THINGS THAT MAKE YOU GO *Hmmm...*

A walk around the fringes of finance

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"Unity to be real must stand the severest strain without breaking"

– MAHATMA GANDHI

"And ever has it been known that love knows not its own depth until the hour of separation"

– Khalil Gibran

"At the end of the day it's about how much you can bear, how much you can endure. Being together, we harm nobody; being apart, we extinguish ourselves."

– Tabitha Suzuma

Well, it was touch and go for a while, but here we are: January, 2012. The 10th anniversary of the euro!!!!!

Well..... that's actually not STRICTLY true. In fact, the euro debuted as a financial unit three years prior, on January 4th 1999, but only in corporate and investment markets.

Initially, there were eleven EU nations that adopted the currency at launch (for those of you keeping score at home they were Austria, Belgium, Finland, France, Germany, Italy, Luxembourg, the Netherlands and the future PIIGS Ireland, Portugal and Spain).

In all, about 290 million people were suddenly represented by a new unit of exchange designed to increase European integration and economic growth.

The euro got off to a flying start - closing its first day of trading at a healthy-looking 1.17 to the dollar (a level it may well soon recapture if recent days are anything to go by) - and looked set to become a serious competitor to the big name wrapper in the world of fiat currency - The Ubiquitous U-S-D.

Three years later - and ten years ago this week - the euro proper became legal tender as banknotes denominated in euro went into circulation across the continent, replacing the Austrian schilling, Belgian franc, Finnish markka, French franc, German mark, Italian lira, Irish punt, Luxembourg franc, Netherlands guilder, Portugal escudo and Spanish peseta. The UK, Sweden and Denmark all decided NOT to join the party after fierce debates in their respective Parliaments which have now cemented some political legacies and irreparably damaged others.

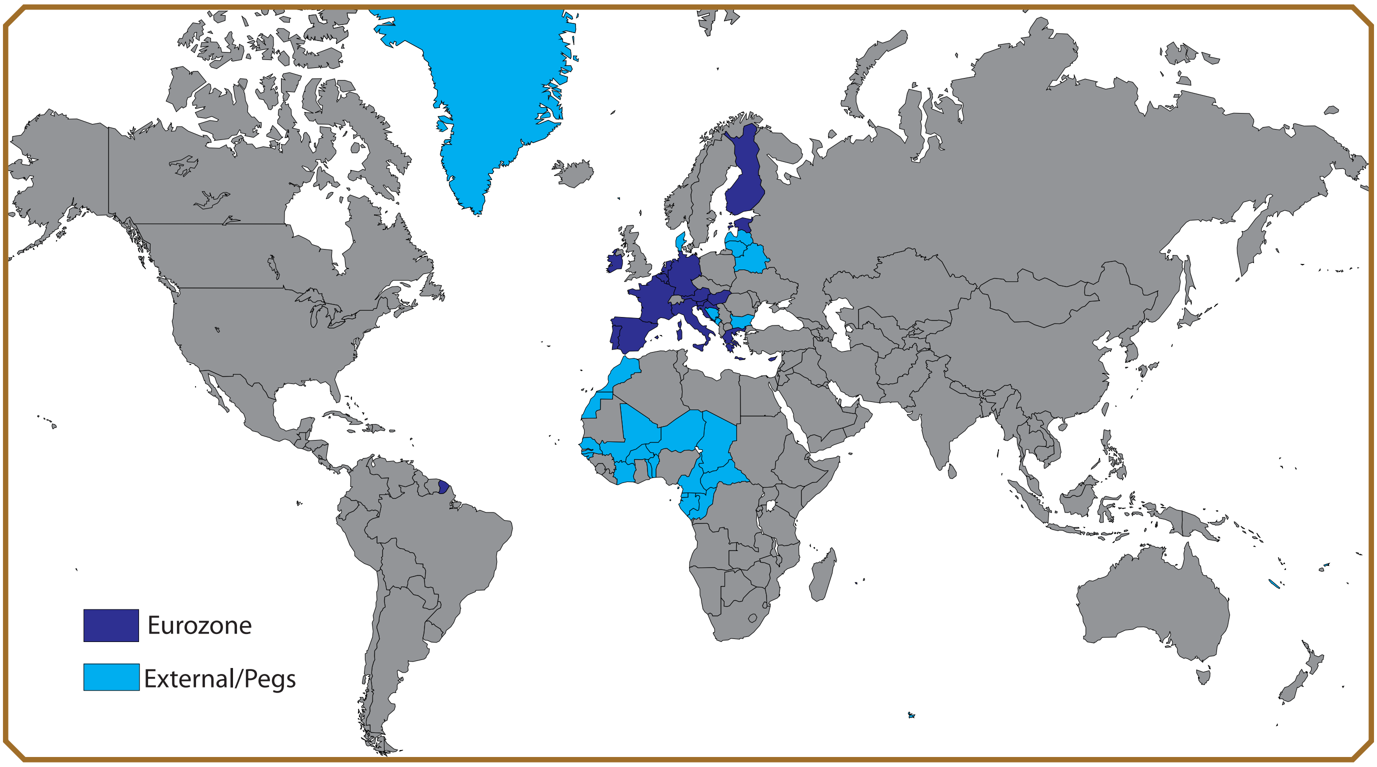
Currently, aside from the 17 members of the Eurozone who have fully adopted the euro (and by now, like the regulars at Cheers, everybody knows their names), Montenegro and Kosovo and several European micro states (Andorra, Monaco, San Marino and the Vatican City) as well as in three overseas territories of EU states that are not themselves part of the EU (Mayotte, Saint Pierre and Miquelon and Akrotiri and Dhekelia) have, in their collective wisdom, decided to adopt the euro and lash themselves to the deck of the SS Eurozone. Together this direct usage of the euro outside the EU affects over 3 million people.

But it doesn't finish there. Oh no. Not by a long chalk.

Cuba, North Korea and Syria all actively use the euro as a trading currency while, outside the Eurozone proper, a further 23 countries have direct pegs to the euro as a result of previous pegs to either the French franc, Deutsche mark or Portuguese escudo. In addition, Bulgaria, Denmark, Lithuania and Latvia also have opted to institute euro-pegs of one form or another.

Collectively, this means that the currency currently walking a very thin line between love and fate is officially used by 350 million Europeans, an additional 150 million people in Africa and a further 25 million people in various territories and, last but definitely not least, a further 500,000 poor souls on various Pacific Islands.

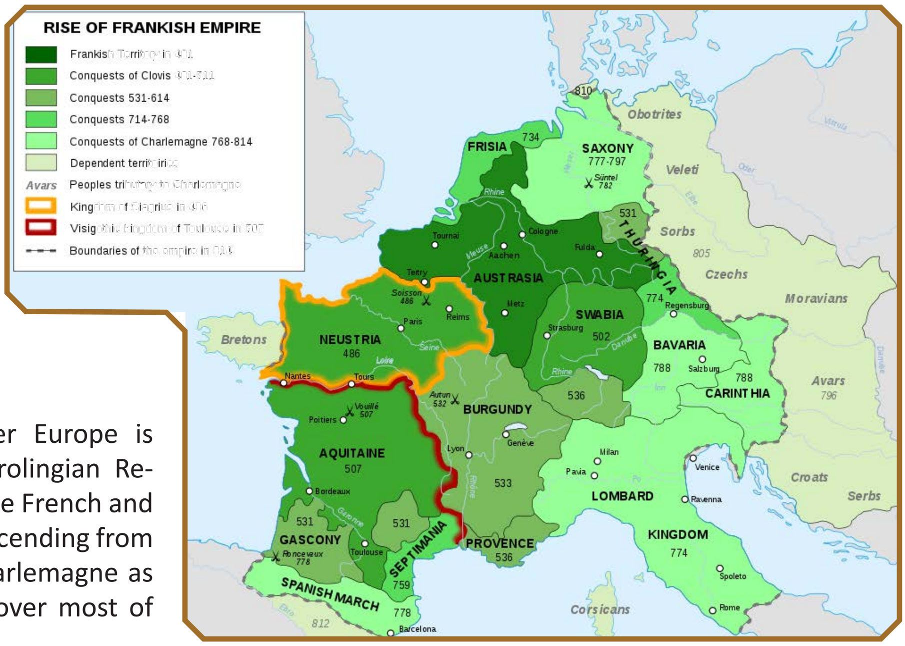
The chart on the next page gives an idea of the coverage of the Euro (including external pegs) and,



SOURCE: WIKIPEDIA/TTMYGH

though the detail required to be able to see the myriad tiny territories that are tied in some way to the euro is unavailable at this resolution, trust me - they are there.

Not since the reign of Charlemagne in the 9th century had Europe been united (almost) under a common currency - although back then, The King Of The Franks had to unite Europe under a slightly more aggressive banner as he expanded the Frankish kingdom into an empire that, after his conquest of Italy, incorporated most of Western Europe. Charlemagne was crowned Imperator Augustus by Pope Leo III on December 25, 800.



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SOURCE: WIKIPEDIA

Charlemagne's rule over Europe is associated with the Carolingian Renaissance and, in fact, the French and German monarchies descending from the empire ruled by Charlemagne as Holy Roman Emperor cover most of

Europe. In his acceptance speech of the Charlemagne Prize Pope John Paul II referred to him as the Pater Europae ("father of Europe"): his empire united most of Western Europe for the first time since the Romans, and the Carolingian renaissance encouraged the formation of a common European identity. As you can see from the map of the Frankish Empire on the previous page, a similarly -shaped 'core' was at its heart.

It was all so easy back then. If the peripheral countries of your alliance don't behave themselves, simply dispatch an army.

Charlemagne presided over the creation of Europe's first 'common currency' - the denier - and, though its introduction was somewhat less of a negotiation than that of the euro, a look at the history surrounding its birth proves that, while things change, they stay the same in many ways:

(Wikipedia): Charlemagne had an important role in determining the immediate economic future of Europe. Pursuing his father's reforms, Charlemagne abolished the monetary system based on the gold sou, and he and the Anglo-Saxon King Offa of Mercia took up the system set in place by Pippin. There were strong pragmatic reasons for this abandonment of a gold standard, notably a shortage of gold itself, which was a direct consequence of the conclusion of peace with Byzantium, which resulted in the ceding of Venice and Sicily and the loss of their trade routes to Africa and to the East. This standardisation also had the effect of economically harmonising and unifying the complex array of currencies which had been in use at the commencement of his reign, thus simplifying trade and commerce.

He established a new standard, the livre carolinienne (from the Latin libra, the modern pound), which was based upon a pound of silver—a unit of both money and weight—which was worth 20 sous (from the Latin solidus [which was primarily an accounting device and never actually minted], the modern shilling) or 240 deniers (from the Latin denarius, the modern penny). During this period, the livre and the sou were counting units; only the denier was a coin of the realm.

Charlemagne instituted principles for accounting practice by means of the Capitulare de villis of 802, which laid down strict rules for the way in which incomes and expenses were to be recorded...

In addition to this macro-oriented reform of the economy of his empire, Charlemagne also performed a significant number of microeconomic reforms, such as direct control of prices and levies on certain goods and commodities.

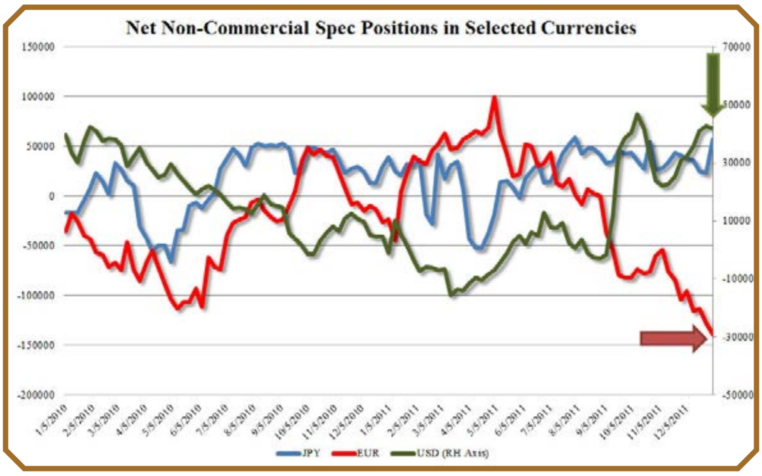
Charlemagne applied the system to much of the European continent, and Offa's standard was voluntarily adopted by much of England. After Charlemagne's death, continental coinage degraded, and most of Europe resorted to using the continued high-quality English coin until about 1100.

Ring any bells?

A gold standard, abandoned mostly due to a shortfall in the amount of the metal required to back the monetary system? A common bloc designed to simplify trade and commerce? Macro-economic reform of the union from the centre? Voluntary adoption by England who was not part of the union?

Ah, well almost.

Anyway, my point is this: In the mid-700s it probably seemed inconceivable that Europe would be united under a common ruler, much less a common currency and, by the mid-800s, it probably seemed equally inconceivable that such a union could split asunder - but such is the nature of unions (and currency blocs for that matter). As the individual members undergo the individual stresses associated with running individual and idiosyncratic economies under a common banner, it is inevitable that there will be periods when maintaining the status quo becomes impossible.



CLICK TO ENLARGE

SOURCE: ZEROHEDGE

It was true of Europe in 800 - it holds true today.

This past week, seemingly out of the blue, the reality of the situation facing the Euro as a currency, as well as the region's economy, seems to have dawned on the collective conscious and, consequently, it has gapped lower at speed, leaving many scratching their heads when, really, the time to be doing that was last year as, despite the obvious fragility of the union, the currency managed to stay relatively strong in the face of a seemingly never-ending flow of headlines that suggested one way or another, its days were well and truly numbered. The net short position in euro hit an all-time high this past week (chart, above) as speculative shorts joined the dogpile with barely-disguised glee (making it likely we will see a countertrend rally - no matter how brief it is).

In fact, had you sold the euro short on January 5th 2011, you would have been losing money until December 12th and ended up making a miserly 1.43% return on your investment (chart, below) DESPITE

SOURCE: BLOOMBERG

having spent virtually the entire 12 months reading headline after headline about the inevitable demise of Greece, possibly Portugal, then Spain, then Italy and finally France. Hard to believe - and yet...

As we enter 2012, it is clear that Europe is still the focus of most people's attention (although I suspect the gradual shift towards the Middle East is a trend that should and will accelerate in coming weeks) and I firmly believe that the continent is finally heading towards a resolution in 2012.

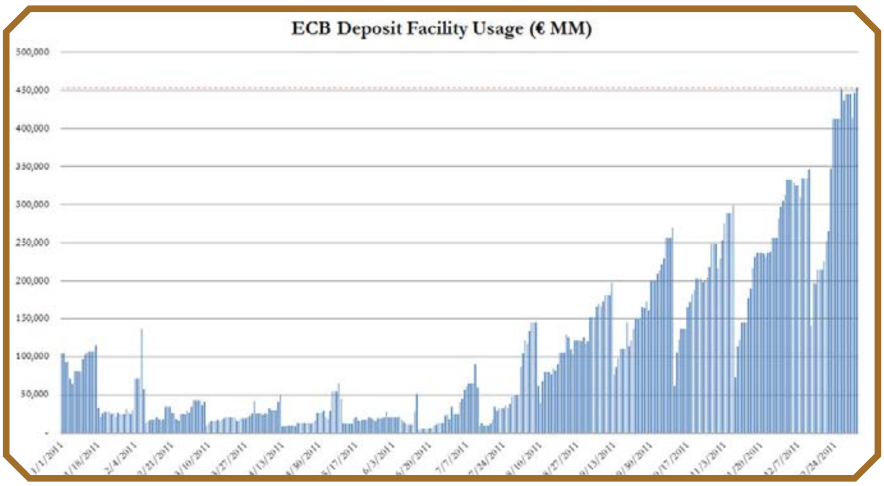
I suspect that resolution will NOT be pretty, will result in much upheaval and, ultimately, mean the end of the euro (at least in its current form), but from the ashes of that resolution we will find the clarity we need to move forward and put the past 2 years of ever-worsening headlines behind us.

Greece is done. Period. They cannot remain in the Eurozone - nor should they and, with the next bailout package (this time north of €100bln) being due in March when a whopping €17.5bln of Greek debt will need to be sold (although, between now and then, any of the 5 smaller auctions - starting with next week's €2bln could tip the scales), it's hard to see how they make it past that point. The Troika's visit to Athens on January 16th will no doubt ramp up the rhetoric once more, but realistically handing ANOTHER €100bln+ to the Greeks would be both cavalier and stupid.

(All € bln)	Italy	Spain	Greece	Portugal	Ireland	Belgium	France	Germany
January	€15.6	€9.2	€4.0	€4.0	€0	€7.4	**€49.5**	**€34.0**
February	**€53.1**	€14.7	€2.3	€4.0	€0	€7.2	**€37.2**	€9.0
March	**€44.2**	**€17.5**	**€17.5**	€2.8	€5.5	€10.4	**€33.7**	**€28.0**
Total	**€112.9**	**€41.4**	**€23.8**	**€10.8**	**€5.5**	**€25.0**	**€120.4**	**€71.0**

The table above highlights the issuance for the PIIGS plus Belgium, France and Germany for the first quarter of this year and, makes quite clear, that something, somewhere has to give. March alone will see the need for €159.6bln to be raised amongst these 8 nations out of a whopping €400bln for the first quarter of 2012.

Now, Signor Draghi's rather cunning 3-year LTRO program, (which last month saw 523 European banks borrow €489 billion last month in exchange for God knows what collateral) COULD provide an opportunity for the banks to scratch the ECB's back by borrowing an inordinate amount of money at the next offering in February and pumping it into sovereign bonds, but that didn't happen in December.



CLICK TO ENLARGE

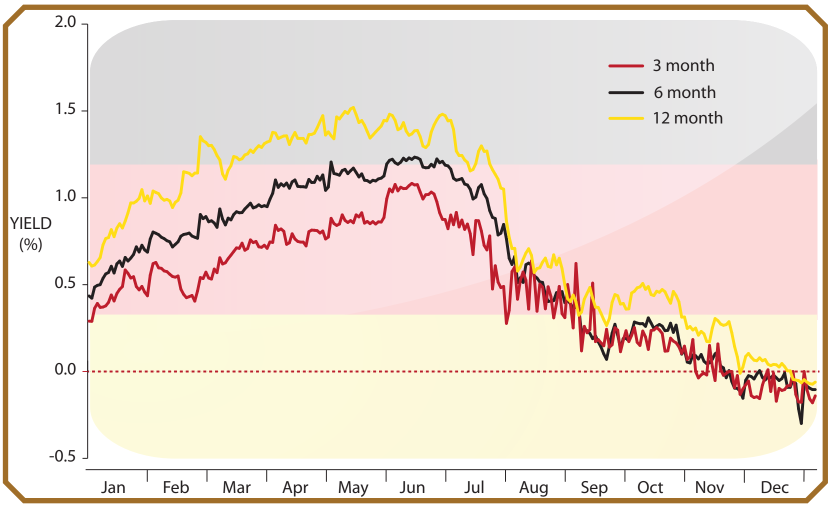
SOURCE: ZEROHEDGE

While I suspect this first tranche was needed to shore up the banks' own balance sheets and that the next LTRO may possibly be the quid pro quo that the ECB is looking for and spark a flood of circuitous cash being lent by the ECB to banks to be spent propping up sovereign bonds which will then be returned TO the ECB at the next LTRO as fresh collateral for MORE loans, there is absolutely NO guarantee that this will take place. Indeed, a significant proportion of that €489 billion - borrowed at 1% - has been deposited back at the ECB for the princely interest rate of 0.25% per annum as you can see from the chart (left).

With deposits at the ECB hitting an all-time high €453bln this past week, it may turn out to be far harder for the ECB to 'persuade' the banks that the money they have been gifted really OUGHT to be finding its way into the economy rather than their own deposit facility as banks, knowing full-well just how terrifying the state of their OWN balance sheets are, run scared of lending any of the ECB's ~~freshly printed~~ temporary injection of cash to their peers:

> *(UK Guardian): Fresh fears about the eurozone banking system were raised when record amounts of cash were deposited with the European Central Bank and Italy's UniCredit spooked markets with a cash call on investors.*
>
> *Some €453bn (£378bn) was lodged in the ECB's "deposit facility" on Tuesday night in a move that some analysts feared showed banks were so concerned about lending it out to rivals that they would rather earn just 0.25% in interest from the central bank.*
>
> *The ECB also revealed that €15bn had been used from its emergency lending facility overnight on Tuesday, following €14.8bn borrowed the previous day.*
>
> *"Interbank funding markets are getting more credit crunched, not less," said Louise Cooper, markets analyst at BCG Partners. Referring to the deposits at the ECB, she said: "This shows how much fear there is still in the wholesale markets – that banks prefer to accept only 0.25% interest rate on their cash rather than lending it out at higher rates to other banks.*
>
> *"Central banks are having to fund banks themselves because so many credit, wholesale and rates markets are not functioning normally and it is getting worse ...*

That's the funny thing about giving money to people - once you DO, it's always a LOT harder to get it back from them and, even if borrowing money at 1% and lending it straight back to the ~~loanshark~~ bank who loaned it to you at 0.25% could hardly be described as 'good business', Europe's banks are really in no mood to let go of any cash.



SOURCE: BLOOMBERG/TTMYGH

Everywhere we look we see fear and loathing as well as a desperate desire to have cash at any cost. Safety is DEFINITELY back in vogue going into 2012 just as it was in 2008.

In Germany, 3-month, 6-month and 12-month bond yields all turned negative in late November and, though the 1-year Bund yield briefly climbed into positive territory, as I write this, all three maturities are, once again, solidly negative (chart, left) as Europeans choose (perceived) safety over any kind of return whatsoever.

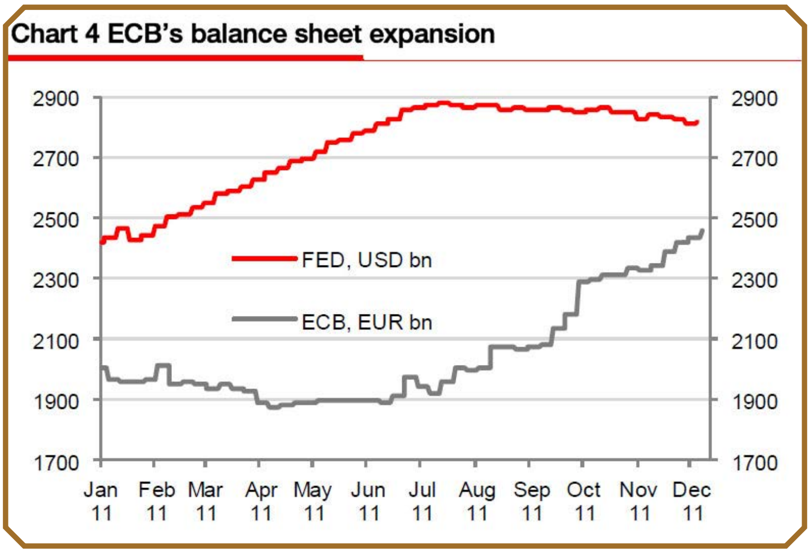
So how does it all end, I wonder?

Well, given that Europe's banks have been told by the EBA to raise €114.7bln euro by the end of June in order to shore up their capital bases (highlights, table, below) - and at this point it is important to remember that it was the EBA who conducted the stress tests which, last July gave Dexia a clean bill of health a mere three months before it needed a bailout from France and Belgium - and the PIIGS plus Germany, Belgium and France (the BIG PFIGS, if you will) need to raise an additional €400bln+ before March, is it any wonder that nobody is letting go of what cash they ARE lucky enough to find themselves holding?

Bank Capital Shortfalls By Country (EBA Stress Test December 2011)					
Germany	France	Austria	Italy	Spain	Portugal
€13.1bln	€7.3bln	€3.9bln	€15.4bln	€26.17bln	€6.95bln

But it gets worse.

Between them, in 2012, the G-7 alone will need to raise over $7 TRILLION in sovereign maturities (to say nothing of an additional $566billion in interest payments), of which Japan and the US (remember them?) require a staggering $5.81 TRILLION. These sovereign nations will all be competing for a shrinking pool of capital in a world that is literally choking on debt and doing anything it possibly can to hang on to cash. Is it any wonder that Central Banks the world over are desperately finding ways to 'reliquify' their respective banking systems?



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SOURCE: FED/ECB/DATASTREAM/SOC GEN

The BoE, SNB and the Fed have shown their proclivity to wards quantitative easing whilst the ECB has steadfastly refused to countenance such an idea - at least outwardly, but, as the chart (left) demonstrates, since July last year, the ECB's balance sheet has expanded far faster than that of the Fed and, despite what the Eurocrats may say in front of the cameras, they know full well that, in a world of competitive debasement and in an economy that is plunging into recession, if they DON'T print, they will be left for dead.

I have been saying for many months now that the ECB WILL print money ultimately, but clearly I was wrong.

The ECB **IS** printing money.

The realisation of covert moneyprinting by the ECB, the gauntlet thrown down by the SNB and the knowledge that the BoE shows up at QE parties like former Big Brother contestants at the opening of a supermarket allied to the safe assumption that the Fed is fueling the QE3 choppers (signs of which I suspect we will see in the January FOMC minutes) means that 2012 is likely to see a flood of funny money that will make 2010 and 2011 look positively miserly.

Which brings us to one last thing; the strange action in gold at the end of 2011.

Having hit $1,900 during 2011, gold 'plummeted' back to a level it hadn't seen since, oh, I dunno, JULY?

Now, naturally, this precipitated yet another 'end to the bull market in gold' (which, after its 9% gain in 2011, still has yet to register a down year since it 'crashed' 5% in 2000), but the manner in which gold sold off in quiet year-end markets was, to say the least, interesting. Granted, the MF Global situation had an effect on futures markets, but in the gold pit, the 'safe haven' asset was taken unceremoniously out to the woodshed and given what we Brits lovingly refer to as 'a good kicking', as can be seen from the chart below, left.

CLICK TO ENLARGE   SOURCE: JESSE'S CAFE AMERICAIN

A regular in these pages, and one of the most astute observers of the gold markets, Jesse, had this to say about the events of December:

(Jesse's Cafe Americain): Like many others who watch the markets I have wondered what might be prompting this obvious bear raid on the paper precious metals market over past four weeks.

It could be explained by any number of economic developments including the decline of the Euro, but that does not really explain the downward market action which has been sporadic and not associated with news, more so than fundamental.

One has to be a bit naive or disingenuous to ignore the blatant bombing of the market with large numbers of contracts for sale during thinly traded markets. This is the not the sort of trading that a profit seeking trader would do except under the duress of a margin call.

I admit this would be less likely if one has a high level of confidence in the CFTC. They have not done much to inspire such confidence in the public this year, particularly in light of their mishandling of the silver market investigation and of course MF Global.

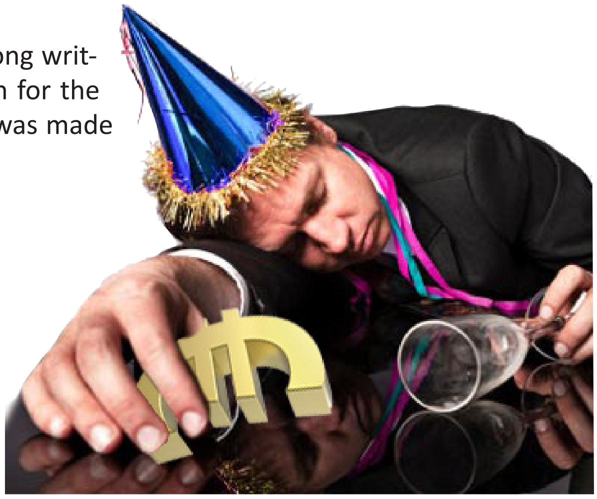
Anyone who watches the tape, rather than waving their hands from the 50,000 feet level, can see this clearly.

From speaking with other traders, and based on my own thinking, I believe that what we are seeing is primarily a type of end of year window dressing supplemented by a broad desire to maintain 'orderly' prices by the central banks.

Whether you take the sell-off in gold at face-value, or whether you think there may be something more, shall we say 'coordinated' behind it, one thing is inarguable - gold begins a year in which Central Banks are going to be forced to print an AWFUL lot of new paper money significantly lower than it was a month before we ushered in that year.

So there we have it. As we celebrate the 10th anniversary of the euro we can cast our eyes ahead to a year of coordinated moneyprinting on an epic and truly global scale that may (or may not.... but ... may) see the end of the latest version of a European 'empire', at least in its present form.

Whaddya say we can all meet up back here next year for the euro's 11th birthday and discuss what happened in 2012?



And so, in closing, I leave you with the words to a song written by Jule Styne, Betty Comdem and Adolph Green for the musical comedy "Bells Are Ringing" in 1956, which was made famous by the legendary Nat King Cole:

"The party's over
It's time to call it a day
They've burst your pretty balloon
And taken the moon away
It's time to wind up the masquerade
Just make your mind up the piper must be paid"

∞ ∞ ∞ ∞ ∞ ∞ ∞ ∞ ∞ ∞ ∞

In this edition of Things That Make You Go Hmmm..... we take a look at the practicalities of shutting the Straits of Hormuz while Charles Hugh Smith explains a far easier way to put Iran out of business than war and see how a raid by Italian tax authorities in the exclusive ski-town of Cortina found a wealth of not just irregularities.

The von Mises Institute explains why 'Gloom & Doomers' just may be the sanest of all commentators, Jeff Clark examines why gold has seen such a sharp sell-off and, in Germany, we see how citizens are rushing to put their money in luxury goods.

Americans are struggling to understand the math behind the big political issues in this election year, retail sales edged higher in December (but at what cost to profits?) and we take a fascinating look at a 2-product, 2-customer wonder, otherwise known as Australia.

There is a fascinating interview with the governor of the PBOC, an examination of the impact the world's top three central banks are having on global GDP, my friend John Mauldin takes his own view out into 2012 (and a must-read one it is too) and, by way of some comfort we hear from a member of the governing council of the ECB who reassures us that the idea of the end of the euro is 'fantasy'.

Phew! You can now officially disregard everything you have read so far. Sorry to have wasted your time.

In our charts section we have two great charts of the euro from Richard Ross of Auerback Grayson, Tim Iacono looks at rising global debt versus the gold price, Jesse finds a curious trend creeping into the jobless numbers in the US and there are even more curious situations developing in both the Fed's custodial account (which is seeing dramatic outflows) and the silver market (which could soon be seeing substantial inflows).

We have a great interview with the always-fascinating Martin Armstrong, Paddy Hirch explains rehypothecation (something we will be looking at in greater detail in coming weeks as, in my opinion, it's one of the most overlooked, yet potentially extremely dangerous) stories currently occupying page 37 of most newspapers and I took the liberty of including an interview I gave to Dr. Jeff Clark this past week in which we discussed a wide range of subjects including my outlook for 2012 and the dangers of mixing emotion with silver.

By way of housekeeping, there will be no Things That Make You Go Hmmm..... next week as I will be traveling, but I hope to be back with you in a couple of weeks.

Would somebody please keep the plates spinning until I get back?

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Finally, I will be taking on my first speaking engagement next month at the Cambridge House California Investment Conference in Palm Springs. The conference runs over the weekend of the 11th and 12th of February so if any readers are in the area and would like to stop by, I would love to see you there.

The line-up this year is fantastic with John Embry, Greg Weldon, Brent Cook, Bill Murphy and Chris Powell of GATA and my friend, Al Korelin just a few of the many speakers in attendance.

It should be a lot of fun and, personally, I'm looking forward to having the chance to meet and listen to insights from some of the sharpest financial minds around.

For details, please click on the link HERE

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Want to Put Iran Out of Business? Here's How

Those attempting to pressure Iran by increasing "tensions" and thus the price of oil have it precisely backwards. The one sure way to fatally destabilize the Iranian theocracy is to adjust the demand and supply of oil so the price plummets (as it did in December 2008) to $25/barrel, and stays there for at least six months.

It has been estimated that the Iranian theocracy cannot fund its bloated bureaucracies, military and its welfare state if oil falls below around $40-$45/barrel. Drop oil to $25/barrel and keep it there, and the Iranian regime will implode, along with the Chavez regime in Venezuela.

Saber-rattling actually aids the Iranian regime by artificially injecting a "disruptive war" premium into the price of oil: they can make the same profits from fewer barrels of oil.

The way to put them out of business is drop the price of oil and restrict their sales by whatever means are available. They will be selling fewer barrels and getting less than production costs for those barrels. With no income, the regime will face the wrath of a people who have become dependent on the State for their sustenance and subsidized fuel.

"... How do you drop oil to $25/barrel? Easy: stop saber-rattling in the mideast and engineer a massive global recession with a side order of low-level trade war."

How do you drop oil to $25/barrel? Easy: stop saber-rattling in the mideast and engineer a massive global recession with a side order of low-level trade war. Though you wouldn't know it from the high price of oil, the world is awash in oil; storage facilities are full, and production has actually increased a bit in North America.

Long-term, Peak Oil is a reality; but in the short-term, production is more than adequate to meet recession-suppressed demand.

The way to drop oil from $100/barrel to $25/barrel is to crush demand via global depression. Let's face it, the global economy is already slipping into depression as credit bubbles pop and austerity and rising debt service expenses bleed off disposable income.

We can nudge the global demand for oil off a cliff with a few other policies, for example, a low-grade trade war with China and Japan. Political leaders everywhere are already itching for a scapegoat, and imports are ready-made and waiting. Slap some heavy tariffs on Chinese and Japanese goods for "dumping" or some other excuse and then the inevitable counter-tariffs will be imposed on U.S. imports. Since U.S. exports to Asia are but a thin slice of imports from those nations, even a low-key trade war will have outsized negative consequences on Asian exporters.

Exports make up a relatively small percentage of Japan's GDP (ditto for the U.S.), but they contribute most of the marginal growth and profits in the Japanese economy. China is hugely dependent on exports and fixed investment in factories and real estate. There is no way the Central Government can spend its way out of the hole created in the Chinese economy as the real estate bubble pops, exports plummet and foreign direct investment dries up.

Europe is already caught in a vice of austerity and rising debt service expenses, so a depression there is already in the pipeline.

CHARLES HUGH SMITH / **LINK**

A raid on Cortina d'Ampezzo, one of Italy's most exclusive ski resorts, has laid bare the startling levels of tax evasion as the new government of Mario Monti attempts to claw back billions in undeclared revenue.

Tax officials traced the owners of 133 Lamborghinis, Ferraris, SUVs and other top-end cars that they found parked in the snow-lined streets of Cortina d'Ampezzo, a winter playground for the rich and famous in the Dolomites.

They found that 42 of the owners – nearly a third – had declared incomes of less than 22,000 euros (£18,000) a year. A further 16 claimed to be earning less than 50,000 euros a year.

The investigation, in Italy's answer to St Moritz, highlights a nationwide problem of Italians cheating the tax man by hugely under-declaring their incomes or declaring no income at all.

The spot checks were carried out by a team of 80 officers from Italy's inland revenue agency, who said it would be almost impossible to run a top-of-the-range BMW or Porsche on such modest salaries, at a time when a full tank of petrol for a high-performance car can cost 180 euros.

"...dozens of businesses, apparently spooked by the attention of the tax inspectors, admitted earnings that were up to four times what they had declared in the same period last year."

Another 118 sports cars were found to be owned by companies, rather than individuals, for the purposes of tax write-offs.

But of those companies, 19 declared losses for the tax year 2009-2010, while 37 claimed to have made profits of 50,000 euros or less.

While Cortina's luxury chalets, designer boutiques and stunning natural setting have long made it popular with celebrities and the mega-rich, the "super blitz", as it was dubbed by the Italian media, sent a chill through its Italian clientele.

The checks came at the height of the ski season, when the population of the town, which hosted the 1956 Winter Olympics, swells from 7,000 to around 40,000.

Tax officials found evidence that hotels, restaurants, boutiques and beauty salons were also hugely under-declaring their takings.

When the town was targeted in the Dec 30 crackdown, dozens of businesses, apparently spooked by the attention of the tax inspectors, admitted earnings that were up to four times what they had declared in the same period last year.

UK DAILY TELEGRAPH / **LINK**

Marc Faber is a market analyst and publisher of the "Gloom, Boom and Doom Report" newsletter. As you may have gathered from that title, he's rather pessimistic about the economy. (He's also been very accurate concerning economic trends over his career.) But he really dropped jaws recently when he made the following statement on CNBC:

> *I am a great optimist in life; otherwise I would commit suicide in view of the kind of governments we have nowadays.*

Hyperbolic suicide comments aside, it brings up an interesting irony that I have been noticing for a while: many of the most bearish economic forecasters describe themselves as optimists in their day-to-day lives. I consider myself extremely optimistic, but my views on the economy are dire at best. The fact that we optimists are so pessimistic about the economy should cause you to take notice and ask if maybe there is something to all this gloom and doom after all.

That may seem like a paradox. If you listen to the financial news, those of us who have been predicting that the economy is on the verge of collapse are "gloom and doomers" who are just negative people. When we say that the Greek debt crisis can't be resolved with more bailouts and that default is inevitable, they call us defeatists. When we point out that America's economy is as bad as or worse than the problems in Europe and that the only solutions to get us out of this mess are currently politically impossible, they say we have no faith in America.

"... I consider myself extremely optimistic, but my views on the economy are dire at best. The fact that we optimists are so pessimistic about the economy should cause you to take notice and ask if maybe there is something to all this gloom and doom after all"

In fact, nothing could be further from the truth. We economic "gloom and doomers" are simply realists who understand the nature of the crisis based on Austrian economic principles. Our thirst for the truth has led us to question the Keynesian economic theories taught in our schools and propagated in the media, which sound sensible on the surface, but fall apart under logical scrutiny. This Austrian understanding of business cycles and the nature of money and human action tells us that unsustainable debts cannot be sustained, and that a debt-based fiat-money system that can't go on forever, won't.

So who are the optimists and who are the defeatists? Let's do a thought experiment.

Close your eyes and imagine you are living in New York City. (Now open your eyes so you can read the rest of this.) Imagine the local weathermen are all astrologists who have declared that although the sky looks dark, our horoscope says we have a bright future ahead of us. The clouds have always moved on in the past, and this time is no different. Then imagine an astronomer comes along and says, "I've done some scientific experiments and studied the data; that dark spot in the sky is actually a comet and it's heading straight for New York."

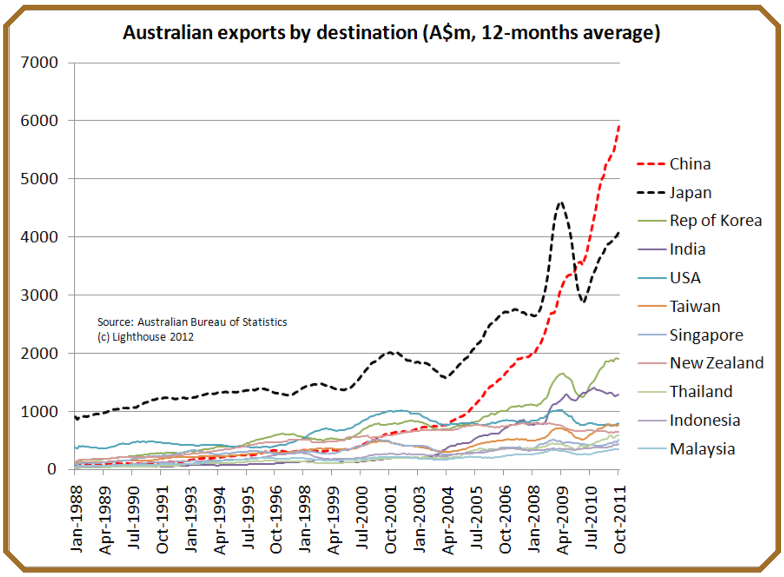
★ ★ ★ *VON MISES* / **LINK**

Australia is the sixth-largest country (2.9m square miles) on earth, just a tad smaller than the contiguous United States (3.1m). They are a little short on people (22.8m), which comes handy, since they dig up their entire country and sell the dirt to China.

Australia has a remarkably low government debt-to-GDP ratio (29%), low unemployment (5.2%), a moderate budget deficit (3.4% of GDP) and moderate inflation.

However, Australia has been running current account deficits of up to 6% of GDP for more than 50 years. The "mates", until recently, didn't like to save, hence most investment has to be financed by borrowing from foreigners.

I was curious as to how much of the success was due to exporting dirt to China. From the



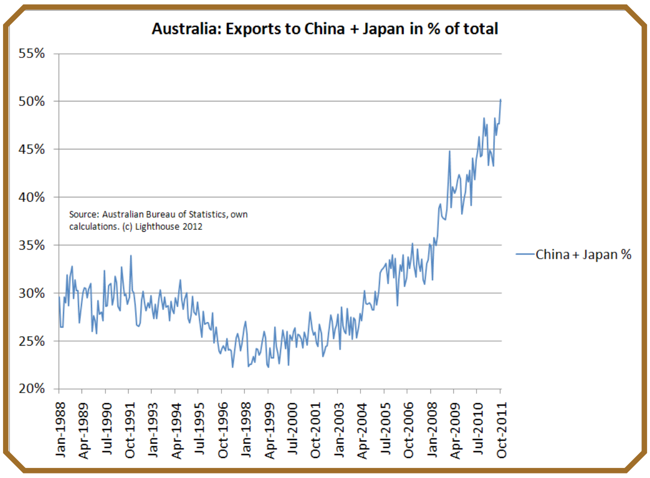
CLICK TO ENLARGE **SOURCE: LIGHTHOUSE**

Australian Bureau of Statistics you get the following data about their top-10 export markets (accounting for 82% of all exports) (chart, left):

A bit more than half (50.2%) of all exports go to two countries: China and Japan. If you stripped out those two, there wouldn't be much growth left.

The dependence on China and Japan has doubled over the last decade:

Over the last 12 months, total exports grew by A$ 35.6bn. Of that growth, 24.2bn, or 68%, came from China and Japan.



CLICK TO ENLARGE SOURCE: LIGHTHOUSE

★ ★ ★ *LIGHTHOUSE INVESTMENT MGT* / **LINK**

The uncertain financial markets and the euro crisis have left many Germans feeling nervous. Worried about the security of their savings accounts, increasing numbers of people are deciding they would rather invest in material goods like art, vintage cars and real estate instead. But experts warn that nothing is 100 percent safe any more.

Franz Herrmann, head of the German Association of Savers (BDS), has spent half a century trying to be a good investor. As a child, he filled piggy banks and, as an adolescent, he put money away in his savings account. Later came a building loan contract, in addition to 12 life insurance policies. "Money attracts money," his father liked to tell him, quoting a German saying. "I was hardwired for saving money," Hermann explains.

"... "People are becoming increasingly cautious about entrusting their hard-earned money to the banks," says Rolf Bürkl of market research institute GfK. It has yet to become a mass movement, but a significant number of people are shifting their money around"

At 52, he says he figured out "what's going on." He'd earned money through his business selling beer steins and jewelry in Munich's city center. But he became convinced that he'd actually lost money through his savings efforts and cancelled his insurance policies, while the small interest earnings from his remaining savings accounts were "eaten up by inflation," he says. To fight back, Herrmann formed the BDS. Now he makes appearances around the country, warning of "money-destroying instruments." He's certain that saving is "state-sanctioned robbery."

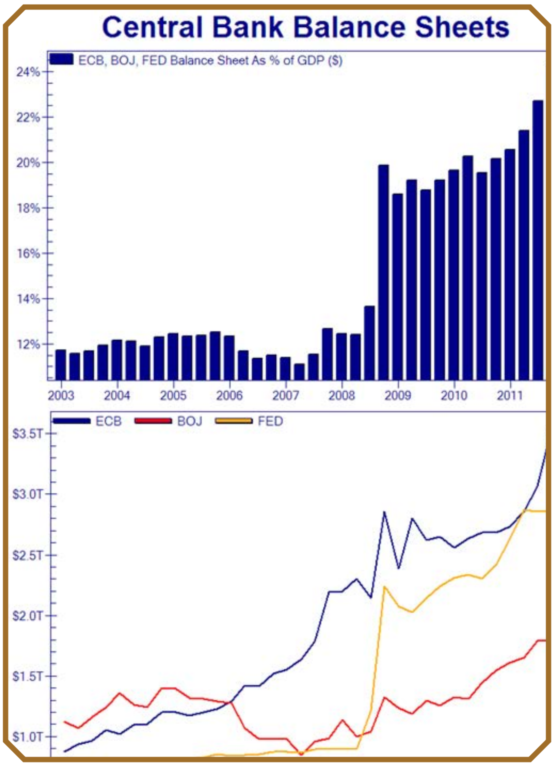
Becoming poorer by saving? As radical as Herrmann's perspective may sound, a growing number of people share his mistrust. They no longer believe in the rates of return promised by the financial industry, while savings and fixed deposit accounts yield pathetic interest earnings, and the never-ending euro crisis feeds fears of inflation or even a currency devaluation.

Surveys by the polling institutes TNA Infratest and Allensbach reflect the current crisis of faith in Germany: Nearly half of the respondents now fear inflation, while every second person with a job questions which form of private investment even makes sense anymore.

"People are becoming increasingly cautious about entrusting their hard-earned money to the banks," says Rolf Bürkl of market research institute GfK. It has yet to become a mass movement, but a significant number of people are shifting their money around, cancelling supposedly rock-solid financial products like life insurance. Some two years ago, customers had already begun criticizing the weak returns on such investments, according to Philipp Vorndran, capital market strategist for wealth management company Flossbach von Storch. “Now many people are asking themselves just what kind of products they actually own,” he says.

Instead of trusting German banks, many investors are turning to tried-and-true institutions such as the Hamburg soccer club St. Pauli. Within the span of just four weeks, some 5,000 fans recently bought a total of €6 million ($7.7 million) worth of shares in the club so it could build a new stadium. They were promised 6 percent interest. The club seems like a secure kind of bank to many. After all, it’s been around since 1910 and has survived the many crises that have befallen Germany since then.

DER SPIEGEL / **LINK**



CLICK TO ENLARGE **SOURCE:** JOHN LOHMAN/BLOOMBERG/BOJ

For anyone who still hasn’t grasped the magnitude of the central planning intervention over the past four years, the following two charts should explain it all rather effectively. As the bottom chart shows, currently the central banks of the top three developed world entities: the Eurozone, the US and Japan have balance sheets that amount to roughly $8 trillion. This is more than double the combined total notional in 2007. More importantly, these banks assets (and by implication liabilities, as virtually none of them have any notable capital or equity) combined represent a whopping 25% of their host GDP, which just so happen are virtually all the countries that form the Developed world (with the exception of the UK). Which allows us to conclude several things. First, the rapid expansion in balance sheets was conducted primarily to monetize various assets, in the process lifting stock markets, but just as importantly, to find a natural buyer of sovereign paper (in the case of the Fed) and/or guarantee and backstop the existence of banks which could then in turn purchase sovereign debt on their own balance sheet (monetization once removed coupled with outright sterilized asset purchases as is the case of the ECB). And in this day and age of failed economic experiments when a dollar of debt buys just less than a dollar of GDP (there is a reason why the 100% debt/GDP barrier is so informative), it also means that central banks now implicitly account for up to 25% of developed world GDP!

What does this mean? It means that nearly $8 trillion in world economic growth is artificial and exists only courtesy of central bank intervention - if one is looking for the reason why there is no mean reversion to a more stable period of time, there’s your answer. It also means that central banks will never unwind their “assets”, either actively, or passively, by letting them mature, as doing so would effectively mean an accelerated return to a non pro forma status quo, one in which global GDP suddenly finds itself $8 trillion less. It also means that in this age of ongoing consumer and corporate deleveraging, central banks will have no choice but to continue monetizing not to generate incremental growth, but to offset debt destruction elsewhere. And of course, in order to sustain global GDP growth of ~3%, they will have to print even more, in other words, accrue more liabilities (excess reserves) which of course would be funded by monetizing even more paper issuance (which Congress would be delighted to oblige with). Which is why we find the announcement by the Fed that it will notify in advance what the Fed Funds rate will be, to be beyond humorous: after all in an environment of active monetization, the only possible interest rate is zero (although the ECB tried a brief experiment otherwise, when it held higher rates than 1% to combat inflation even as it tried, unsuccessfully, to create a debt monetizing off balance sheet vehicle- the EFSF and the ESM).

★ ★ ★ *ZEROHEDGE* / **LINK**

The ayatollahs' growing armoury is dwarfed by that of the United States. But any attempt to close the oil lanes is likely to lead to a major conflict.

"... Oil revenues make up around 80 per cent of Iran's foreign currency earnings. The rial, Iran's currency, fell 12 per cent this week after it emerged that all 27 members of the European Union had agreed to implement a complete ban on oil shipments from Iran. Overall, the rial has fallen 40 per cent in value in the past month."

The last time Iran tried to close the Strait of Hormuz, the trade artery linking the oil-rich Gulf states to the outside world, the Revolutionary Guards had only a few rubber dinghies and primitive mines to achieve their goals. Next time, they will be far better prepared.

For the ayatollahs, the Strait of Hormuz, which lies between Iran and the tiny sheikdoms of the Gulf, has become a national obsession in their long-standing confrontation with the West. They know that, for all their long-held nuclear ambitions, they will never be able to match America's military supremacy. Even if they were to develop the know-how to fit a nuclear warhead to a ballistic missile, the odds are that the weapon would be shot down the moment it left its launch pad by one of the hundreds of anti-missile batteries the US has deployed around the Gulf region in anticipation of just such an eventuality.

So far as the ayatollahs are concerned, a far more effective way of attacking the West would be to place a stranglehold on their economies. As General Sir David Richards, the head of Britain's Armed Forces, commented at the end of last year, that the biggest threat facing Britain is the parlous state of its economy. And the economies of Britain and the other major developed powers would be thrown into chaos if the Iranians carried out their threat to close the Strait of Hormuz.

The free and uninterrupted passage of trade through this narrow passage of water is comparable to the importance of the English Channel in sustaining the prosperity of Europe, a status that is enshrined in the United Nations Convention on the Law of the Sea. On average, 14 crude oil tankers pass through the Strait each day carrying an estimated 17 million barrels, more than a third of the world's seaborne oil shipments. In addition, it has become a vital conduit for tankers carrying liquefied natural gas from states such as Qatar, as the Western economies become ever more dependent on gas for their energy needs.

At a time when tensions over Iran's nuclear programme are reaching crisis point, it was almost inevitable that Tehran should start making ominous noises about closing the Strait if the US and its European allies follow through on their threat to impose wide-ranging sanctions on Iran's oil industry.

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★ ★ ★ *UK DAILY TELEGRAPH* / **LINK**

CLICK TO ENLARGE **SOURCE: CASEY RESEARCH**

In spite of some short-term fixes, there remains no real resolution to the sovereign debt issues in many European countries. We're certainly not spending less money in the US, and now we're bailing out Europe via currency swaps with the European Central Bank. Shouldn't gold be rising?

Yes, but nothing happens in a vacuum. There are some simple explanations as to why gold remains in a funk.

The MF Global bankruptcy, the seventh-largest in US history, forced a high degree of liquidation of commodities futures contracts, including gold. Many institutional investors had to sell whether they wanted to or not. This is similar to why big declines in the stock market can force funds and other large investors to sell some gold to raise cash for margin calls or meet redemption requests.

The dollar has been rising. Money fleeing the Eurozone has to go somewhere, and some of it is heading into US bonds, which means first converting the foreign currency into dollars.

It's tax-loss selling season, something that's also impacting gold stocks. Funds and individual investors are selling underwater positions for tax purposes. Funds also sell their big winners to lock in gains for the year and dress up quarterly reports.

These forces have all acted to depress the gold price.

Notice I didn't say that gold has suddenly become viewed as a poor safe haven. Nor that many of the world's major currencies are no longer being debased... nor that global sovereign debt issues are resolved... nor that interest rates are positive. No, the fundamental reasons for owning gold are still intact. So don't let the selling depress you.

Let's put gold's recent price action into perspective. It peaked on September 5 at $1,895 (London PM Fix) and has thus been in decline for about three months. Yet look at the bull market's biggest three-month correction in relationship to the ultimate trend.

JEFF CLARK / **LINK**

Many Americans have strong opinions about policy issues shaping the presidential campaign, from immigration to Social Security. But their grasp of numbers that underlie those issues can be tenuous.

Americans vastly overestimate the percentage of fellow residents who are foreign-born, by more than a factor of two, and the percentage who are in the country illegally, by a factor of six or seven. They overestimate spending on foreign aid by a factor of 25, according to a 2010 survey. And more than two-thirds of those who responded to a 2010 Zogby online poll underestimated the part of the federal budget that goes to Social Security or Medicare and Medicaid.

"It's pretty apparent that Americans routinely don't know objective facts about the government," says

Joshua Clinton, a political scientist at Vanderbilt University.

Americans' numerical misapprehension can be traced to a range of factors, including where they live, the news they consume, the political rhetoric they hear and even the challenges of numbers themselves. And it isn't even clear how much this matters: Telling people the right numbers often doesn't change their views.

This isn't exclusively an American problem. Estimates by people in the U.K., Italy and France of immigrant populations in their nation miss by a bigger percentage than do Americans' estimates, and Britons overstated the magnitude of U.K. net contributions to the European Union by more than 100 times in a 2010 survey.

Some of these findings may show simply that people don't have a good grasp on very small or large numbers. Take a poll last year that found Americans overestimated federal spending on the Corporation for Public Broadcasting by a factor of at least 100. Arthur Lupia, a political scientist at the University of Michigan, says while Americans were far off the mark, the average response of 1% to 5% signals "that lots of people know that the amount spent is a small number." CPB was budgeted $430 million last year, 0.01% of federal outlays.

"Numbers are hard," says Ellen Peters, a psychologist at Ohio State University. "They're difficult to evaluate and remember because they're abstract symbols," and their meaning shifts depending on the context. And absorbing policy numbers may not be worth the effort: "People are more likely to remember numbers accurately when that information is more valuable to them," Ms. Peters says.

WSJ / **LINK**

Retailers salvaged their December sales figures with deep discounts, but the results released Thursday could spell trouble for the coming year for both the industry and the economy at large.

Sales at stores open at least a year at major retail chains rose 3.4 percent compared with December 2010, according to data compiled by Thomson Reuters, just above the 3.3 percent that analysts had expected.

But the cost of propping up sales was high. Profits "were a mess" for many retailers, said Paul Lejuez, an analyst at Nomura Equity Research. Consumers were buying less than retailers had expected, and stores had to mark down inventory to get it out the door by Christmas.

SALES

Results are for the five weeks that ended Dec. 31, except as noted, compared with the period a year earlier.

COMPANIES	TOTAL SALES, IN BILLIONS	CHANGE	CHANGE IN SAME-STORE SALES
Wal-Mart *releases its sales figures quarterly*			
Target	$10.1	+ 2.6%	+ 1.6%
Costco* *5 weeks to Jan. 1*	10.1	+ 9	+ 7
Macy's	4.9	+ 6.6	+ 6.2
TJX*	3.3	+ 8	+ 8
Kohl's	3.2	+ 1.7	– 0.1
J.C. Penney	2.9	– 2.3	+ 0.3
Gap*	2.0	– 1	– 4

CLICK TO ENLARGE **SOURCE:** NYT

The results show the American consumer has not bounced back from the recession, analysts said. Consumer spending accounts for the largest portion of the economy. But the shaky holiday results add to an already weak snapshot of the consumer situation, including flat incomes and a slow job market.

"Retailers came in with pretty conservative assumptions, and they were hoping to blow them out of the water — they really didn't," said David L. Bassuk, managing director and head of the retail practice at AlixPartners, a consulting firm. Retailers were resorting to promotions like " '50 percent off our whole store,' '60 percent off our whole store,' which is when you can see times are tough," he said.

With too much supply and limited demand from consumers, "there's not enough room for all the retailers of old," he said. The new year would probably bring "closing of stores and, I think, closing of retailers," he said, adding, "It's a more dire situation than many had anticipated."

Chains including Target, Kohl's and J. C. Penney lowered their fourth-quarter profit expectations on Thursday, saying they had to discount items to entice shoppers in December.

Craig Johnson, president of Customer Growth Partners, said he believed those companies were affected by the good performance at Macy's. Same-store sales at the company were up 6.2 percent, above analysts' expectations, and the company said Thursday that both same-store sales and profit for the quarter should be higher than expected. Macy's now forecasts fourth-quarter profit to be $1.55 to $1.60 a share, up from $1.52 to $1.57 a share.

Walmart, the nation's biggest retailer, does not report monthly same-store sales. During the recession, it benefited from a trading-down effect — people who shopped at Target would switch to Walmart — but analysts said they did not believe that explained the problems at Target, Kohl's and J. C. Penney now. "Keep in mind, sales were O.K.," Mr. Lejuez said; the problem was profits.

NYT / **LINK**

Amid global economic uncertainty, People's Bank of China Governor Zhou Xiaochuan is one of the world's most talked-about central bankers.

Zhou attracts as much attention as U.S. Federal Reserve Chairman Ben Bernanke and European Central Bank President Mario Draghi because the world's financial markets are vitally interested in China's interest rate trends, bank deposit reserve ratio adjustments, and yuan-dollar exchange rates.

"... the international economy is changing rapidly, and its outlook remains uncertain. Thus, we must be prepared to respond to new situations."

Zhou is a big-thinking strategist with firm ideas about financial reform. He's also a tactician who can find opportunities for promoting reform in any situation. His harmoniously pursues realism and idealism, seeking gradual progress while pushing for financial reform.

The year 2011 was difficult and complex for China' economy. The year 2012 will be no different. What does Zhou see ahead, and what lessons can be learned from the past year?

In an interview in December, shortly after the Chinese government set its 2012 policy goals at the annual Central Economic Work Conference in Beijing, Zhou sat down with Caixin to discuss his personal and the central bank's views toward inflation and monetary policy adjustments, interest rate control, exchange rate reform, capital account liberalization and the internationalization of the yuan. His comments follow:

Caixin: China's macro-economic policies were adapted to fit changing economic situations in 2011. How do you see the economic situation in 2012 and corresponding policy options?

Zhou Xiaochuan: The Central Economic Work Conference clearly articulated macro-economic policy, taking into account two considerations: Efforts to prevent an economic downturn, and efforts to restrain inflation.

First, we are encountering concurrent issues in the international arena, including an evolving European debt crisis, U.S. economic uncertainty, and slowing growth in emerging economies. More importantly, the international economy is changing rapidly, and its outlook remains uncertain. Thus, we must be prepared to respond to new situations.

On the other hand, looking at China's domestic economy, local governments will have leadership reshuffles in 2012 and the capacity for growth in the Chinese economy is still great. At the same time, the consumer price situation has changed for the better, and the need to control inflation is not as pressing as it was in early 2011. Of course, there are still uncertain factors, such as the impact that the real estate market will have on the national economy.

Overall, we need to plan for the worst external environment without relaxing efforts to keep prices from rising too quickly. We need to rationally manage inflationary expectations. Meanwhile, economic structural adjustment is still a difficult task. Macro-economic policymakers need to weigh all these issues.

★ ★ ★ *CAIXIN* / **LINK**

We are used to countries like Argentina having their problems. But in the 1990s we saw what happened to both Canada and Sweden as they had to deal with that lack of confidence. While they had different answers, they came through their respective crises, although there were clearly economic costs, higher unemployment, losses, and very difficult decisions made. It is not just "banana republics" that have debt problems.

Only a few years ago, European regulators were allowing European banks to leverage as much as 40 to 1, gorging themselves on sovereign debt, because everyone "knew" that sovereign nations in a modern world would not – indeed could not! – default; so why worry about leverage on government debt? Until Greece and then Ireland and then Portugal and now Italy, etc. I was writing early last year that Greek bonds would lose 90% of their value. This week we read that Greece indeed wants private investors to agree to a 90% write-off. Soon it will be public bond holders like the ECB that will take haircuts.

"... No country starts borrowing money with the thought that they will keep on borrowing until there is an economic collapse. It all starts with good intentions"

No country starts borrowing money with the thought that they will keep on borrowing until there is an economic collapse. It all starts with good intentions. No bank lends money not expecting to have it returned. Then things change over time. Since there seemed to be no problem with the current level of debt (and spending), why can't we increase it a little more?

There are countries that can keep their budgets and debt under control (like Switzerland and others). But politicians like to promise benefits today and pay for them with debt that future generations must incur (like the US and countries all over Europe). Or they try to spend their way to prosperity and growth (like Japan).

And of course they promise that "in the very near future" they will get the deficits under control. "We will grow our way out of the problem. We will limit the growth of spending next year, when the economy is better. We can always raise taxes on the rich. Or increase consumption taxes. Or create some taxes somewhere." Whatever it takes to convince the bond market to keep on funding their spending.

And so the choices to provide this benefit and that program, each justified by some reason and desired by some group of voters, add up over time. Everything goes well until there is a recession. Then revenues go down and costs go up, because unemployment benefits rise. But because the natural business cycle leads to recovery and growth, things soon get better and the game continues.

But then the accumulated debt becomes too much to handle when the next recession comes along. And bond investors lose confidence and the Bang Moment has arrived. Cochrane shows that there is no magic number or formula, no way to know in advance when that moment will be. Unless a country chooses to deal with the pain of cutting spending and raising revenues, eventually there is a true crisis, resulting in massive dislocations and losses. Bond holders lose a large percentage (if not all) of their investments. That moment is often precipitated by a credit or banking crisis. And when the banking system freezes up, businesses lose access to capital, and the recession can turn into a depression if not dealt with aggressively. But that means pain.

★ ★ ★ *JOHN MAULDIN* / **LINK**

The idea that the troubled eurozone could collapse is "complete fantasy" according to a policymaker at the European Central Bank (ECB).

Luc Coene, a Governing Council member at the ECB, said that even if Greece was to leave the euro, Europe would unite to protect the system.

"If the Greeks decide to leave, something that seems to me to be completely inconceivable ... Europe will certainly stand shoulder to shoulder to protect the system," he told the newspaper La Libre Belgique.

"...I think that, for the moment, we are starting to have control over the situation,"

Mr Coene said that Europe was starting to take control of its budget deficits, but that it would take time to see how effective the austerity measures put in place would be.

"I think that, for the moment, we are starting to have control over the situation," he said.

"Now we need a bit of time to see what is the degree of success that all of these plans will have."

He added that investors would be cheered when they saw action to control budgets taking effect, and start to finance countries again.

"Once we see that the results are there, markets will be reassured and will finance countries," said Mr Coene, who is also the Governor of Belgium's central bank.

He dismissed the idea that the ECB should intervene by directly buying government bonds, arguing that it would not be a solution to the crisis and would require the central bank to take on a lot of political risk.

His comments came after the International Monetary Fund's chief economist said that banks exposed to Greek debt could be forced to take bigger writedowns because of the country's worse-than-expected finances.

★ ★ ★ *UK DAILY TELEGRAPH* / **LINK**

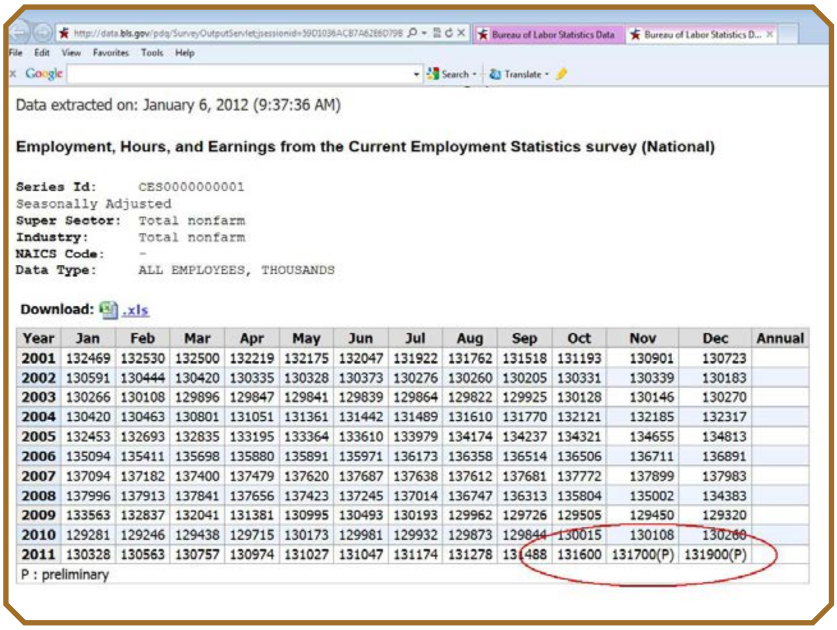
The wonderful Richard Ross of Auerback Grayson on the euro:

rross@agco.com

I did not write something about this, but I do wish to point out something new. The BLS has always rounded the headline number of course, but now they are starting to round the 'raw number' as shown in the first picture below. That I have never seen before.

Considering that the headline number these days is around a couple hundred thousand, rounding the raw number to the nearest hundred thousand is almost bizarre.

★ ★ ★ *JESSE* / **LINK**



Data extracted on: January 6, 2012 (9:37:36 AM)

Employment, Hours, and Earnings from the Current Employment Statistics survey (National)

Series Id: CES0000000001
Seasonally Adjusted
Super Sector: Total nonfarm
Industry: Total nonfarm
NAICS Code: -
Data Type: ALL EMPLOYEES, THOUSANDS

Download: .xls

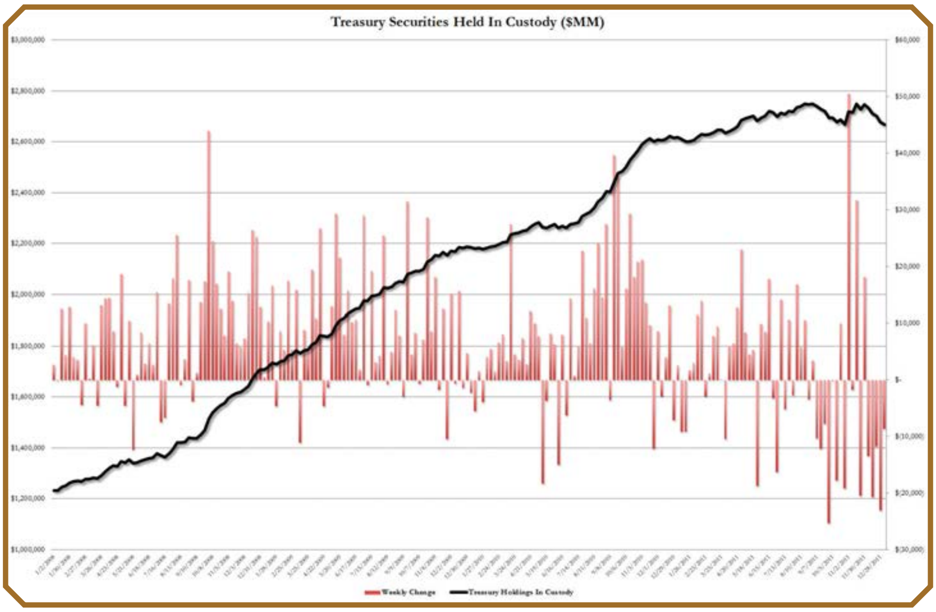
Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
2001	132469	132530	132500	132219	132175	132047	131922	131762	131518	131193	130901	130723	
2002	130591	130444	130420	130335	130328	130373	130276	130260	130205	130331	130339	130183	
2003	130266	130108	129896	129847	129841	129839	129864	129822	129925	130128	130146	130270	
2004	130420	130463	130801	131051	131361	131442	131489	131610	131770	132121	132185	132317	
2005	132453	132693	132835	133195	133364	133610	133979	134174	134237	134321	134655	134813	
2006	135094	135411	135698	135880	135891	135971	136173	136358	136514	136506	136711	136891	
2007	137094	137182	137400	137479	137620	137687	137638	137612	137681	137772	137899	137983	
2008	137996	137913	137841	137656	137423	137245	137014	136747	136313	135804	135002	134383	
2009	133563	132837	132041	131381	130995	130493	130193	129962	129726	129505	129450	129320	
2010	129281	129246	129438	129715	130173	129981	129932	129873	129844	130015	130108	130260	
2011	130328	130563	130757	130974	131027	131047	131174	131278	131488	131600	131700(P)	131900(P)	

P : preliminary

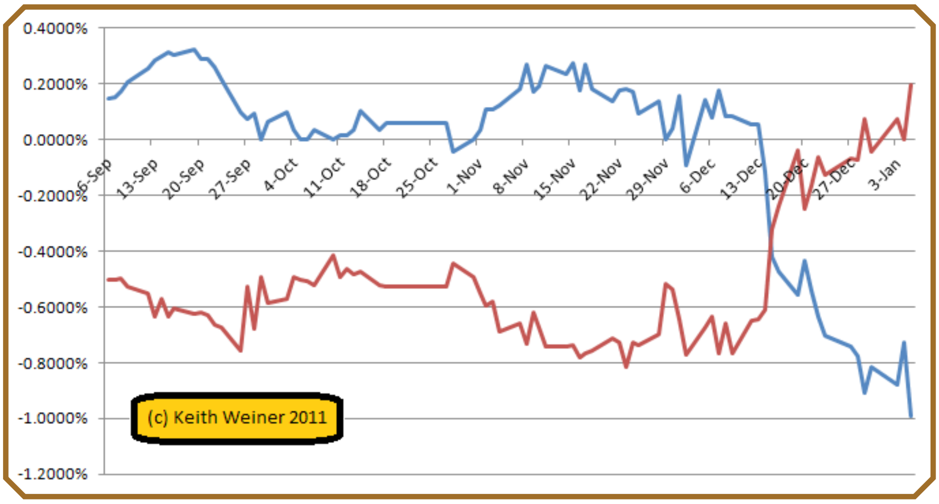
CLICK TO ENLARGE **SOURCE:** JESSE'S CAFE AMERICAIN

While there were few nuggets worth mentioning in yesterday's H.4.1 update, one item is certainly worth noting. After we pointed out last week when we noted that there was a record monthly dump of Treasury paper from the Fed's custodial account amounting to some $69 billion, the week ended January 4 has seen yet another outflow, this time amounting to $9 billion in US Treasurys. This is the 5th week in a row of foreigners selling US paper, and while it has yet to match the record 6 weeks of outflows from October, the consolidated outflow notional is now a record high at $77 bilion, higher than the previous record of $52 billion. Needless to say banks from around the world are repatriating dollars. The question is what they are converting the USD into, and how much longer will the go on for: the last thin the US can afford is a wholesale dumping of its Treasurys. Because as the chart below vividly demonstrates, the traditional diagonal rise in foreign holdings of US paper has not only pleateaued, but it is in fact declining: a first in the history of the post-globalization world.

★ ★ ★ *ZEROHEDGE* / **LINK**



CLICK TO ENLARGE **SOURCE:** ZEROHEDGE



CLICK TO ENLARGE

SOURCE: KEITH WEINER

Absent a shortage or other anomaly, the March [silver] price should be close to the spot price + the cost of carry (interest rate and storage). March silver should be at a slight premium to spot silver. This condition is normal, and it is called "contango".

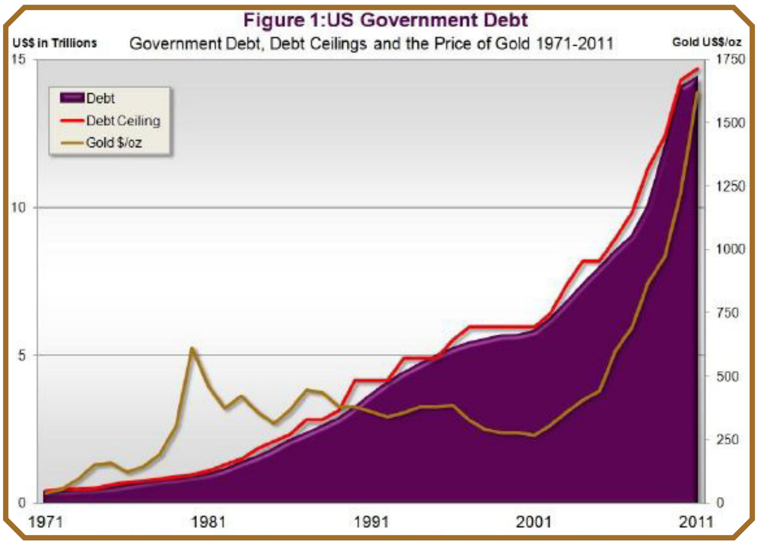
But that is not the case for March silver (or Jul 2013 and beyond). Those contracts are priced too low for anyone to make any money carrying silver. Instead, it would be profitable to de-carry silver. See the graph for a picture of the basis (the annualized profit one would make to carry) and the cobasis (the profit to de-carry). The basis is negative and falling; the cobasis is positive and rising.

A de-carry is the inverse of a carry. One simultaneously sells silver, and buys a future against it. Silver (and gold) are unlike all other commodities in that the above-ground inventories are massive, compared to annual mine production. Whereas in wheat, for example, there is a genuine shortage before the harvest. If one wants to buy wheat two weeks prior, one must pay a large premium compared to the first contract settled after the harvest.

In a normal commodity, backwardation means shortage. The backwardation develops because no one has any of the physical good. So they cannot decarry it, and thus the spot-future spread can go deeper and deeper into backwardation.

But in gold and silver it means something else entirely. People have the metal. But for whatever reason(s), they choose not to take this free money. In the silver market right now, trust is in short supply. In the past (think fall 2010 through spring 2011), this has been resolved by sharply rising prices which coax fresh metal out of hiding.

DAILY CAPITALIST / LINK



SOURCE: TREASURYDIRECT/IACONO

Now, here are few data series that I've never seen on the same chart before – U.S. debt, the debt ceiling (just for fun, apparently), and the price of gold. This is from a presentation yesterday by Nick Barisheff, President & CEO of Bullion Management Group, at the 2012 Empire Club of Canada Investment Outlook Luncheon.

Perhaps today, gold is acting more like a hedge against debt than inflation...

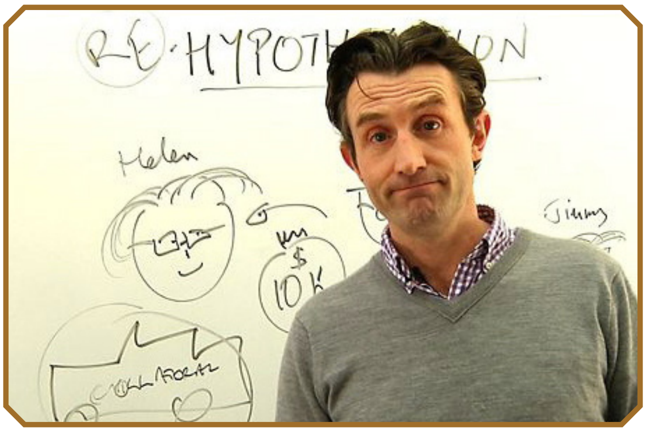
TIM IACONO / LINK

A real treat today as two of the greats, Jim Puplava and Martin Armstrong, spend time discussing the roadmap for 2012. Needless to say, Martin is concerned and sees capital controls as an inevitable consequence of policy and he has some interesting views on the likely trajectory of gold. As always, Martin gives a truly fascinating interview:

CLICK TO LISTEN

"This is exactly how Rome collapsed. There was a Roman Emperor, Maximinus in 238 [AD], he simply declared all wealth in the Roman Empire to be his. That's it. And, what happened, is that, and what you're going to see over the next few years, as you attack the rich, as the Romans did, what happens is that, somebody now hoards their money. They no longer invest it, they hide it, and they don't keep it in banks. And consequently, that reduces the velocity of money. And as it reduces the velocity that is what creates the economic decline. So that interest rates, even during the Great Depression, fell to 1%, nobody would borrow because they didn't see an opportunity to make money. And every possible mistake that every government has made before us, we are following step by step."

Confused about Rehypothecation after the MF Global debacle? No need to be. Let Paddy Hirsch take all the mystery out of it with the aid of his trusty whiteboard...



CLICK TO WATCH

CLICK TO LISTEN

Finally today, yes, I'm afraid he's back.

This week I had the pleasure of talking to Dr. Jeff Lewis out in San Francisco about the origins of this newsletter, the outlook for 2012 and the pitfalls of allowing your emotions anywhere near your silver trading...

I've had this video sent to me by two friends recently (thanks Mike and Bob) and here, in stunning HD, it is absolutely extraordinary.

We really are, as a good friend of mine is wont to say, clever little apes...

Enjoy.

Hmmm…

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