

The system has passed the point of no return

by John Hoefle

We are living in an extraordinary time, a time which presents both grave dangers and great opportunities. The choice facing humanity is stark: a new Renaissance, in which creativity and reason flourish; or, a new Dark Age, in which the law of the jungle reigns, an eat-or-be-eaten world in which most of humanity is on Prince Philip's menu.

The global financial system is collapsing with breathtaking speed, and the party is just beginning. We've moved from an era in which mere companies are going under, to an era in which entire nations are collapsing. The international institutions which seemed so powerful just a few months ago, are now being swept aside by tidal waves of losses. The International Monetary Fund (IMF), which once struck fear into the hearts of nations, has proved powerless to stop the onrushing crisis, its poison no longer sufficient to contain the situation. The very system itself, is crumbling.

In May 1997, the financial oligarchy launched an all-out financial assault on the nations of Southeast Asia, beginning with Thailand (Figure 1). Leading the assault, was the British

Empire's drug-pushing financial warfare specialist, George Soros; behind him, was arrayed the full might of the oligarchy's banks and investment houses.

The main goal of this attack was to destabilize the continent, and prevent the emergence of a regional bloc committed to implementing the Eurasian Land-Bridge development program. A secondary goal, was to steal billions of dollars.

In July, Thailand fell, agreeing to allow its currency, the baht, to rise and fall at the whim of the speculators, and begging for help from the IMF. In rapid succession, the nations of the Philippines, Malaysia, and Indonesia were hit by similar attacks. By December, the IMF had promised—but only partially delivered—"bailout" packages to these nations, and to South Korea.

With typical oligarchic arrogance, the Asian nations were blamed for what was termed an "Asian crisis," or the "Asian contagion." But the Asian nations were responsible, only to the extent that they had allowed themselves to be seduced by the sirens of the free market, which made them vulnerable in the first place.

The nature of the present financial system, is that it must loot in order to survive, and it must grow, or it collapses (Figure 2). It is a giant pyramid scheme, which must suck in ever-increasing amounts of money. So, the oligarchy deploys its banks, and creatures like George Soros, to go out and steal money for the bubble.

But, it is not only Asia. The entire world is under attack. Most of Africa has already been destroyed, Russia is in convulsions, and Ibero-America is also melting down (Figure 3).

In the early stages of this crisis, money that had been invested in Asia, or would have been invested in Asia, fled to what was perceived as safe havens: Europe and the United

FIGURE 1
Asian stocks collapse in wake of speculative assault

(May 30, 1997 = 1.0)



FIGURE 2
A typical collapse function

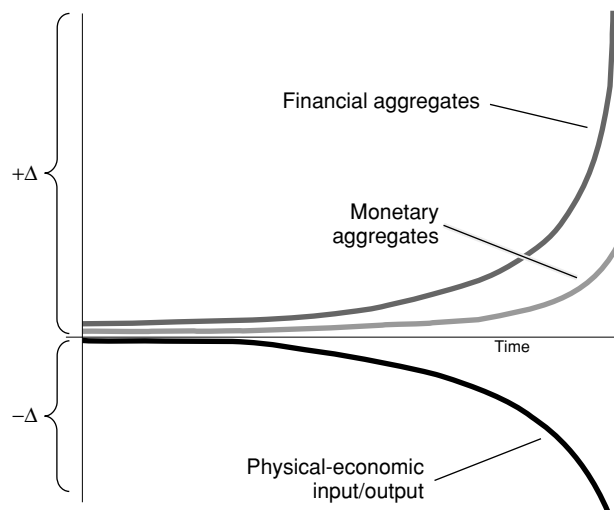


FIGURE 3
Ibero-American stocks plummet

(May 30, 1997 = 1.0)



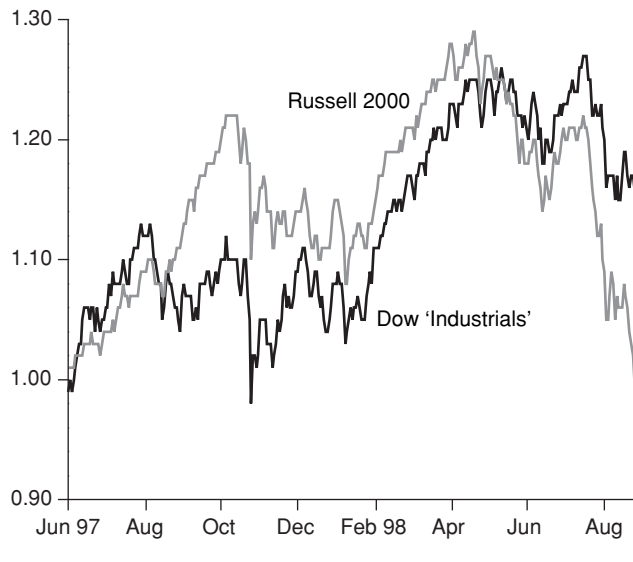
FIGURE 4
European stocks are no longer a safe-haven

(May 30, 1997 = 1.0)



FIGURE 5
U.S. markets also collapse

(May 30, 1997 = 1.0)



States. The major European stock indices soared to record heights, as did the Dow. But that changed in mid-July. Now, all the markets are dropping (**Figure 4**).

In the United States, most eyes are focussed—maybe even fixated—on the Dow. But, as fast as the Dow is falling, the

broader U.S. stock market is falling even faster (**Figure 5**). The “Down” Jones Industrial Average, after all, consists of just 30 stocks, and is relatively easy to manipulate—it’s not even an industrial measurement, as it includes such decidedly non-industrial companies as McDonalds, American Express, Disney, and Wal-Mart. It also includes two of the biggest derivatives players in the world, J.P. Morgan and Travelers, which between them have nearly \$10 trillion in derivatives. The Russell 2000, on the other hand, excludes the blue chips, and measures the smaller companies.

But the losses so far, are just the tip of the iceberg.

It is claimed, repeatedly, that the United States’ economy is in no danger, because our “economic fundamentals are sound.” We may suffer some fallout from the “Asian contagion,” or the “Russian crisis,” or the “Ibero-American crisis,” but we’ll be okay, because our “fundamentals are sound.”

Many people want to believe this. After all, the computer models all show that “historically”—even as far back in pre-history as 1980—the stock market always goes up. When the occasional blip occurs, it’s just an opportunity to buy. “Everybody knows that. We’re all with the smart money now, we’re all above average.”

This delusion, of course, is fostered by the oligarchs, whose main goal is to convince you to keep your money in the market, so they can pull theirs out.

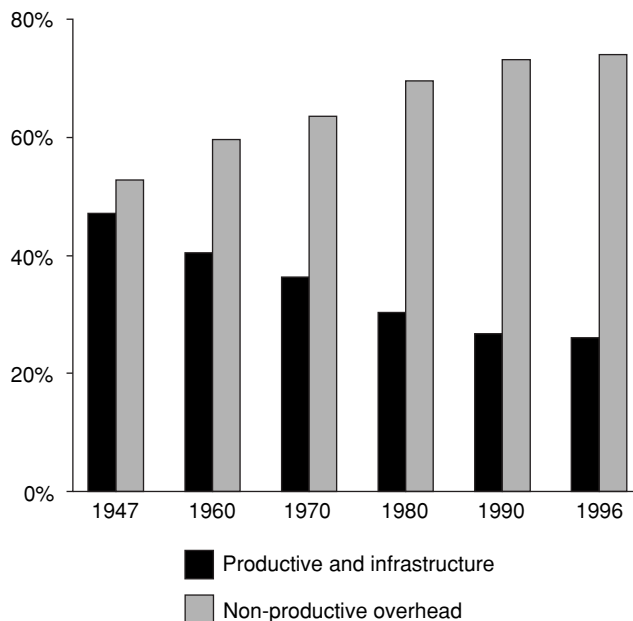
Physical economy a disaster

The truth is, that fundamentally, our economy is a disaster. Our studies show that the U.S. physical economy has declined by some 50% since 1967, or about 2% a year, and the rate of that decline is accelerating. We get that not by measuring

FIGURE 6

Productive compared to non-productive labor force

(percent of total labor force)



prices, but by measuring a market basket of essential goods on a per-capita, per-household, and per-square-kilometer basis. When you look at the economy in terms of physical production and the services needed to support that production, you get an accurate picture. The money figures are worthless.

At the end of 1967, the Dow stood at 900 points. Since then, it has risen more than ninefold, while the physical economy has dropped by half. No wonder Federal Reserve Board Chairman Alan Greenspan keeps his money in Treasury securities.

Coming out of World War II, nearly half of the U.S. labor force was involved in the productive side of the economy: the production and distribution of goods, and provision of essential services, including research, health care, and education (Figure 6). Over the years, while the number of people employed has risen significantly, the number of production workers has remained relatively constant, meaning that virtually all of the net job gain has been in the overhead category. Today, only one in four workers is employed in the productive sector. Adding overhead jobs — hamburger flippers, Internet jockeys, stockbrokers, and the like — does not increase productivity. Rather, it increases overhead, and adds to the burden the productive sector must support.

The condition of the productive sector will get even worse, as entire sections of the world economy collapse. The effect can already be seen in the decline of U.S. goods exports, which is dramatically increasing the U.S. trade deficit (Figures 7 and 8).

FIGURE 7

Fall in U.S. goods exports parallels world economic collapse

(billions \$)

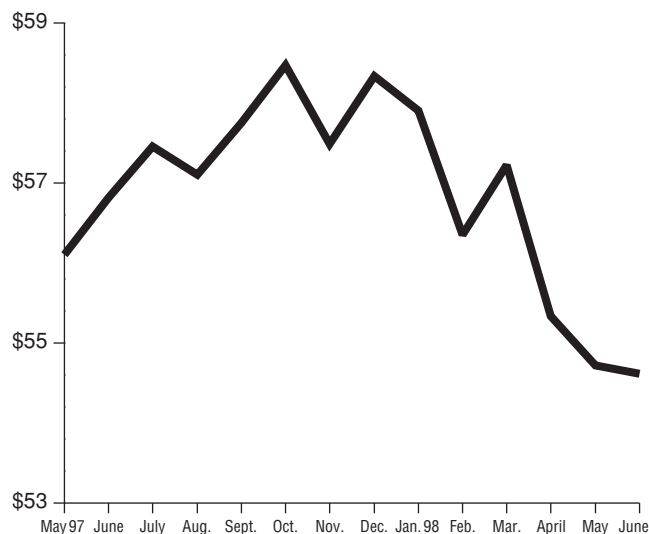
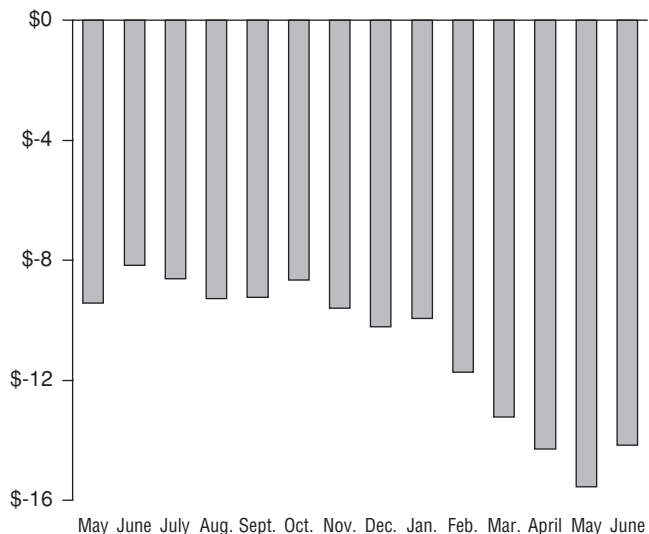


FIGURE 8

Growth in U.S. trade deficit fuelled by decline in exports, 1997-98

(billions \$)

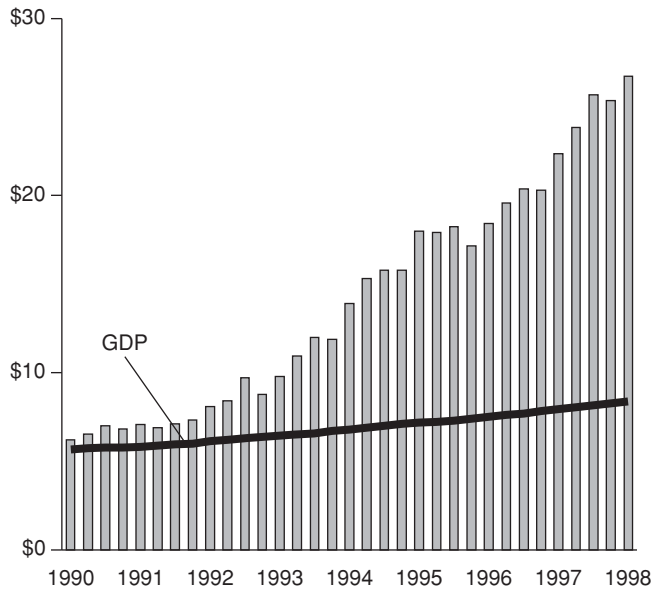


One place where the United States does have growth, is in the derivatives market. Gross Domestic Product is a poor measure of economic growth, because some two-thirds of GDP is overhead, but the growth in derivatives is far outrun-

FIGURE 9

U.S. bank derivatives vs. Gross Domestic Product

(trillions \$)



ing even that bloated statistic. Overall, the United States has some \$40 trillion in derivatives, of which the commercial banks hold \$27 trillion (Figure 9).

When the derivatives market blows up, the United States will be sitting squarely at ground zero (Figure 10). Overall, the United States has about one-third of the global derivatives exposure: Our banks dominate the over-the-counter market, and the United States accounts for nearly half of the trading on the world’s derivatives exchanges.

The result are exposures so large, that tiny drops in the derivatives markets would be enough to blow them out of the water. Just seven U.S. banks have \$25 trillion in derivatives exposure, backed up by just \$114 billion in equity capital (Figure 11). A loss equivalent to just 0.2% of its derivatives portfolio would wipe out all of Morgan’s equity, bankrupting the bank, and a loss of 1.2% would wipe out any of the top seven.

Figure 12 shows what it looks like, when you compare Morgan’s equity and assets to its derivatives holdings. They call this risk management.

The bankers’ response

You can see why bankers are getting hysterical. Some of them are beginning to figure out that, to quote Chicken Little, “The sky is falling.” But, rather than face reality, they are determined to try to save themselves, by saving their system.

Take Alan Greenspan, for example.

FIGURE 10

U.S. at ground zero of derivatives explosion

(share of global derivatives exposure)

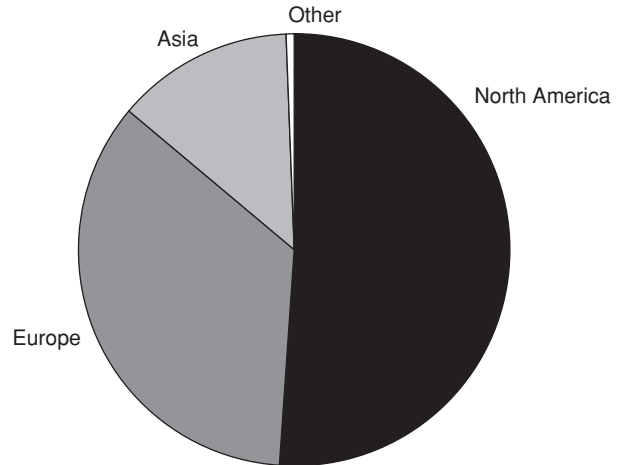
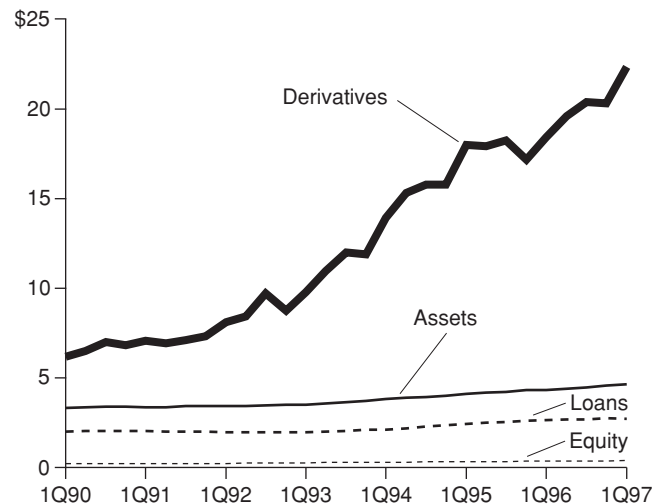


FIGURE 11

U.S. banks addicted to derivatives: derivatives versus assets, loans, and equity

(trillions \$)



We do not as yet fully understand the new system’s dynamics. . . . We have tried to confront the current crisis with the institutions and techniques we have.

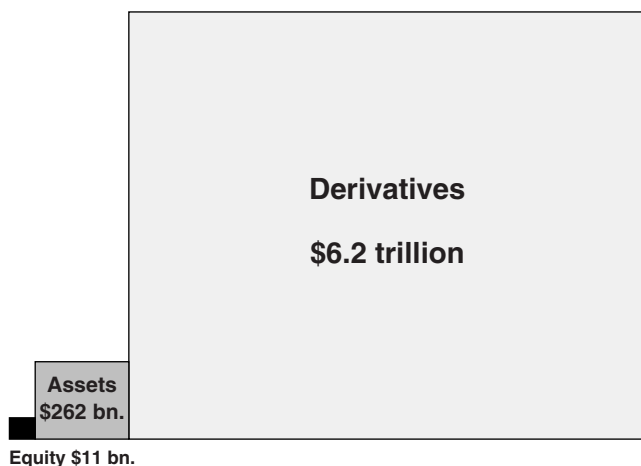
—Fed Chairman Alan Greenspan, to Congress, May 1998

Greenspan doesn’t understand that the rules of the game have changed, and he is foolishly prescribing another dose

FIGURE 12

J.P. Morgan & Co.'s derivatives, assets, and equity compared

(as of Dec. 31, 1997)



of the same medicine which is killing his system.

Or, here is another comment from the Fed, from a “senior Fed official,” to *American Banker* magazine in August 1998: “The problem with models is that they reflect your best guess. . . . It is out of the parameters of what the banks were expecting.”

The computer models, which project that the economy will continue to do what it has been doing, cannot account for the discontinuity which has occurred. Reality is outside the parameters. Who could have known?

Then, there is the Aug. 24 *Wall Street Journal*:

The financial firestorm that has been scorching economies around the globe is intensifying into one of the world’s worst—and most baffling—currency crises since the system of fixed exchange rates crumbled a quarter of a century ago. . . . What makes the crisis so unnerving is that there is no clear solution in sight—no financial firebreak that governments or international financial institutions can construct to slow the spread.

This is precisely where sticking with the current axioms must inevitably lead. The system can’t be saved, and the attempts to save it with the current “institutions and techniques,” are merely fanning the flames of the firestorm.

Reverse leverage is beginning to kick in, and that spells disaster for the markets. The bubble was built on borrowed money, and derivatives bets backed by borrowed money. That means faster growth on the way up, and even faster collapse on the way down. The speculators are having to

sell assets in a falling market in order to cover their debts, driving the market even lower.

The derivatives danger

Where reverse leverage will prove most deadly, however, is in the derivatives market, which is so interlocked that a big default in one area, could set off a chain reaction of failures which would race around the world in hours. This would be the proverbial “big one.”

The alarm bells are already sounding over derivatives losses in Asia and Russia.

In Russia, Western banks and other institutions bought large amounts of government-backed bonds, called GKO’s; then, to protect themselves against a devaluation of the ruble, they bought derivatives contracts which would pay off, if the ruble collapsed. The ruble did collapse, hitting the investors with big losses. But now, thanks to the Russian meltdown and the freeze on certain currency transactions, they find that their prospects of collecting on as much as \$100 billion in currency derivatives has been called into serious doubt.

The imposition of currency controls by Malaysia, has called into question the collectibility of currency derivatives based upon Malaysia’s currency, the ringgit.

In Japan, where the government has insisted on defending, rather than correcting trillions of dollars of fictitious real estate values and unpayable debt, Finance Minister Kiichi Miyazawa warned Parliament on Aug. 25 that there is a “danger of default” on some \$350 billion in derivatives contracts held by the bankrupt Long-Term Credit Bank. With overall derivatives exposure in the range of \$10-\$15 trillion, a derivatives crisis in Japan would immediately mean a derivatives crisis worldwide.

The magnitude of losses already incurred in the derivatives market is not known, but judging by the losses now being reported by banks, securities firms, and the hedge funds, the losses are already in the billions of dollars. As J.P. Morgan and the other big derivatives players know, the margin between survival and disintegration, is a very thin one indeed. When that line is crossed, the entire global financial and monetary system will simply disintegrate, in a chain-reaction. Poof. No more system.

Which brings us to Prince Philip and his Chaos faction. They want the system to disintegrate, and they plan to use that collapse to wipe out the nation-states and take the world back to feudalism. Their plan is simple: to wind up on top of whatever pile of rubble is left after the crash. They have been consolidating their control over precious metals, strategic minerals, energy sources, food supplies, communications networks, and other essential industries over the last few years, in order to have a stranglehold after the system disintegrates. Their motto is, “If you need it to live, we want to own it. Then you either pay our price, or die.” But, even if you pay, you might just die anyway, as civilization gives way to a new Dark Age.