Davos, Debt & Systemic Failure
When West Meets East

The preferred diet of most Davos attendees is a fusion inspired composition of individual, government, and corporate debt combined with a free-market frissee of lax regulatory oversight held together by a roux of central bank credit that dissolves instantly when paired with matching counter-party risk.

The January 2008 gathering in Davos, Switzerland at the World Economic Forum is similar to the 1957 meeting in Palermo, Sicily of American and Sicilian Cosa Nostra crime families who met to discuss mutual problems and opportunities. The notable difference being that those in the Cosa Nostra live outside the law; while those at the World Economic Forum in Davos make them.

Those in Davos, however, share with the Cosa Nostra a common problem—the success of both depends on inherently unstable systems. The Cosa Nostra model is based on violence and greed which is both its strength and weakness. Capitalism, the source of wealth for those in Davos, is based on greed and leveraged debt, a combination as powerful and effective as the system of the Cosa Nostra—and just as unstable.

WHEN SYSTEMS FAIL

Unstable systems can function for years without serious problems. But over time, unstable systems will always break down. We are witness to such a systemic failure today. Global credit markets are slowing and contracting. The capitalist system responsible for economic expansion and wealth is in disarray.

Debt, in capitalist systems, is a wondrous device. That is, until it can't be paid back. Under capitalism, credit fuels expansion but it does so at a cost. As capitalism expands, credit becomes debt and the greater the expansion, the greater the debt.

EXPANSION BEGETS DEMISE

Capitalism's fatal flaw is apparent only in its later stages. As capitalism matures, its inherent systemic instability manifests. The very expansion of capitalism sets in motion its demise. The Achilles heel of capitalism is its perpetual need to expand.

Only perpetual capital expansion can create sufficient capital flows to service and retire previously created debts, the amounts of which are always increasing because of the accruing compound interest being charged. While any slowdown is cause for worry, a contraction bodes far worse.

FEAR IN DAVOS
WHAT A DIFFERENCE A YEAR MAKES

One year ago, the mood at Davos was one of quiet, almost smug, confidence. The on-going economic expansion appeared to be endless, the profits of investment bankers skimmed off the top of productive enterprise was greater than ever. Private equity, the investment banker’s equivalent of flipping real estate, was the hottest game in town.

It is no longer. Today in Davos, the scent of Armani is now mixed with the acrid smell of anxiety produced by falling markets and uncertain futures. Concern has replaced confidence. The major phernome in Davos today is fear.

World Economic Forum

Davos, Switzerland

By invitation only

Investment Banks
Vultures
Private Equity Funds
Hyenas
Central Bankers
Government Representatives
Other Predators

Guests
The Media
Bond Rating Agencies

WHEN WEST MEETS EAST

A year ago, the confidence of those gathered in Davos was based on the belief that if an economic slowdown occurred, it would be offset by (1) the expansion of Asian economies and (2) the ability of global markets to decouple from slowing American demand. Both assumptions have proved themselves wrong.

The recent expansion of Asia was made possible by the debt-based consumption of American consumers. Now that America's consumers have run out of cash and credit, the economies of Asia—China, India, Japan, Korea, Taiwan, Malaysia, etc. will slow. When capital markets slow, you know what happens; and, if you don't, you soon will.

WHEN CREDIT MEETS SAVINGS

As capitalism expanded from the west to the east, western bankers hoped their success would be repeated. They were wrong. Asians responded to the new paradigm and their new found wealth by saving, not spending.

Western bankers were dismayed by this unexpected reaction. If Asian economies continued to save instead of spend, it would slow the expanding juggernaut of capitalism; and if capital expansion slows, like bicycles, capitalism doesn't do as well at slow speeds.

CHINA AND GOLD

As western bankers run out of markets to exploit, leaving behind tapped out and overextended borrowers, e.g. consumers, governments, corporations etc., it was hoped Asia would provide the new horizon needed for capital markets to expand.

Asia instead will be a conundrum to the west. Not the surrogate state, militarily and economically, that Japan is in danger of becoming, China will prove to be less amenable to the western bankers hoping to economically colonize the last great prize of imperialism's global puzzle.

While Chinese spend, they also, as do most Asians, save. They are currently holding $1.2 trillion in foreign savings—and this ingrained tendency to save will not give western bankers the acceleration they need to keep capital markets expanding as western markets contract.

At Davos, Dominique Strauss-Kahn, the Managing Director of the IMF, urged emerging economies with sound balance sheets to run fiscal deficits in order to offset a slowdown by US consumers. Will Asian economies choose to encumber their balance sheets in order to save the west's capital markets? It is not likely.

Asians, in times of fiscal stress, prefer the safety of gold to credit and debt; and, although gold is no longer viewed as a mainstream investment in the west, gold still retains its traditional appeal in the east:

In Caishikou Department Store, a popular physical gold dealer in Beijing, more than 100 people lined up to purchase bullion for the Lunar Year of the Mouse on Nov. 22, the first trading day of the products. More than 200 kilograms of the gold bars were sold within 1.5 hours. Moreover, the total subscription amounted to two tons.

Xinhua, January 19, 2008

Gold will be the choice of Chinese seeking safety and profit in the coming year. India, another large emerging Asian economy, values gold as much, if not more, than China. This does not bode well for bankers in the west.

Davos will not be the same next year. If you're planning on going, be sure to take some air freshener.

Darryl Robert Schoon
www.survivethecrisis.com
www.drschoon.com

Note: I will be speaking at Gold Standard University Live in Dallas, TX, February 11-17 which is presented by Professor Antal Fekete. This is a unique opportunity to hear Professor Fekete who is an expert on gold and its role in monetary matters. Details are available at www.professorfekete.com .