

The Impending Global Liquidity Crisis

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Stock markets across the world have been skyrocketing lately. In fact, Forbes reported on Tuesday that: "all 22 of the developed-world markets tracked by Morgan Stanley Capital International are in positive territory year-to-date. ...Emerging markets are looking just as flush. Of the 29 emerging market countries that MSCI tracks, only four--Argentina, Sri Lanka, Russia and Venezuela--are in negative territory."

Yahooo! The markets are soaring and we've entered a new "globalized" Age of Prosperity.

Sounds great doesn't it?

There's just one little problem; the Commerce Department announced yesterday that that GDP in the first quarter was revised downward to a measly .6%.

Are you kidding me? Economic growth is underwater and yet the stock market is still flying-high? What gives?

It's easy. The markets are just responding to the growth in the money supply which is in double-digits just about everywhere around the world. When there are more dollars chasing the same number of assets---stocks go up. It's just that simple. What we're seeing isn't the result of investor confidence or industrial output. Heck no! Stocks are rising because our \$800 billion current account deficit is recycling into the stock market. What we are really seeing is the first signs of inflation---galloping inflation which will soon spill over into the broader economy.

If we eliminate the "frothy" exuberance of America's trade deficit, then the stock market would be sucking air through a tube right now. And, you can bet that as soon as our foreign creditors wise-up and start raising interest rates the Dow Jones will quickly become the Dow Doldrums and the economy will nosedive into a 1929-type Depression.

Does that sound overly pessimistic?

At present, the "don't worry, be happy" crowd still thinks the good times will roll on forever. They don't see that the US consumer is running out of gas and won't be able to sustain his gluttonous spending spree much longer. He's already stopped siphoning the equity out of his home (\$600 billion last year) and now he's has started to max-out his credit cards. (Credit card debt increased 9.2% last month alone!) Now, US consumers are facing a blizzard of bad economic news---rising prices at the gas pump, a 6.7% increase in food prices, and a sickly dollar that keeps losing ground on the currency exchange. (Kuwait is the latest country to announce they will be dumping the dollar for a basket of currencies)

Currently, the US gobbles up two-thirds of the world's credit each year with no conceivable way of paying it back. That won't last much longer. Central banks around the world are increasingly hesitant to accept are our flaccid greenbacks and the Chinese are the only ones who are still buying

our Treasuries. That's mainly because it gives them power over political decision-making in Washington. The truth is the Chinese are planning to send the US into receivership and take over as the world's bank. With dollar-backed reserves of \$1.3 trillion, their plan appears to be going "full-steam ahead".

The bottom line is that we are buried beneath a \$9 trillion mountain of debt and there's no way to dig out. If there's a break in the liquidity-flows to our stock market---stocks will crash, unemployment will soar, and we'll be pulled into a deflationary downspin.

Economic soothsayer Elaine Supkis puts it like this:

"World wealth isn't growing, world DEBTS are growing and the place they are growing the fastest is the US which is the sole terminus of world trade at this point. The biggest growth industry today is selling debt instruments. The entire existence of hedge funds, for example, is to funnel profits from uneven trade with the US back into the US via dumping debts onto the backs of any corporations that can run up more debts!" (http://elainemeinelsupkis.typepad.com/money_matters/)

Get it? It's all just recycled dollars---debt piled on debt piled on debt piled on debt-- repeat ad infinitum. America's equities portfolio = 1% assets, 99% pure helium.

This may explain why Treasury Secretary Hank Paulson has been frantically beating the bushes for "foreign investment" to keep the stock market bubble afloat. He has no interest in rebuilding America's industries or increasing our competitiveness. No way. What he's looking for is a quick liquidity-fix to keep the over-bloated stock market sputtering along while more wealth is shifted to mega-rich corporations. In fact, no one in Washington is even talking about renovating America's battered manufacturing sector. What do they care if we turn into a nation of busboys and bed-pan cleaners? They're just hanging around long enough to sell off whatever's left of our national assets then it's "off to new markets in the Far East".

And, they are doing a great job, too! The United States is handing over 1.5% of its national wealth every year to foreign investors while the American public continues to snooze away.

We're having a giant garage sale and everything must go---roads, water, mineral rights, natural gas etc. We're getting "picked clean" and no one seems to care.

The boys in Washington and Wall Street don't work for you and me. They're destroying the currency and selling everything that isn't bolted to the floor. Then, they'll pack-off to Asia and Europe where they can begin the scavenging-cycle all over again.

How bad will it get in the USA?

Consider these comments from Princeton University economist Alan Blinder, who recently attended the business summit at Davos, Switzerland: (summarized by Rep. Ron Paul)

"Word has it that there may be plans yet again to "outsource" highly skilled American jobs to other countries. Approximately 40-million American jobs could be at stake and yet US workers have not been told or consulted about it, until now. Just to put the number of 40 million into perspective, that is more than twice the amount of people that are employed in manufacturing. (According to Alan Blinder) The 'choice' jobs of skilled Americans could be lost and given to foreign countries within the next decade or two."

40 million high-paying US jobs will be outsourced to lower-wage countries within the decade?!?

This is a blueprint for the economic destruction of America!

Maybe this will finally convince the dozy American public that the corporatists who run Washington are a disloyal gaggle of traitorous swine. "Globalization" is public relations swindle designed to steal jobs, plunder the economy, and shift wealth to ruling elites.

The name of the game now is to keep the stock market flying-high for as long as possible while the transfer of wealth continues unabated. That means the hucksters on Wall Street will have to devise even better scams for expanding debt--increasing margin limits, escalating derivatives trading, loosening accounting standards, inflating the booming hedge fund industry, and--the new darling of Wall Street--increasing the mega-mergers, the biggest swindle of all.

These over-leveraged mergers create boatloads of new credit, but add nothing to GDP. They reflect the basic disconnect between the stock market and the real economy. May is on track to be the biggest month for global mergers ever recorded. Marketwatch reports:

"For the year to date, companies have announced at least \$2.2 trillion in deals worldwide. Of these, US companies have engaged in \$830 billion".

But look at the figures---Do they sound familiar?

Once again, the insightful Elaine Supkis makes this observation:

"Note that the 'deals' roughly equal our trade deficit. This isn't accidental. They are one and the same! And I will never see this fact stated so baldly in our media. No one dares say it in public."

Wow; she's right. Our trade deficit is being concealed by these gargantuan mega-deals in the markets.

And there's something else we need consider about these mergers; they're not producing growth in the economy. In fact, GDP keeps falling while stocks keep going higher.

Why?

Because the mergers do not increase productivity; they're an indication of "asset inflation". As Thorsten Polleit says, "the government-controlled paper money systems have decoupled credit expansion from the from the economy's productive capacities." The link between the stock market and GDP has been broken by inflation.

Henry C K Liu explains it like this in his article "Liquidity Boom and Looming Crisis" in the Asia Times:

"The five-year global growth boom and four-year secular bull market may simple run out of steam, or become oversaturated by too many late-coming imitators entering a very specialized and exotic market of high-risk, high-leverage arbitrage. The liquidity boom has been delivering strong growth through asset inflation (property, credit spreads, commodities, and emerging-market stocks) WITHOUT ADDING COMMENSURATE SUBSTANTIVE EXPANSION OF THE REAL ECONOMY. Unlike real physical assets, virtual financial mirages that arise out of thin air can evaporate again into thin air without warning. As inflation picks up, the liquidity boom and asset inflation will draw to

a close, leaving a hollowed economy devoid of substance. ...A global financial crisis is inevitable”.

Liu’s right. There’s no “expansion in the real economy”—no increase in output; no boost in GDP. It’s all recycled credit which will “evaporate” at the first sign of trouble.

Greenspan’s low interest rates and currency deregulation have set us up for “global liquidity crisis”.

The basic problem is that credit growth has been outpacing GDP for some time now. That means that debt has been building up faster than the rate of growth in the economy. Eventually those imbalances will have to work themselves out by way of a steep recession or perhaps another Great Depression. There’s a price to pay for low interest rates and, inevitably, we will end up paying it.

Thorsten Polleit of the Mises Institute explains it like this in his article “The Dark Side of the Credit Boom”:

“Today's government-controlled paper-money systems have decoupled credit expansion from the economies' productive capacities: "circulation credit" feeds a "credit boom" that is doomed to end in severe economic, social and political crisis. Austrian economists of the Mises Institute fear that the collapse of the credit boom will lead to the destruction of the currency through a deliberate policy of (hyper-)inflation, destroying the free-market order.”

“Destruction of the currency”; is that too strong?

No. In fact, the United Nations issued this gloomy statement just last week:

“The United States dollar is facing IMMINENT COLLAPSE in the face of an unsustainable debt”. America’s current account deficit is now a matter of international concern.

Polleit says that “the increase in debt-to-GDP ratioscan actually be observed in all major currency areas, not only in the United States”. This is true. Most of the industrial countries in the world have increased their money supplies to dangerous levels to avoid strengthening against the dollar. It is a prescription for disaster.

If the Fed chooses to lower interest rates now; (to ease the slumping housing market) they will only aggravate “existing disequilibria”. In fact lowering of interest rates will only perpetuate “the fateful expansion of circulation credit that must end in a collapse of the monetary system”.

So, why would the Fed engage in such reckless behavior when it violates fundamental laws of economics? According to Polleit, “the ongoing lowering of interest rates and the accompanying rise in circulation credit and debt-to-GDP ratios — the characteristic features of today's state-controlled paper-money systems — is driven by a deep-seated anti-capitalist ideology.”

This is also true. The serial “bubble-makers” at the Federal Reserve secretly hate the free market system; that’s why they are engaged in plutocratic social engineering. They're using interest rates as a means for shifting wealth from one class to another and creating a centrally-controlled economy. Their actions are essentially anti-free market and “anti-capitalist” as Polleit says. We can see this trend even more clearly in US foreign policy where the pretense of “free markets” has been abandoned altogether and America is securing its resources with gunboats and missiles rather than with a checkbook.

The current credit bubble is bigger than anything we’ve ever seen before. For example “The total

market volume of credit derivatives outstanding was an estimated US \$20.2 trillion in 2006, amounting to around 1.5 times annual nominal US GDP....The market is expected to grow further to US\$33.1 trillion until 2008. In fact, the credit derivative market has become the biggest market segment of the international banking business already. The problem, however, is that the “credit derivative markets have emerged on the back of a government-controlled credit and money supply system. And as the latter is assumed to be crisis prone, credit derivative markets might be seen as a multiplier of the crisis potential inherent in today's monetary system”.

In other words, the whole \$20 trillion derivative's market is at risk because it is built on a shaky foundation of hyper-inflated currency. Once again, if money supply exceeds GDP there'll eventually be a day of reckoning. We expect that derivatives and hedge funds will get hammered once the huge imbalances begin rumble through the markets.

So, what should we be looking for now?

Any break in the liquidity chain will send markets into downward spiral. The likely catalyst for such a crash could be contagion from the housing bubble creeping into the stock market, a sudden downturn in the Shanghai stock market, (which is up nearly 300% in just 2 years) or an increase in Japan's interest rates. Any one of these could potentially trigger a massive sell-off on Wall Street.

Today's stock market needs a steady flow of cheap capital to stay afloat. That's why Paulson is desperately looking for new investors. But there's a basic problem which the markets cannot escape. Inflation is surfacing in all the countries where the stock markets are soaring because of their increases in the money supply. When the central banks are finally forced to raise interest rates; money will tighten up, it'll be harder for creditors to make their payments or for banks to issue additional loans. As credit dries up more people will default on their loans, demand will drop off for consumer goods, prices will fall, and we will go into deep recession.

Once this process begins, speculators will be forced to abandon their positions, liquidity will continue to evaporate and the market will go into freefall.

Markets are self-correcting. Eventually the overleveraged debt-instruments, which pushed the Dow to historic highs, will be expelled from the system, but not without considerable pain for everyone involved.

Here's an excerpt from Paul Lamont's excellent article “Credit Collapse—May 10” which provides a compelling description of what happens a credit bubble begins to unwind:

“On May 10, 1837, the banks of New York suspended gold and silver payments for their notes. Fear of a bank run spread throughout the United States. The young country fell into a 7 year depression. How could two decades of prosperity end so suddenly? According to *America: A Narrative History*: “monetary inflation had fueled an era of speculation in real estate, canals, and railroad stocks.” Cracks in the dam were visible much earlier, as the stock market peaked in inflation-adjusted value three years prior. According to Rolf Nef, debt levels in the private sector rose to 150% of GDP. In late 1836, the Bank of England concerned with inflation raised interest rates. As rates rose in England, credit tightened, and U.S. asset prices began to fall.

On May 10, investors panicked and scrambled for cash. “By the fall of 1837 one third of the work force was jobless, and those still fortunate to have jobs saw their wages fall 30-50% within 2 years. At the same time, prices for food and clothing soared.”

We can expect a similar scenario in the very near future. When interest rates are kept below the rate of inflation for an extended period of time; enormous equity bubbles arise and threaten the entire system. The stock market is undergoing a period of asset inflation. It has broken free from the real economy and is headed for a crash. As Edward Chancellor, author of "Devil Take the Hindmost: A History of Financial Speculation" says: "The growth of credit has created an illusory prosperity while producing profound imbalances" in the American economy....At some point the system will have to adjust "to face a new reality. The process of adjustment is likely to be painful. It may well end in either an extraordinary deflation...or an extraordinary inflation."

Get ready. The credit boom is coming to an end.

<http://www.informationclearinghouse.info/article17821.htm>

Cleaves Alternative News. <http://cleaves.lingama.net/news/story-532.html>