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What is happening now?

The 'marginal productivity of debt' tells the story of where we are at this time in our economic history. Debt or leverage has some benefits for a time period. Capitalism is a system which grows when capital is available for all to spend and when the debt assumed can be serviced from the cash flows of consumers and businesses. However, when the amount of debt reaches a specific threshold level, the process reverses and capital is destroyed by the creation of additional debt. We are now at that point in our economic history. Here are some significant ratios to ponder:

1945: \$1.00 of debt created on average \$3.00 of real wealth (GDP)

1965: \$1.00 of debt created on average \$1.00 of real wealth (GDP)

1983: \$1.00 of debt created on average \$.50 of real wealth (GDP)

1998: \$1.00 of debt created on average \$.30 of real wealth (GDP)

2007: \$1.00 of debt created on average \$.20 of real wealth (GDP)

2010: \$1.00 of debt will create approximately \$.06 of real wealth (GDP)

The message of the above ratios is that debt or leverage can increase our living standards for a limited time period (say 1945 to 2007). However, as debt reaches unsustainable levels, the Ponzi scheme of debt and leverage reverses and becomes the problem rather than the solution. Americans and the world are now at this point in history. As debt levels continue to increase, the ability of our Capitalistic system to service this debt becomes impossible and counter productive.

What does this mean? This means that Capitalism (as structured since 1944 under the Bretton Woods System) is over. Yes, we may have a couple of years left before the total collapse and crash, but the handwriting is on the wall for all to see and witness. Are you aware that 75% of all the debt within our global system has been created since 1990? Are you aware that the GDP of the USA was over \$14 trillion in 2008, and is now declining? Are you aware that the tax receipts collected from USA citizens are now declining? Are you aware that unemployment in the USA will exceed 9% in 2009 and will likely grow further in 2010 and beyond? Are you aware that the USA must borrow around 2.5 trillion in 2009 to avoid default and a collapse of the dollar? Where does all this money come from? Who can repay the existing debt (around \$60 trillion and growing exponentially) which our government has accumulated to date?

Can the government and the FED re-inflate our economy and the world economy once more to temporarily service all the existing debt? My view is absolutely NOT. Re-inflation (as espoused by many pundits) is over and done. We now must recognize that a hyper-deflation is on the horizon and emerging like a huge tornado from hell. The FED is impotent (as an institution) and all the 'funny money' from this organization is only destined to make our situation much worse over time. Imaginary money symbols (\$1.00 and multiples thereof) can not produce real wealth or growth when the imaginary numbers can not be repaid out of existing and future cash flows. Capitalism has turned into an imaginary numbers game (a Ponzi scheme) with no easy exit strategy. Check out this web site for further information: www.ft.com/capitalismblog

Conclusion: Get out of debt if you can. Reduce debt if you can. Eliminate debt if you can. Cash is King during deflation. Learn to barter for goods and services when you can. Simplify your life style. Gold and silver may help in the short term as the dollar declines. Eventually, however, a new global economic system will be needed. See my web site for one alternative for the future.

Donald B Swenson, Philosopher/Economist/Teacher/Student
Marana, Arizona
Email: don@kingdomeconomics.info
Web site: www.kingdomeconomics.info