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Spoiler warning

"I am certain that my fellow Americans expect that on my induction into the Presidency I will address them with a candour and a decision which the present situation of our people impel. This is pre-eminently the time to speak the truth, the whole truth, frankly and boldly. Nor need we shrink from honestly facing conditions in our country today.. So, first of all, let me assert my firm belief that the only thing we have to fear is fear itself – nameless, unreasoning, unjustified terror which paralyzes needed efforts to convert retreat into advance.. In such a spirit on my part and on yours we face our common difficulties. They concern, thank God, only material things. Values have shrunken to fantastic levels; taxes have risen; our ability to pay has fallen; government of all kinds is faced by serious curtailment of income; the means of exchange are frozen in the currents of trade; the withered leaves of industrial enterprise lie on every side; farmers find no markets for their produce; the savings of many years in thousands of families are gone.."

- From President Franklin D. Roosevelt's Inaugural Address, March 4, 1933.

Just two years after 'The China Syndrome' lifted the lid on Spanish practices in the US nuclear industry, Jane Fonda and her production company, IPC Films, did a similar hatchet job on US banks with 1981's 'Rollover'. The Alan Pakula-directed film is certainly of its time (that is to say, paranoid and narrowly racist); environmental concerns have now segued into economic and financial malaise, with Arabs and their petrodollars as the enemy (if it could be remade today, and it probably couldn't, the Chinese and the Renminbi would doubtless be replacing them). Investors with strong stomachs – and these days, that needs to be all of us – can watch the devastating final minutes here, as the US / global financial system is brought to its knees.

We are often accused of being permabears, and it simply isn't true. We will, however, accept any charges of being brutal realists or pragmatists. What ***is*** true is that the financial world has been in a state of crisis for at least the past four years, and despite all the Sturm und Drang and the endless pontificating from the markets commentariat, the nature of the crisis is neither widely recognised nor widely understood. Greece, for example, is a sideshow. But it is symptomatic of the cause, which we identify as fundamentally a problem of debt.

As Chris Martenson has observed (and we note, in passing, how it takes non-financial professionals to see clearly through the fog of the present), perpetual expansion is a requirement of modern banking. The supply of credit at least doubled during the 70s, then again during the 80s, then again during the 90s, then again during the noughties. Martenson suggests, and we fully believe, that there is now simply more debt in the world than can ever be paid back. You can see it in pictorial form here. Note that that debt is concentrated in the western economies. So on the one hand, we have a requirement for perpetual economic expansion, if only in the cause of debt service. On the other hand, the western economies have run into the sand. A recent McKinsey report on debt plainly identifies the problem. After a forty year party of debt-fuelled growth, we have the hangover of deleveraging. Historic episodes of deleveraging fit into one of four archetypes:

1) austerity (or "belt-tightening"), in which credit growth lags behind GDP growth for many years;

2) massive defaults;

3) high inflation; or

4) growing out of debt through very rapid real GDP growth caused by a war effort, a "peace dividend" following war, or an oil boom.

McKinsey's words, not ours. So choose your poison – assuming you have a choice.

And therein lies the problem. The dead weight of debt was amassed in large part by politicians promising more than they could ever deliver, with taxpayers now and to be born involuntarily taking up the slack. And it was facilitated by banks, the scale of whose malinvestment excesses has effectively caused their finances to be fused with those of national governments. Whether the crisis is resolved via options 1, 2, 3 or 4 (or combinations thereof) will be a function of cultural stability and political will – it is certainly not precisely predictable. The UK, so far, under a fractious coalition government has opted for 1. The grisly farce that is Greece will probably plump for 2. Option 4 looks unrealistic but US militarism cannot be entirely discounted. Option 3 continues to look like the most politically expedient "solution" for most of the indebted world. The business of investing involves a probabilistic quest for certainty where none exists. Hence asset diversification. But we have established to our own satisfaction a few ground rules. G7 government debt looks like a 'safe haven' bubble that could end disastrously. But if G7 government bond yields really are sustainable at their current, pitifully low levels, that implies a Japanified prolonged deflation that is logically consistent with a disaster for most other traditional assets. So sensible and uncorrelated investments scream out as one solution – we vote for systematic trend-following funds, and are now examining insurance-linked and infrastructure investments. And one thing "seems" certain: ongoing currency debauchery in the west, which would make the case for the monetary metals even without the simultaneous, grave and tangible threat to our banking and financial infrastructure.

During the conclusion of 'Rollover', a tearful young Asian banker summarizes the *intra-day* damage to her dealing room head: stock market down 10%; the same for the dollar; rival firms essentially bankrupt; gold just breaking above $2,000. His response: "By tonight, that'll be cheap." The economic logic is sound. We have been conditioned for the last forty years to price gold (for example) in an inconstant currency, the dollar. (Using the euro, the mongrel currency of a mongrel political union, would make the problem no more easily resolvable.) We make no apology for requoting Andreas Acavalos on the topic:

"..the problem of economic calculation under a fiat monetary regime is fundamentally insoluble. It cannot be solved for exactly the same reason that you cannot solve the problem of "measuring" a length of cloth with an elastic tape measure. The only "solution" is to throw away the elastic and use a yardstick that cannot be stretched at will."

That yardstick, of course, is gold. Mr Acavalos, again:

"Since it is unfortunately not within our power, as ordinary citizens, to do away with fiat money, we have to live with it and manage our affairs accordingly; we must, in other words, take rational economic decisions in the context of an irrational monetary regime that distorts relative prices and renders them increasingly meaningless as guides of where to invest. Here, I think, is where the role of gold comes in: acquiring gold is not an investment. It is a conscious decision to REFRAIN from investing until an honest monetary regime makes rational calculation of relative asset prices possible."

According to Wikipedia, the phrase "spoiler warning" started appearing during the early days of the internet so that unwitting readers didn't have vital plot points inadvertently revealed to them ahead of time. We apologise for giving away the plot to 'Rollover' – but as you'll find if you make the attempt, it's a difficult film to track down. I cannot recall its ever having been broadcast on terrestrial television here in the UK. Watch those final minutes and you can appreciate why. Films about meteorites, volcanoes, even earthquakes, the authorities can handle. Films about monetary and economic breakdown.. Confidence and trust are inherently part of the modern financial system. Once broken and driven away, they will not easily return. With luck, the sort of panic that we see in the last minutes of 'Rollover,' as an institutionalized and local bank run becomes public and international, will not recur in our lifetimes. But the current pace of "progress" in the euro zone and for that matter global debt crisis might suggest otherwise. "By tonight that'll be cheap." Six words that should inspire fear in every politician and monetary policymaker, in Europe and elsewhere.

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