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# The Rising Frustration



With The

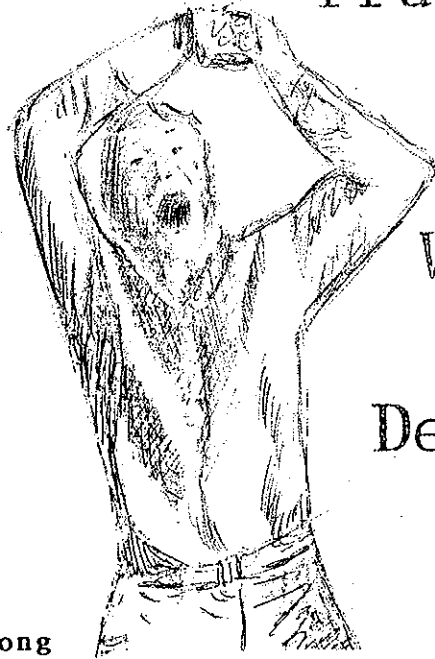
Debt

Crisis

Martin A. Armstrong  
Former Chairman of Princeton Economics International, Ltd.

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# The Rising Frustration



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By: Martin A. Armstrong

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**T** IS the season of discontent rather than to be jolly. We are in such dire circumstances that nobody will be able to put Humpty Dumpty back together again. If you simply take the total US National Debt since 1940, it has risen to \$11.9 trillion by 2009 of which \$8.161 trillion has been interest expenditures. The total amount of interest paid out since 1940 accounts for 68% of the total national debt. This is truly a staggering number that is beyond contemplation. It is what currently drives all the markets and has sent the talking heads talking in circles. But the government can censor whatever it desires. It can imprison every dissident it can find and claim they were tax-cheats or some other accusation to justify turning them into criminals to pretend it is not a political imprisonment. But, the Emperor has no Clothes. Mahatma Gandhi (1869-1948) remarked on such outrageous tyrants. He said first they ignore you. Then they laugh at you, Third they then fight you. And fourth, then and only then can you defeat them. The government of the United States has ignored the warning of a debt crisis. They then tried to call anyone pointing out the crisis a nut case and laughed at them. When the "nuts" gain credibility, they then are accused of something to imprison them. And then and only then, does the inevitable unfold.

We are rapidly crossing that point of no return. Nobody will be able to put Humpty Dumpty back together again. The government turns to the NY Bankers for advice. That is like a drug addict going to the drug dealers to ask advice if he should stop taking drugs. When the NY bankers are PRIMARY dealers who sell the debt, THEY CANNOT GIVE ANY ADVICE ON THE SUBJECT OF DEBT! So we are in a truly hopeless death spiral and there is nobody to call and say help! Fix it!

History buries empires, nations, and cities all in a common grave. So many have fallen thanks to an irresponsible debt crisis it is hard to list all the failures. Some are indeed memorable. For it is not some magical cycle that causes the mass burials, but that the passions of man never change and thus we find that history repeats because government is ALWAYS and without EXCEPTION corrupted to the point that government always dies by its own hand.

One of the best examples from this long history of common graves in which empires, nations, and cities are buried demonstrating that DEBT alone can destroy a government is from the city of Mainz. It was the excessive debt and the incompetent management of the government that destroyed the city.

The parallel of our current Public Debt Crisis has often been drawn to Rome. But the comparisons are similar only to a point. It was the incompetence of the management of the government, the squandering of public resources, and the excessive taxation that truly undermined Rome as an empire. Yet there was the evolution from a CONQUEST economic model whereas the state gained economic benefit by conquering another and taking all its gold. That CONQUEST model collapsed when they ran out of new countries to conquer. Then Rome turned inward against its own people taxing them to the point of driving industry and capital out of Rome. We have followed that course of events, but we have not yet been confronted by the barbarians at the gate that leads to massive military expenditures to the point that at the time of Constantine, it was said that there were more government people than there were tax payers.

That is the real key that ultimately brings down the house of cards and this is the crisis of which I have focused upon that is creating the DEBT CRISIS. It was the very government employees rioting in Greece. It was trying to push the retirement back by 2 years in France that led to the riots. Now there are serious issues arising in Britain that will soon be felt in the USA.

The political collapse of Mainz is a clean example of the crisis in debt that we face today. The city of Mainz had gained its rights to be self-governing in 1118. It had become a free city in 1244. But the corrupt management of the city was pervasive. From about 1332 onwards, the trade guilds (unions) became deeply involved in managing the government that managed to stem the tide of any economic crisis until 1411.

Mainz was the birthplace of printing in Western Europe - Johannes Gutenberg who had invented movable type for printing about 1440 and this period had been known as the Age of "Golden Mainz" fueled largely by debt and the good times.

To have funded the city's Golden Age and its freedom, it was building a national debt with perpetual deficits year after year. The debt crisis that was brewing was truly massive. From the outside looking in, Mainz was the symbol of wealth. It was the envy of all and it appeared to be the land of milk and honey.

However, in 1411, the cracks in the looking-glass began to appear. The debt crisis was multiplying like a virus in a lab dish. Taxes were now rising and a political upheaval was in motion. The payments on its debt reached a crisis point and 48% of the expenditure now went to interest to roll the debt.

In 1411, there was a popular uprising that now forbade the sale of any more debt without the consent of the trade guilds. Yet, the financial conditions continued to worsen. By 1436-1437, about 75% of the total city expenditure was now being consumed by interest.

Interest rates began to rise as there were subtle fears that Mainz might not be able to pay its debts. The interest rates climbed to find buyers for their debt. The interest rates jumped from 3% to 5% during the 1430s.

By 1444, the total debt of the city of Mainz had now reached 373,184 gulden. The amount of money owed was truly staggering for a city. In 1448, the city tried to sell just 21,000 gulden to rollover debt coming due. There was NO BID!

The crisis that hit showed that 60% of its debt was held by people outside of the city - foreign debt holders. The city was forced to default and the fun just began. Because of this high external debt, the city lost its independence. Mainz was now seized and placed under an imperial ban by the Holy Roman Empire. The Pope excommunicated the city for being a borrower under the Sin of Usury.

The rich fled the city, which began prior to the bankruptcy. They held their capital and wealth outside of Mainz just as capital remains offshore today because of taxes. Deserted by the rich, the city became impoverished, it was captured and then set on fire for retribution.

I have tried to explain the REAL issues of how markets actually move. It is hard at times to overcome the misconceptions that are propagated by those who wish to comment on historical events without doing the full research to comprehend what actually takes place.

The Great Depression is the classic example of misconception. To a fish in a curved bowl, his view of reality will be distorted according to the curve of the bowl. It will be like a fun-house mirror that makes you look weird.

The problem that we face is always one of perspective. If you analyze everything from a US perspective, you cannot see what the rest of the world sees. We are always hampered by our biased perspective.

What I have learned has not been from some text book. It is not from watching TV. I was trained by my clients that just so happened to be worldwide. I ran as a globe trotter giving workshops & seminars, and in meetings on every continent. Because I did not lecture, but had to listen to solve the problems presented to me by clients, I saw the world in their eyes.

The models we constructed were global. Every aspect had to be remapped to the then currency in question. It made no sense for a client to pay me for an opinion that the Dow would rise 20% and advise that they then should jump-in with both feet, only to then ignore the fact that the dollar would drop by 40% against their particular currency. I could pretend to be right, but they would lose everything.

It was essential to be able to run the models on a global perspective that would then show the real trends. The CFTC in particular hated Princeton Economics. Their absurd view was I was manipulating the world economy. Trying to reveal the truth in the face of such nasty morons was not important. They felt that since we advised on over \$3 trillion when the US National debt was \$6 trillion, was somehow manipulating the world economy even though this had nothing to do with trading, but strategic survival.

I suppose the CFTC thinks if everyone is as stupid as they are, then somehow the world will be better off. If there was anyone who manipulated the world economy it was none other than their mentor - Karl Marx who hated the free markets about as much as regulators.

If it were not for Marx who said taking all the toys away from the "rich" and handing them to government employees would solve the problem, we would not be in this crisis for the West also embraced Marx. The communists took all property while socialists left you with the title, regulated it, taxed it and accomplished the same ends. Marx inspired all regulation and unions. It was all Marxism at the center of everything since the 1890s. Just 3 years after the Sherman Antitrust Act, the Panic of 1893 hit and the US was broke by 1896.

All the so called "Free" nations are followers of Marx who was the most influential of all economists ever to write on the subject. NOBODY - but NOBODY has ever manipulated the world economy other than Marx. There is no government that did not embrace his ideas of socialism and to the extreme communism. When Russia and China seized all property, the West did the same allowing private ownership, but they regulated what you could do and took the majority of any capital gains both long-term and short. And when you died, they took it all again. And they said you were free and they were not Marxists. Ya! And I am somehow still manipulating the world economy from here. If I were, we would not have had a real estate bubble.

The greatest problem we face is the lack of true comprehension about how things work. Take the stock market to ZERO, and it will not create a depression. Wipe out real estate, you wipe out everything for people believed this was their savings. Mortgages were about 74% of total consumer debt. Wipe out the debt markets, and you get Mainz.

It is a delicate mix of the level of debt, the interest rate, the distribution between domestic and foreign holders, and the percent of total expenditure that is unfunded compared to the tax rate. Putting this all together globally reveals the big winner and losers.

The debt crisis in Europe is far from over and as the Wall Street Journal reported on November 10th, 2010, Ireland tied its fate to the banks. The debt crisis reported before placed the damage at 50 billion euro, or as the Journal stated "nearly \$50,000 for every household in the Emerald Isle." Id./p1

I was called in on many different crisis events. When Citibank got in trouble over the mortgages in other lands (including Australia) many foreign offices wanted me to meet at a global summoning of all Citibank offices that were around the world. It was going to be held in South East Asia. Their mortgage crisis was caused by foreign exchange. New York at the last minute refused to call me rejecting the requests of Europe and Asia insisting that they did not want to air their dirty laundry before Princeton Economics.

The point is this. The bankers are FAR from experts on the world economy any more than I am an expert of lending money for mortgages or brain surgery. We are all best in fields we have spent time. But when the bankers do not understand the global economy or how markets actually develop, rise, bubble, and crash, why do governments constantly call these people who pretend to give advice and couldn't get it right in the middle of a dream. They still would screw everything up even when it is their own dream.

Ireland is hit hard by the incompetent banking system that is by far NOT limited to Ireland. Even Goldman Sachs had to be bailed out and borrowed from Buffett to survive. Yet people will listen to bankers and hang on their every word as if they know what the hell they are really doing anyway.

Ireland is imploding. I have received numerous letters from Ireland asking if I could help. The answer to save Ireland exists. But they have to be ready for a new way of doing things to save the country.

Ireland is in a debt crisis implosion that is being caused by the massive bad loans and leverage the banks got themselves into, and that suppresses the real estate market which in turn creates the economic decline and that cuts into the tax revenue that then forces a reduction in government. We are watching these dynamic forces feed into each other.

There are ways to deal with this crisis but they are going to require dramatic and profound change. I wrote before, that I see a possibility for Britain and Ireland to be the first to reform. I stand ready to help when they are serious about saving their people from disaster. Until then I must keep my mouth shut on the how details.

This is not a simple liquidity crisis. If it was just that simple. Pouring trillions into the banks was the WRONG move and has been like passing a law that fines the wife if she fails to force her husband to take out the trash. The banks were the FIRST blush of the problem, but that was the least of it. You cannot save the banks and the nation without understanding the real crisis.

The fate of the Irish banks will still be shared by others. We are in a CONTAGION crisis. As the banks foreclose, they depress the real estate, that depresses consumer spending when they fear their savings are gone, and that depresses revenues for the government and forces higher taxes, lower economic growth, and increasing the odds of political upheavals, revolutions, and war. WE HAVE TO BREAK THE CYCLE OF THIS CONTAGION IN A REAL AND PRACTICAL MANNER THAT IS NOT BASED UPON SMOKE & MIRRORS!

On the one hand, you have people now blaming the mortgaged property owner and argue they have to be forced out or the real estate market will never come back. So go ahead. Throw everyone out on the street and throw 40% of the houses up for sale and watch what happens. The depression will be massive! Real Estate is dead for 26 years from 2007. There will be some rallies, but the game is over. They created the 30 year mortgage to restart the real estate market back during the Depression. How do you expect to do that now without any such tool?

This is more than just forcing people out of the homes and selling them for scraps. You are ASSUMING that people will jump back in and housing will rise in price as soon as that gut is gone at any price. The NASDAQ bubble was 2000. The market did not come back yet. Ain't gona happen! So either we face the reality of a COMPLETELY new economic model or we hang up everything now.