

We Are Driven - Taken for the Ride of Our Life March 27, 2009

Doug Wakefield with Ben Hill

Over the last few weeks, the very bearish technical readings in daily sentiment have reversed. A few days ago, the US Census Bureau reported that, after sinking to the lowest level on record in January, sales of newly constructed homes rose unexpectedly in February, rebounding nearly 5%. The Commerce Department reported that durable orders jumped 3.4%. Clearly, if these numbers are not revised, which is increasingly frequent with government stats lately, they are positive signs for the beginning of a recovery. The day they were released, the Dow moved up more than 200 points its first hour of trading, and since March 9th we've seen a rally of almost 1400 points. Why be bearish now? Why not jump on board?

While the current rally in the Dow Jones Industrial Average – the most visible market to the average American – has caused everyone to breathe a collective sigh of relief, the underpinnings of the rally leave us questioning its long-term sustainability.

First, let's examine the Dow on Wednesday, March 18th, 2009.



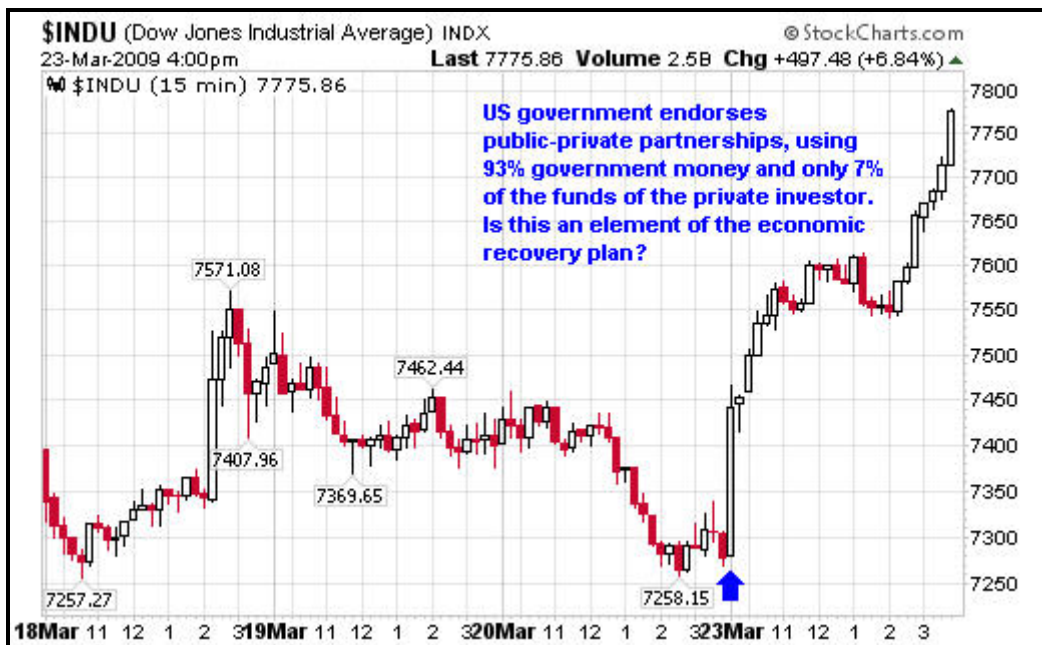
No rocket science here. On this day, Bernanke simply announced that the Fed would hand out fistfuls of dollars. On that day a CNN Money article titled, [Fed Buying \\$300 Billion in Treasuries](#), states:

“The Federal Reserve announced Wednesday it would buy \$300 billion of long-term Treasuries over the next six months in order to try and get credit flowing more freely again.

The Fed also announced plans to buy an additional \$750 billion in mortgage-backed securities; a move designed to lower mortgage rates.”

Maybe at 2:00 EST on Wednesday, March 18th, traders forgot that just one day prior, at a meeting in Washington, Bernanke informed the Council on Foreign Relations that the reason for the purchase of \$300 billion in Treasuries and \$750 billion in mortgage-backed securities, was because the Fed needed to “redouble its efforts after the [central bank’s balance sheet shrank 17 percent](#) from a \$2.7 trillion December peak.” Perhaps they forgot that in that same report “Bernanke acknowledged the chance that the unemployment rate will exceed 10 percent for the first time in a quarter century.”

The reason presented for the explosive, 6.8 percent rally three trading days later, on Monday, March 23, 2009 was much the same.



After weeks of handwringing over the need for the US Treasury to come up with a plan to purchase toxic assets from banks in order to help get credit flowing through the financial system again, Mr Geithner and crew presented a \$1 trillion bailout program. Geithner's March 23rd, 2009 article in the Wall Street Journal was titled, [My Plan for Bad Bank Assets](#). In it Geithner states:

“Today, we are announcing another critical piece of our plan to increase the flow of credit and expand liquidity. Our new *Public-Private Investment Program* will set up funds to provide a market for the legacy loans and securities that currently burden the financial system.

The *Public-Private Investment Program* will purchase real estate related loans from banks and securities from the broader markets. Banks will have the ability to sell pools of loans to dedicated funds, and investors will compete to have the ability to participate in those funds and take advantage of the financing provided by the government.

The new *Public-Private Investment Program* will initially provide financing for \$500 billion with the potential to expand up to \$1 trillion over time, which is a substantial share of real-estate related assets originated before the recession that are now clogging our financial system. Over time, by *providing a market for these assets that does not now exist*, this program will help improve asset values, increase lending capacity by banks, and reduce uncertainty about the scale of losses on bank balance sheets. The ability to sell assets to this fund will make it easier for banks to raise private capital, which will accelerate their ability to replace the capital investments provided by the Treasury.” (Italics Mine)

Over the last year, we have been told that excessive leverage is the reason for this structural global financial crisis. Once again, it looks as though traders on that day paid little attention to the details - the devil's always in the details.

In case you haven't been reading on this lately, let me go over the important parts. They used to be called Public-Private Partnerships, but “a rose by any name would smell as sweet.” All partnerships are not 50/50, and in this one the public, that is, the average American citizen, pays 92 percent of the bill to make the banks whole on some bad investments they made. The US government

provides a “loan” of 85 percent and an “investment” of 7 percent out of all of the “surplus money they have on their balance sheets,” or through the hidden tax of inflation upon its citizens. Of course, the private investors put up 8 percent, and, one would suppose, gets to split profits with the government. And for all this, the average person gets to keep the banking system afloat for one more day.

So, let’s stop from the giddiness of the recent rallies and ask a few questions.

First, “Where did we find all this extra money lying around to help the banks with their toxic assets?” The [US Treasury’s website](#) showed the national debt stood at \$11 trillion the day Geithner suggests we “provide financing for \$500 billion with the potential to expand up to \$1 trillion over time.” We’ve certainly come a long way in the last half century. On August 21st, 1962, in an article titled, [US Debt Climbs to \\$300 billion: Figure Amounts to \\$1600 for each person in Country](#), the New York Times, noted, “The total national debt has reached \$300 billion for the first time in history, the Treasury said today.”

If the rapid growth of our nation’s debts seem irrelevant to Geithner or Bernanke, our largest creditor holds a different view. Having [just lost substantial amounts](#) of their reserves through their State Administration of Foreign Exchange, China’s opaque manager of nearly \$2 trillion in foreign reserves, on March 13th 2009, Chinese Premier Wen Jiabao, voiced his concerns about US money printing. On that day, in an article titled, [China ‘worried’ about US Treasury holdings](#), MSNBC reports:

“‘Of course we are concerned about the safety of our assets. To be honest, I’m a little bit worried,’ Wen said at a news conference Friday after the closing of China’s annual legislative session. ‘I would like to call on the United States to honor its words, stay a credible nation and ensure the safety of Chinese assets.’”

In February US Treasury data shows that China’s holdings of US Treasury debt [hit \\$739 billion](#), up from \$535 billion just last August. Will China always buy any amount of debt Bernanke and Geithner dole out? On March 23rd 2009, Financial Times released an article titled, [China Calls for New Reserve Currency](#), stating:

“China’s central bank on Monday proposed replacing the US dollar as the international reserve currency with a new global system controlled by the International Monetary Fund.

In an essay posted on the People’s Bank of China’s website, Zhou Xiaochuan, the central bank’s governor, said the goal would be to create a reserve currency ‘that is disconnected from individual nations and is able to remain stable in the long run, thus removing the inherent deficiencies caused by using credit-based national currencies.

Analysts said the proposal was an indication of Beijing’s fears that actions being taken to save the domestic US economy would have a negative impact on China.

Although Mr. Zhou did not mention the US dollar, the essay gave a pointed critique of the current dollar-dominated monetary system.

‘The outbreak of the [current] crisis and its spillover to the entire world reflected the inherent vulnerabilities and systemic risks in the existing international monetary system,’ Mr. Zhou wrote.

To replace the current system, Mr. Zhou suggested expanding the role of Special Drawing Rights, which were introduced by the IMF in 1969 to support the Bretton Woods fixed exchange rate regime but became less relevant once that collapsed in the 1970s.

Mr. Zhou said the proposal would require, ‘extraordinary political vision and courage’ and acknowledged a debt to John Maynard Keynes, who made a similar suggestion in the 1940s.”

And, perhaps this is the direction that was intended all along. If you’re unfamiliar with the idea that John Maynard Keynes proposed in the 1940s, let me take you back to that era, when the world was still reeling from another world crisis and currencies were far off the radar screen of most individuals. On page 481 of, [A History of Money and Banking in the United States](#), Dr. Murray Rothbard notes:

“While the [US] White Plan envisioned a substantial amount of inflation to provide greater currency liquidity, the British responded with a Keynes Plan that was far more inflationary. By this time, Lord Keynes had

abandoned economic and monetary nationalism for Britain under severe American pressure, and his aim was to salvage as much domestic inflation and cheap money for Britain as he could possibly induce America to accept. The Keynes Plan envisioned an International Clearing Union (ICU), which, in return for agreeing to stable exchange rates between currencies and the abandonment of exchange control, provided a huge loan to its members of \$26 billion. The Keynes Plan, moreover, called for a new international monetary unit, the 'bancor,' which could be issued by the ICU in such large amounts as to provide almost unchecked room for inflation, even in a country with a large deficit in its balance of payments.”

And, Geithner is open to China's suggestion. On March 26th 2009, a Chinese news source, the People's Daily Online, noted:

“Meanwhile, Timothy Geithner, speaking at the Council on Foreign Relations in Washington on Wednesday, said that the U.S. is ‘open’ to China's proposal.”

‘I haven't read the governor's proposal. He's a very thoughtful, very careful distinguished central banker. I generally find him sensible on every issue,’ Geithner said, saying that however his interpretation of the proposal was to increase the use of International Monetary Fund's special drawing rights (SDRs) – shares in the body held by its members – while not creating a new currency in the literal sense.

‘We're actually quite open to that suggestion – you should see it as rather evolutionary rather building on the current architecture rather than moving us to global monetary union,’ he said.

‘The only thing concrete I saw was expanding the use of the (SDRs),’ Geithner said. ‘Anything he's thinking about deserves some consideration.’

The continued use of the dollar as a reserve currency, Geithner added, ‘depends on how effective we are in the United States...at getting our fiscal system back to the point where people judge it as sustainable over time.’”

Though we discuss the behind the scenes aspects of these maneuvers in more detail in the closing pages of our November 2008 issue of *The Investor's Mind*, "The Power of...the Few," we will briefly touch on SDRs in the [IMF's own words](#):

"The Special Drawing Right (SDR) was created by the IMF in 1969 to support the Bretton Woods fixed exchange rate system.

After the collapse of the Bretton Woods system in 1973, the SDR was redefined as a basket of currencies, today consisting of the euro, Japanese yen, pound sterling, and U.S. dollar. The U.S. dollar-value of the SDR is [posted daily](#) on the IMF's website."

As we read the [IMF's website](#) further, we learn that the IMF has been trying to expand the amount of SDRs in circulation for years. The only thing the IMF needs to do so is a "yes" vote from the US on an IMF amendment. In the same issue of *The Investor's Mind*, we quote George Soros' October 28th 2008 article in the *Financial Times*, where Soros states, "The financial crisis is spinning out of control. It is time to start thinking about creating special drawing rights or some other form of international reserves on a large scale, but *that* is subject to American veto."

On April 2nd 2009, the [G20 will meet in London](#) to discuss the largest expansion of lending powers of the IMF in world history. Both [Japan](#) and the [United States](#) have indicated that they will loan the IMF up to \$100 billion, while [the EU](#) has stated that they will loan the IMF €75 billion.

While the UK has not agreed to an amount to loan to the IMF, as of this release, their financial stress indicates that they are having severe problems of their own right now. On March 25th 2009, a Bloomberg article titled, [UK Bond Auction Fails for the First Time since 2002](#), reports:

"The UK failed to find enough buyers for 1.75 billion pounds (\$US 2.55 billion) of bonds for the first time in almost seven years as debt investors repudiated Prime Minister Gordon Brown's plan to stem the worst economic crisis in three decades."

While most individuals refuse to believe that we have arrived at this juncture, any good contrarian looks to history to get their bearings. An expansion of a central

currency will shift power away from independent countries and towards the global powers that be. And though, in light of the US's profligacy, this may sound like a good idea to many, there is ample evidence to suggest that we were led to this point for a reason. Joan Veon, founder of the [Women's International Media Group](#), shows us that the "Public-Private Partnership" has been around since at least 1996 and talks about the history of such arrangements.

"I first heard the term Public-Private Partnership (PPP) when I attended the June 1996 United Nations Habitat II conference in Istanbul Turkey. The first time I read the conference's Programme of Action, I missed it completely. After I returned from Istanbul, I went back over the document and was shocked at its prominence. I spent six months trying to figure out what it was and I even conducted several interviews with people at the U.N. and other agencies.

A Public-Private Partnership is exactly what it says it is. First, it is a partnership that is business arrangement, and it is for profit...Historically, such deals were considered glaring conflicts of interest, and as such, not in the best interest of the people...When you marry government and business, all existing rules of law and government change as the checks and balances of our Constitution no longer pertain...The door is open for anything – politically, socially, and economically. Plunder is tyranny."
(The United Nations Global Straightjacket (1999) Joan Veon, pp83-86)

So if you have recently been swept into euphoria of this explosive rally of the last few weeks, and haven't spent a great deal of time studying the history of money and politics, now is the time to start asking a great many skeptical questions. History suggests that the second quarter of 2009 could be among the most important periods in financial history.

Regards,

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