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Now What's Going On

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EUROPE HIT BY DOWNGRADES

The Sovereign Debt Crisis is alive and kicking. The S&P's Ratings on France and 8 others were lowered fueling fresh worries that the Debt Crisis is not resolved. France and eight other euro-zone countries had their ratings downgraded on their sovereign debt Friday, sparking renewed global worries over Europe's ability to bail itself out of financial crisis. Why anyone could possibly think that ANY of the world governments will be able to bail themselves out is like the person who gets married after 5 times and actually expects this is the one! It is the triumph of **HOPE** over **EXPERIENCE**. This is precisely what is keeping the financial markets in turmoil. The talking head just talk. There is no substance to what they say anymore, for no one seems to think and chew gum simultaneously – forget about walking. When there is no plan whatsoever to ever pay off the debts, how can a sound person assume that the debt crisis will simply solve itself? Holders of sovereign debt are incredible stupid. They are no different from the eternal optimist who has fallen off the top of the Lippo Building in Hong Kong and as he passes the fourth floor he is heard saying: **“Well so far so good.”**



Standard & Poor's Ratings Services stripped triple-A ratings from France and Austria and downgraded seven others, including Spain, Italy and Portugal. It retained the triple-A rating on Europe's No. 1 economy, Germany. However, one must ask how long that will stand.

The downgrade to France, the Eurozone's second-largest economy, is a wake-up call. This will make it at least potentially more expensive to fund the Eurozone's bailout fund to help troubled states, because the fund's own triple-A rating depends on those of its constituents. The downgrades also directly affect the banks and the ECB. The changes will impact the European banks, who will be forced to take on these government issued € bonds by their own governments, yet downgrading the debt will force changes in the rules for collateral at the ECB and with their own government or European regulators. The idea of using government debt as reserves is giving way to reality. Soon, we will be back only too corporate debt, which was the case when the Federal Reserve began in 1913. It stimulated by purchasing corporate paper, not government bonds. That directly stimulated. Using government debt replaced corporate with World War II making it an incestuous indirect means of stimulus.

Country	Moody's	Fitch	S&P
Austria	Aaa	AAA	AA+
Denmark	Aaa	AAA	AAA
Finland	Aaa	AAA	AAA
France	Aaa	AAA	AA+
Germany	Aaa	AAA	AAA
Luxembourg	Aaa	AAA	AAA
Netherlands	Aaa	AAA	AAA
Sweden	Aaa	AAA	AAA
UK	Aaa	AAA	AAA
Belgium	Aa1	AA+	AA
Slovenia	Aa3	AA-	A+
Czech Rep	A1	A+	AA-
Estonia	A1	A+	AA-
Malta	A1	A+	A-
Slovakia	A1	A+	A
Spain	A1	AA-	A
Italy	A2	A+	BBB+
Poland	A2	A-	A
Lithuania	Baa1	BBB	BBB
Bulgaria	Baa2	BBB-	BBB
Cyprus	Baa3	BBB	BB+
Hungary	Baa3	BB+	BB+
Latvia	Baa3	BBB-	BB+
Romania	Baa3	BBB-	BB+
Ireland	Ba1	BBB+	BBB+
Portugal	Ba2	BB+	BB
Greece	Ca	CCC	CC

Those who call the Greeks thieves who started all of this by deliberately lying for a decade about their finances, fail to realize that all governments have played the same games revising how their economic statistics have been calculated post-1980. With the absence of political will and integration, there needs to be major reform. However, that is not likely absent a major financial collapse.

This is part of the final stages of **DEFLATION**. As debt defaulted in 1931, the **INFLATIONARY** turn around took about two years to unfold. As it stands right now, this downgrade is still reflecting the collapse in asset values. As sovereign debt is downgraded, the resale value of existing debt declines. This not only undermines the banks giving them incentives to avoid sovereign debt investment, but pension funds are hit as their asset values also decline. Thus, this is very much the final stage of **DEFLATION**. Inflation starts only when the majority of bond holders begin to realize that they are better off with private assets. This will make the shift from **PUBLIC** to **PRIVATE** asset investment come alive.

No government debt will be safe! Nobody will ever pay off anything. It is merely a question of time. That appears to be coming next year – 2013. By 2017, we may end up with a new World Monetary System.