Introduction / Unclassified / Further Inquiry

A word on systems dynamics, applied mathematics, complexity, Hayek, icy roads

Video 1: CNBC Eamon Javers
http://www.cnbc.com/id/15840232/?video=1653093678&play=1
(for 1 minute 50 seconds)

The Sovereign Debt Crisis and the Currency Wars (20 mins)

The Sovereign Debt crisis is a combination of:

- Runaway deficit spending
- Added on fiscal stimulus
- Substitution of public debt for private debt; bailouts
  (GM, Irish banks, Fannie Mae, AIG, Goldman, etc.)

Sovereign debt cannot be repaid in real terms

- Traditional formula was higher growth and/or higher taxes
- But growth now in deflationary collapse and taxes hurt growth

Problem with Euro

- Failed to distinguish the currency from the bond issuers
Two different things: Corp v. Treasury in U.S.

Germany benefits from unified, weak euro but has tiger by the tail

**Default inevitable – only issues are how**

Outright default – the deflationary default

Confiscatory taxation – the fiscal default

Hyperinflation – the inflationary default

Some combination of the above

It’s all one crisis – Dubai, Greece, Ireland, Portugal, etc.

**Currency Wars happen when growth stagnates**

When pie is expanding, people don’t fight over shares

When pie is shrinking, people do fight over crumbs

\[ \text{GDP} = C + I + G + (X – M) \]

**Slide 4: \( \text{GDP}=C+I+G+(X-M) \)**

When \((X – M)\) is the only source of growth, currency wars begin

All advantage is temporary

Escalation is inevitable

Escalation includes:

- Capital controls
- Protectionism
- Trade Wars
- Gold
- Shooting wars

Political Backlash has begun: Iceland v. Ireland

**Video 2: European Parliament**

http://www.youtube.com/watch?v=Fyq7WRrGPGq&feature=player_embedded

(Entire clip)

**What’s in your Wallet? – Quantitative Easing, Inflation & Deflation (20 mins)**

**Slide 5: What’s in Your Wallet?**
The conundrum of inflation v. deflation and the illusion of price stability

The “Quantum of Loss” theory

Total losses are given based on misallocated capital & returns

Can be shifted in time

Can be shifted by identity of losers (banks v. taxpayers)

The “V” versus the “L”

Slide 6: Dynamics of the Housing Bubble

Americans have tolerance for pain and appetitive for growth

Americans have low tolerance for stagnation, unfairness

Fed wants inflation

Slide 7: When is an Asset not a Liability?

Reduces real value of debt

Supports asset prices

Creates negative real interest rates

But the Fed is not getting inflation

Being exported to China via exchange rate

Pull of intrinsic deflation is too strong

Velocity is plummeting (MV = pY)

Slide 8: MV=pY

Slide 9: Velocity of Money

Danger is Fed will do “whatever it takes” to the point of instability

Slide 10: Growth in Monetary Aggregates

Transparency, social media, mobilization are new phenomena

Dynamic model of dollar collapse

Slide 11: Dynamic Model of Dollar Collapse

Slide 12: Average Maturity of Debt – The Short Fuse
China, Russia and the Rise of State Capitalism (20 mins)

Slide 13: Rise of State Capitalism

**Washington Consensus v. Beijing Consensus**

**Elements of Classical 17th-19th Century Mercantilism are:**

- Principal forms of wealth are tangible, i.e. land, commodities, gold
- Acquisition of wealth internationally is predominately a zero-sum game
- Sound policy includes favoring domestic industry, exclusive trading blocs, discrimination and protectionism
- Export subsidies, import tariffs, exclusivity in trading relations are normative
- Trade is the continuation of war by other means

**Elements of the Globalized Washington Consensus are:**

- Free Trade
- Freely Convertible Currencies
- Freely Floating Exchange Rates
- Free Flows of Capital, interest, dividends
- Few Restrictions of Foreign Direct Investment
- Mobility of Labor
- Reciprocity and non-discrimination in overseas expansion of global companies
- Protection of Intellectual Property, patents, trade names, trademarks, etc.
- Protection of Creditors
- Reasonable Anti-Trust enforcement
- Non-protectionism, low or no tariffs, most favored nation treatment
- General adherence to the Rule of Law

**Elements of the Beijing Consensus are:**
Wealth creation may not be strictly zero-sum but may be increased through sub-optimal policies.

Intangible and intellectual property may be a form of wealth but may also be amenable to mercantilist approaches.

Mercantilist policy may be applied selectively rather than exclusively and still be advantageous under certain conditions.

Evidence is large and growing the Russia and China are pursuing Neomercantilism

- Differentiated taxation of rare earth exports by China
- Captive mining industries in Russia and China
- Large and growing role of the state sector – Gazprom, Sinopec, CIC
- The German-Russian Axis, Nordstream
- The concept of Greater China

Conclusions

These problems are not residuals or artifacts but are new and expanding.

Neomercantilism rational in a world of diminishing marginal returns to complexity.

Victory in a negative sum game is still victory. I lose, you lose more, I win.

We are not helpless – The United States as Gold Superpower (20 mins)

Now for some good news

Brief history of gold in U.S. monetary policy

- Destruction of paper currency / hyperinflationary episodes
- Revolutionary War
  - Hamilton backed currency on gold/silver standard
- Civil War
  - Grant deflated, returned to gold standard
- 1876-1914 Hey Day of Sound Money
  - Real growth with "good" deflation
- 1922-1936 Rise and Fall of the Gold Exchange Standard
1944-1971 Rise and Fall of Bretton Woods

Survey of Gold Powers today – U.S. as the “Saudi Arabia of Gold”

Conclusions

Gold standard associated with growth and rising living standards

In deflationary crisis, President will devalue against gold
  FDR in 1933-1934
  Nixon Shock of 1971
  Bipartisan

Bernanke fighting inflation / seeking devaluation today
  Will fail because currency wars always fail

Dangers are: Deflationary collapse, protectionism, trade war, etc.

Solution is: Reflation via gold and stability via gold standard

Question: Get there with planning or with chaos?

Policy and Prospects (15 mins)

No way out of the debt crisis

Confusion, fear and anxiety on the increase

Loss of trust in elites and elite solutions

Dynamic instability of trying more and more of the same

Political backlash, finger pointing, “too much” v. “not enough”

No dry powder, financial system not robust to war, natural disaster, another financial collapse
In extremis, secure the gold under IEEPA / Offer Europe Treasury Receipts
Revert to global gold standard managed by U.S.
Develop contingencies now
Operation Unified Quest 2011

Slide 25: Operation Unified Quest 2011

Video 3: Rollover (5 mins)
http://www.youtube.com/watch?v=m1aQ-XGWors&feature=related
Begin at 1:35 and run until 5:30 (about 4 minutes)

Slide 26: Thank you / Contact Information

Questions (25 mins)