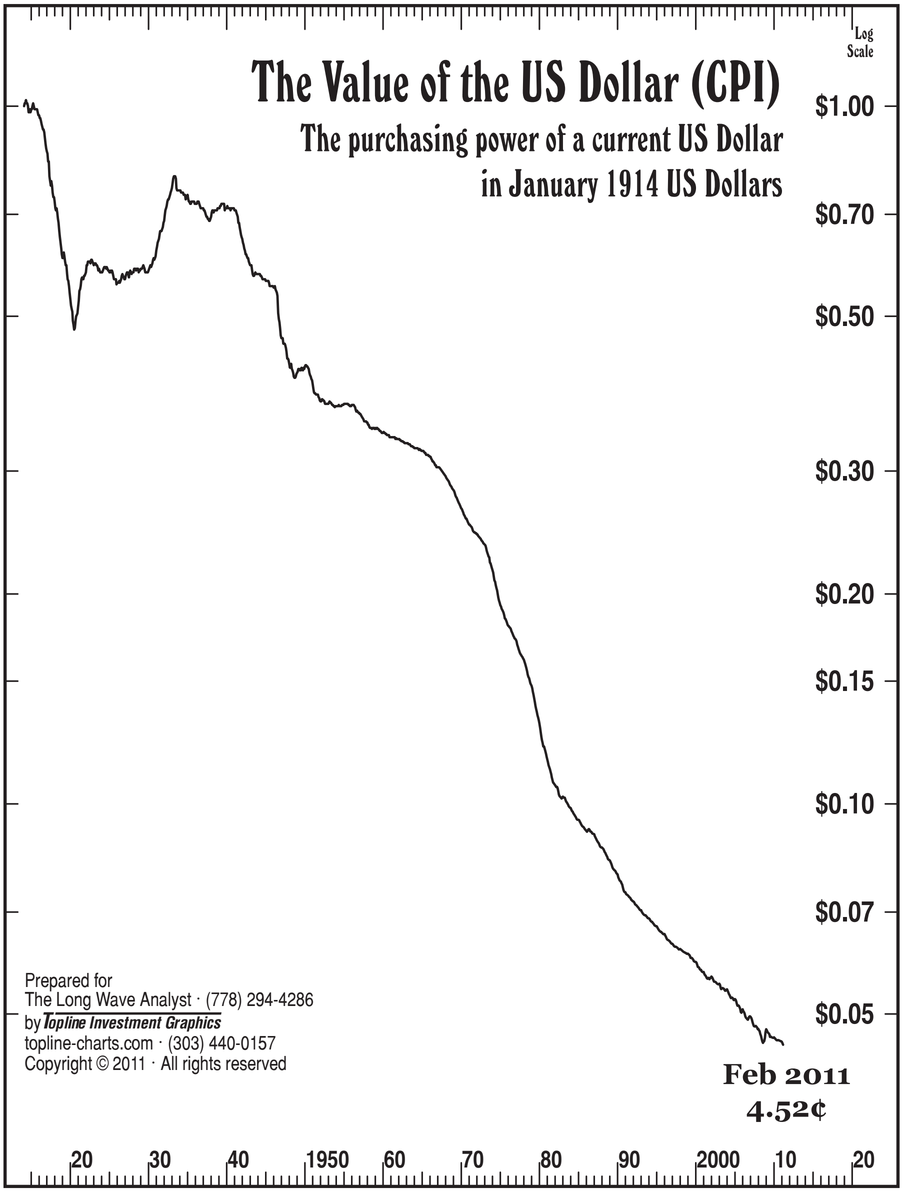
The price of gold is telling us that the end is near. In July 1999, the price of gold reached a low of $252 (U.S.) per ounce and paper assets were all the rage at that time. A secondary low, a double bottom, at $255 (U.S.) per ounce occurred in April 2001. From that point on the gold price has been rising, gathering momentum, in the face of monetary printing presses working overtime all over the world. As I conclude my writing, July 26, 2011, gold is trading at $1,620 (U.S.) per ounce.

On the chart below we can see how much the paper U.S. dollar has been devalued against gold since 1999. In July 1999 $1,000 U.S. could buy almost four (3.96) ounces of gold; as of today (July 26, 2011), $1,000 U.S. will buy just 0.62 ounces of gold. The American dollar since 1999 or even 2001 has depreciated by almost 85% against gold. Let's look at it in another way, in 2001 a $500,000 (U.S.) home would have cost the equivalent of 2,000 ounces of gold, today that $500,000 (U.S.) home could be purchased for only 312.5 ounces of gold. Today, 2000 ounces of gold could purchase six $500,000 (U.S.) homes and still have money left over to buy a $33,000 (U.S.) car for each garage.

Paper money is not governed by the natural law of money. Money must have value, because it is exchanged for something of value. Paper has no value except that decreed by government fiat. "A sound money is the quantity of which cannot be created by the passage of law. It is a money that is not based on a promise to pay. Money is a unique economic good because it neither directly creates wealth nor is consumed when wealth is exchanged. Its vital function is that of a medium of exchange-both now and in the future." The Privateer-Number 683, July 2011 (This is a private newsletter, which I strongly recommend).


The Value of the US Dollar in Gold
How Many Ounces $1,000 buys
Prepared for
The Long Wave Analyst · (778) 294-4286
by Topline Investment Graphics
topline-charts.com · (303) 440-0157
Copyright © 2011 · All rights reserved
Log Scale
4.0
3.0
2.5
2.0
1.5
1.2
1.0
0.8
0.7
0.6
2000
2005
2010
7/20/1999 3.96
3.07 10/5/99
4/2/01 3.91
4/7/03 3.13
2.62 2/5/03
10/6/06 1.78
1.38 5/12/06
10/24/08 1.40
0.99 3/17/08
2/5/10 0.95
0.82 12/2/09
0.65 4/28/11

“A sound money is one that retains its purchasing power over LONG periods of time, periods which stretch well beyond a human lifetime (The British pound tied to gold-1821-1914). A medium of exchange is essential for the division of labour which makes economic prosperity possible because it allows specialization. This specialization leads to the most efficient use of scarce factors of production-including the scarcest factor of all which is time. Money is essential to this process because it can be saved to be used for future exchanges. But this is only true if it has been obtained in exchange for REAL economic goods and services.” Ibid.



Is this the picture of a sound money that has retained its purchasing power? Since the inception of the Federal Reserve at the end of 1913, one U.S. dollar then is worth 4.52 cents (U.S.) today.

Paper money is contrary to the law of nature, which exists throughout the economic and financial domain. It has been devised through man's incredible hubris as lawful money. When the end comes it will be like the tsunami that recently hit Japan. The incredible destruction of this natural force could not be held back by the sea walls that man had built to withstand it. The massive destructive waves caused by the collapse of paper money are rising right in front of us. We must move to high ground or perish in the oncoming onslaught.

The demise of paper money happens because people refuse to accept it as money, because it has lost virtually all of its purchasing power. What happens to the U.S. dollar, for example, if all U.S. creditors refuse to lend the United States any more money and furthermore, decide to sell off all the American debt they already own? Under these circumstances the U.S. dollar, of course, becomes worthless. But then, all the different country currencies are nothing but paper backed by debt. And there isn't one of them that's not going to fail.

If we were to draw a timeline for how this failure plays out, we would say that it starts this year in 2011. Many of you will know that I put great store in the work of the great cycles master W. D. Gann. Mr. Gann never divulged the essence of his cycle work, but one of the things that he did communicate to us was that annual cycles were very important, particularly the twenty-year cycle. I have found, too, that the hundred year cycle is important, probably because it's five twenty-year cycles. (See-'This Is It' to see how accurately we can make predictions based upon these cycles).

Anyway, to get back to why I anticipate that the world monetary system will begin its collapse this year, we go back four twenty year cycles to 1931 and see that was the year in which the world monetary system began to fail. It started in May of that year when a bankrupted Austria abandoned the world gold exchange standard system. The most important event of that year occurred in late September, when Great Britain abandoned the gold monetary system.

The U.S. abandoned the monetary system in 1933, which spelled the conclusion of the gold exchange standard system. So it might be in 2013 that the U.S. dollar loses its world reserve currency status.

In 1914, the combatants in the First World War abandoned the true gold standard system, so it might be in 2014 that the world returns to a monetary system backed by gold.

When they fail because they are essentially credit money systems then credit must fail too. It almost did in 2008. When credit fails the economy ceases to function. What that means is that food doesn't get delivered to grocery stores; petrol isn't transported to the gas stations; even water and natural gas are cut off by the companies responsible for their delivery; the banking system collapses; governments cease to function and anarchy prevails.

Footnotes

1. Gleeson, Janet. Millionaire, The Philanderer, Gambler and Duelist Who Invented Modern France. Simon Schuster, New York, NY, 1999. P. 137
2. Ibid P.138
3. Ibid P. 147-148
4. Ibid P. 182
5. Ibid P. 197
6. Ibid P. 207
7. Ibid P. 221
8. Ibid P. 225
9. White, Andrew Dickson. Fiat Money Inflation in France. The Foundation for Economic Education Inc, Irvington-on-Hudson, New York 1959 (originally published 1876). P. 26

10. Ibid P.32-33
11. Ibid P. 45
12. Ibid P. 53
13. Ibid P. 53
14. Ibid P. 59
15. Ibid P. 110-111

Written By: Ian Gordon