



## The Six Horsemen of the Apocalypse.

by Joe Average.

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*And I looked, and behold a pale horse: and his name that sat on him was Death, and Hell followed with him. And power was given unto them over the fourth part of the earth, to kill with sword, and with hunger, and with death, and with the beasts of the earth.*

Book of Revelation, Chapter 6, Verse 8.

The Book of Revelation carries the grim prophecy that the Apocalypse will be heralded by the appearance of four fearsome riders on horseback... War, Famine, Pestilence, and Death.

In today's economy, more and more economists are beginning to worry that **a return of the normal business cycle might soon usher in an end to the current global expansion** that has been so **diligently orchestrated by the world's central bankers**. Concerns are rising that the stimulatory effect produced by a series of inflating markets and bubbles (i.e. the historic rise in the stock market, the NASDAQ bubble, the consumer debt and government debt bubbles, the real estate bubble, the explosion in hedge funds and derivatives, etc...) may be waning. The fear is now that if these markets implode or deflate too rapidly, that we **may be on the verge of a financial meltdown**. Six looming horsemen may portend such a coming financial **Apocalypse**.

### Horseman 1...Debt.

Following the stock market slump of 2000 to 2002, Alan Greenspan led the world's central bankers in a **concerted effort to eliminate the normal business cycle** that, in the past, would have seen **distorted financial excesses and monetary profligacy** purged by a dip into recession. This was achieved, firstly, by pushing interest rates down to historic lows and keeping them low for a long period and, secondly, flooding the markets with massive amounts of "out of thin air" credit.

**U.S. debt to GDP has soared to 335% against Germany at 64% and Canada at 75%. The U.S. trade deficit, which was \$158 billion in 2002, is now heading towards \$500 billion (and projected to be above 7% of GDP by year's end). Consumer mortgage debt, fanned by the flames of a red hot property market, has soared to an amazing \$2.3 trillion between 2000 and 2003 and is still bubbling.**

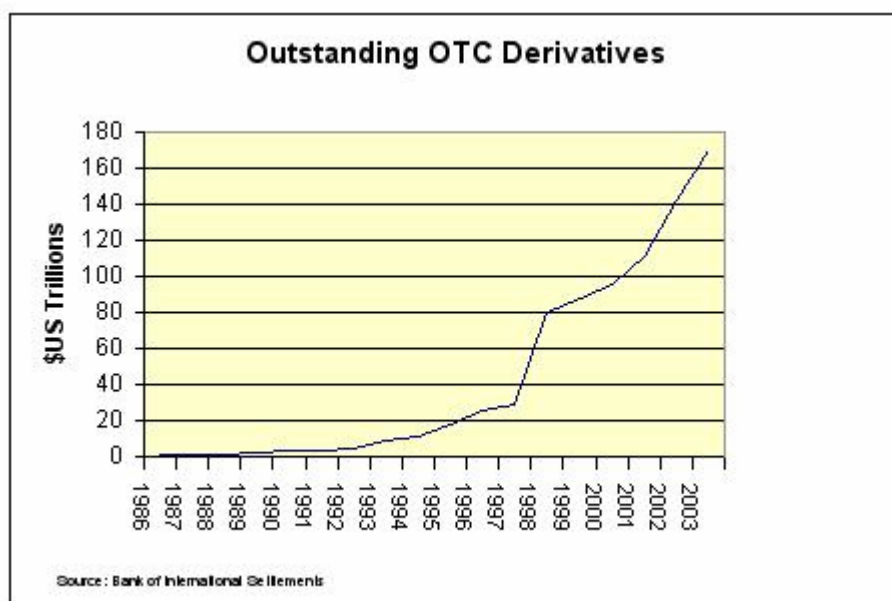
With consumers showing signs of reaching **saturation point** when it comes to **taking on more debt**, signs of a **slowing down in the retail sector**, and the spectre of **rising inflation and interest rates**, governments and consumers alike find themselves at the mercy of a change of mood by global investors. The global economy is **in danger of finally slipping into recession** with the accompanying **risk of a rapid loss of jobs and rising unemployment**.

Alan Greenspan has been successful in maintaining confidence in global markets and keeping a major recession at bay by manipulating one asset bubble after another. With Wall Street in count down mode to his imminent retirement, it remains to be seen how well his successor, “**printing press/ helicopter money**” **Ben Bernanke**, can fill his shoes and prolong the “**Greenspan Put**” effect. Meanwhile, the suspicion is that the Federal Reserve will resort to adding another trillion dollars to the money supply between now and January if necessary to ensure the **Dow remains above the psychologically important 10,000 (that’s the line drawn in the sand)**...long enough to ensure that the Sheriff gets out of Tombstone alive.

## Horseman 2...Derivatives.

**Derivates were created in 1973** with the opening of the Chicago Board Options Exchange, and became popular when the Futures Trading Act for Derivatives was signed into being by the Reagan administration in 1983. They were designed for their hedging ability to redistribute risk.

**By 1988 the value of derivatives had grown to \$1 trillion. Today in 2005, the value of the global derivatives market has gone ballistic and is now estimated to exceed \$270 trillion... 7 times the entire global economy and 27 times the U.S. economy!**



Graph courtesy Bank for International Settlements [www.bis.org](http://www.bis.org)  
Full publications are available for free on the BIS website.

Over the past twenty years the following **financial disasters** have been attributed to dangerous bets made using these **highly leveraged** financial instruments:

- **1987.... Stock market crash** attributed in large part to action of derivatives.
- **1995... 223 year old British institution, Barings Bank goes broke** due to the actions of rogue trader Nick Leeson who lost \$1.4 billion trading the Nikkei.
- **1998... Long Term Capital Management debacle** (caused by the trading of exotic derivatives) forces Federal Reserve to mount a \$4 billion rescue to prevent the collapse of global stock markets.
- **2001... Enron collapses** revealing that it has morphed into a major derivatives dealer rather than remaining an energy trader.
- **2003... Fannie Mae** is forced to account for \$1.9 billion lost on its derivatives portfolio sending its stock price crashing.

Warren Buffet has described derivatives as a “mega-catastrophe waiting to happen”, and likened them to “financial weapons of mass destruction”. The fact that three of America’s largest banks have huge exposures in this area (JPMorgan Chase Bank with \$43 trillion, Bank Of America with \$16.5 trillion, and Citibank with \$15.5 trillion) must keep some Federal Regulators awake at night.

### Horseman 3... Oil and Commodities.

The **past four years** have witnessed **one of the greatest resources booms in history**. The price of oil has increased almost fourfold to peak above \$70. The price of Copper recently hit its highest level for eighteen years (rising to \$3970 from \$1400 in 2001). Iron ore reached its record high level in November last year. The spot price of uranium is trading at about \$29 per pound compared to \$8 four years ago.

Global commodity prices were driven higher largely by a **seemingly insatiable demand from China** as it assumed the role of **manufacturer to the world**, which in turn was largely driven by a seemingly insatiable demand by American consumers for cheaper imports. **Hedge funds**, always quick to spot the new game in town, threw their enormous weight of money into the commodities market **driving prices still higher**.

**Now, with many commodities having hit cycle highs, the fear is that the boom could end within two years.**

**The Baltic Dry Index** (which measures the shipment of raw materials like cement, steel, grains and lumber) **has collapsed almost 50% over the past twelve months!** China, thanks to a continuing surge in steel production, has gone from being an importer of steel to becoming a net exporter of steel causing **global steel prices to slump** dramatically. Some economists are forecasting that commodity prices will crumble (e.g. that **alumina may drop up to 50% from its recent peak of \$424 a tonne**) as **commodity producing countries such as Brazil and Australia ramp up supply**. **Coke have already fallen from a high of \$420 last year to just \$150 a tonne now**. With prices sliding almost 40% in recent months, Chinese coke producers are beginning to lose money and it is feared they may refuse to honour contracts to take delivery of coking coal from Chinese domestic suppliers.

**At the moment all attention is focused on the price of oil!**

Most analysts see the current pullback in oil from a high of \$71 as merely a correction within a **long term bull market**, with many predicting that oil will again be driven up to record highs. This conviction is based on the **premise that oil is a finite global resource facing depletion due to inexorable growth in demand from China and India.**

Matthew Simmons (author of *Twilight in the Desert: The Coming Saudi Oil Shock*, and **oil policy adviser to U.S. President Bush**) believes the world has passed “**Peak Oil**”, the point of maximum oil production. He is adamant that demand will race ahead of supply and suggests at \$70 a barrel (or 21cents a pint), oil is still ridiculously cheap. **Simmons believes that prices of \$300 to \$400 a barrel are not impossible in the future as nations compete aggressively to meet their energy requirements.**

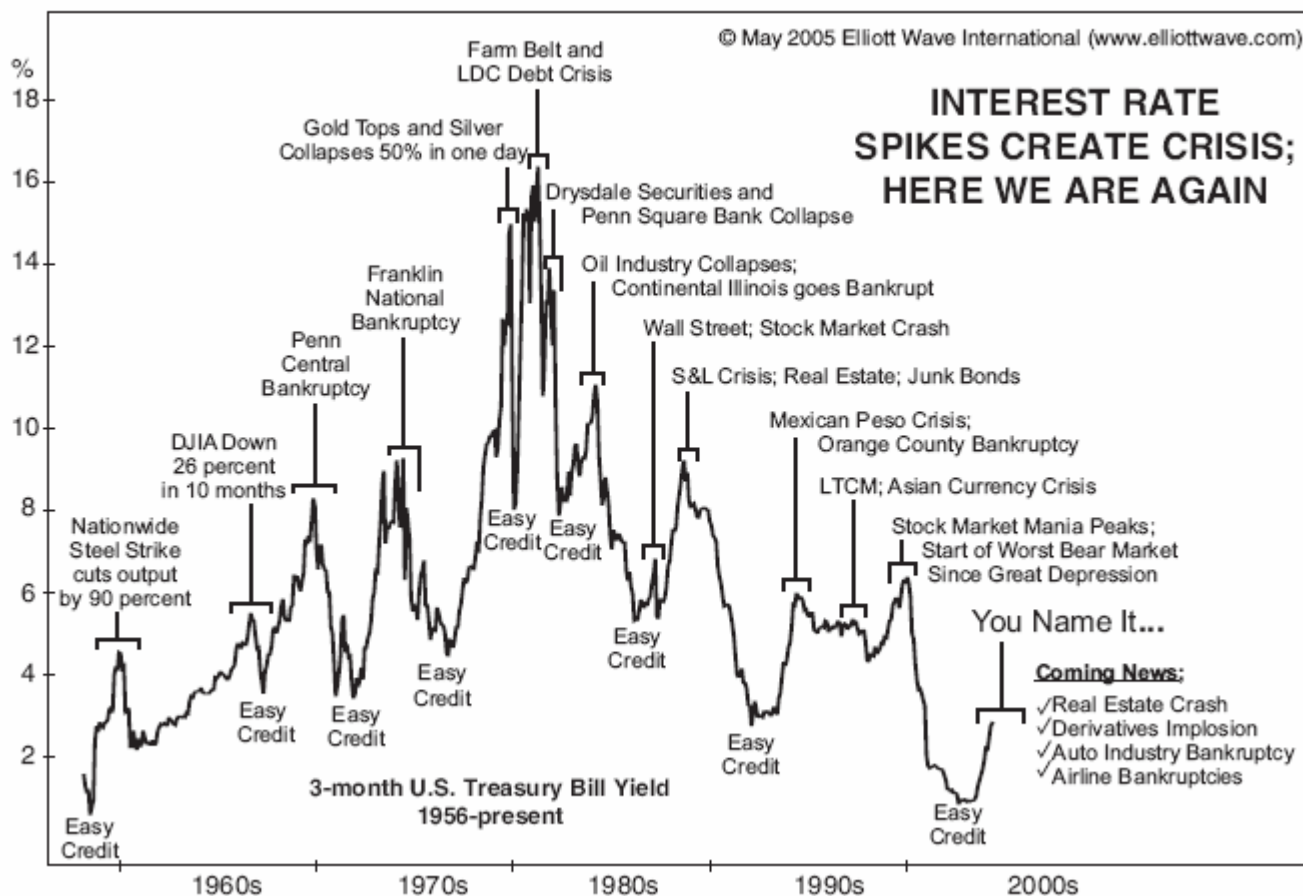
**Contrarians are sceptical about the “Peak Oil Theory”** claiming much more oil remains in frontier areas, and that “abiotic oil” and technological advances will come to the rescue. Besides, this group actually **believe the oil market may crash** resulting in a **world awash with oil** since **sky rocketing oil prices usually lead to recession and ensuing “demand destruction”**. The International Energy Agency calculates that each \$10 rise per barrel cuts growth by 0.5% and adds 0.5% to inflation.



**Joe worries: So which is it to be? “Peak oil” or “demand destruction”? Either way...sounds like Trouble with a capital “T”!**

## Horseman 4...Interest Rates.

*The Elliott Wave Financial Forecast — April 29, 2005*



Graph courtesy Elliott Wave International [www.elliottwave.com](http://www.elliottwave.com)

**Alan Greenspan's Federal Reserve slashed interest rates 12 times from 6.5% to 1.25% in the wake of the stock market crash of 2000 to 2002. Rates were then held down at fifty-year lows to encourage consumers to prop up the economy through borrowing and spending until business investment kicked back in. Unfortunately, much of this "easy money" found its way into real estate and other malinvestments resulting in a series of "bubbles" which ignited the flames of inflation. Belatedly, the Fed is now doggedly racheting up interest rates to minimize further fallout from its "easy money" policies.**

**It goes without saying that rising interest rates generally spell trouble for stock markets, bond markets, businesses, real estate values, and debt laden consumers!**

## Horseman 5...China.

Twenty five years ago Europe and the U.S. both acted as powerhouses to the world when it came to global growth and spending, helped in part by Japan.

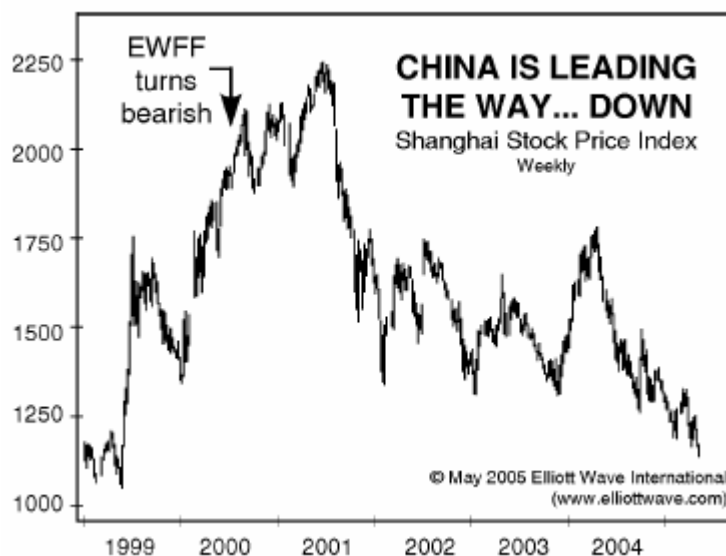
**Today, global spending is being propped up disproportionately by relentless U.S. demand which is being fuelled by new low cost suppliers like China and India. Ominously, these world imbalances keep on getting bigger.**

Economic prudence once warned that national deficits over 5% were danger signals. In 2005 the U.S. deficit is 6.5% and feared to reach 7% by year's end. That same deficit now accounts for 70% of the entire world's red ink flows!

One of the globe's surplus economies which is helping feed the beast is China, in what has been described as **“the largest vendor-finance scheme in history”** (Barry Hughes...Credit Suisse consultant). China has also been pivotal in counteracting rising **INFLATION** in the Western world by exporting **DEFLATION** from its low-wage, low-cost manufacturing shores.

With the global economy now so reliant on the Chinese growth engine, what lies immediately ahead for this emerging super power?

**If stock markets lead the economy** (as authorities like Robert Prechter of Elliott Wave International believe), then **the graph below paints a chilling picture.**



Graph courtesy Elliott Wave Financial Forecast [www.elliottwave.com](http://www.elliottwave.com)

## **Horseman 6...Bird Flu, War and Terrorism.**

**“FLU HITS EUROPE”** were the headlines everyone had been dreading.

Confirmation that the deaths of 2000 turkeys on a **Turkish farm near the Aegean Sea** were indeed caused by the **deadly H5N1 “Asian bird flu” strain**, and that a similar outbreak had occurred north in **Romania on the Black Sea**, sent European health officials into panic mode. The fear had always been that the lethal strain **would finally find its way from East Asia to the European continent...and now it had!** Romania's Danube delta, Europe's largest wetlands, provides the major resting place for migratory wild birds travelling from as far away as Russia and Scandinavia to North Africa for the winter.

**The importation of all poultry meat, livestock and related products** from these two countries was immediately **banned**. The British Government prepared **plans for a mass cull of poultry if necessary** and at the same time announced it was examining **the unprecedented step of sealing its borders by closing all airports and ports**. The French government have ordered 200 million protective masks. Nations around the globe are **scrambling to stockpile supplies of anti-flu drugs** even as some experts warn **“the existing vaccines don't work”**.

A World Health Organization adviser on infectious diseases said spread of the virus to **Greece and Croatia** after **Russia and Kazakhstan, Turkey and Romania** was predictable. And now the virus has been isolated in birds in **Canada and Japan**.

**H5N1 is currently regarded as the greatest disease threat to humanity. A worst case scenario being bandied around is over 26 million people becoming seriously ill and as many as 7 million dying from a global pandemic.**

**In the U.S. alone it is thought a rampaging Avian Flu could kill 2 million and lay low tens of millions more.** The Director of the Center for Biosecurity at the University of Pittsburgh Medical Center went so far as to say that such a catastrophe could prove to be a “**a nation-busting event**”.

The last time the world was ravaged by a killer bug of that virulence was back in 1918 when the Spanish Flu killed over 40 million people and affected anywhere from 20 to 40 per cent of the world's population.

**Not only would it shatter the American economy...it would also shatter the entire global economy!**

And all this on top of the ongoing conflicts in the Middle East, Iraq, Afghanistan, and the ever present threat of imminent terrorist attack be it in London, Bali, Russia, you name it.

It is easy to see how the fragile confidence and mood of investors and consumers alike could easily go into freefall should some catastrophic “out of the blue” shock suddenly strike.

International borders could quickly be closed; international freight and passenger volumes would plummet; and the global economy would grind to a debilitating standstill.

*May you live in interesting times.*

Chinese Proverb.

Cheers, Joe (aka Dr. William R. Swagell).  
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