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"The Latest European 'Rescue' Deal is a Sham. The Danger is Greater Now than Ever!"

"Don't be fooled. Greece is likely headed for default, and the Eurozone itself is at risk.

"And even if Greece survives, Italy is building up an even bigger disaster—one that can't be avoided or cured by bailouts and austerity measures.

"This is not just a European problem—it will directly affect us all. Read on for more!"

James DiGeorgia, Editor

Quiz question: what's the biggest economy in the world?

If you answered 'the United States', you're wrong.

Yes, the US is the largest *national* economy.

But the largest economy overall is the European Union (EU), with a GDP of €12.3 trillion (about $16 trillion, roughly $1 trillion more than the US GDP).

So why is this important? It's because…

The world's largest economy—and by extension, the world's entire economy—is in serious trouble.

Despite the best efforts of its leaders, the European Union is crumbling. The PIIGS economies (Portugal, Ireland, Italy, Greece, and Spain), especially Greece and Italy, are threatening to trigger a systemic collapse of the entire continent.

Wait a minute—didn't European leaders just announce a new rescue package that will fix everything? Yes, they did just announce yet another rescue package. And it will be just like all the previous ones.

Fool Me Once, Shame On You. Fool Me Nineteen Times, And…

…shame on those who keep falling for the same trick every single time.

Ever since the European crisis began, it's happened over and over again.

First, a PIIGS country nears default. European leaders scramble to avert disaster. Investors flee like rats from a sinking ship.

Meetings are held and deals are brokered. Reluctantly, the stronger EU countries cough up mountains of cash to bail out the offending PIIGS nation. The chastened nation promises to tighten its belt and behave better.

Investors cheer, and stampede back into European assets.

A couple of months later, the bailout money is used up. Then a PIIGS country nears default, and leaders scramble… and the cycle happens all over again.

So far, we've seen four major bailouts (Ireland, Portugal, Greece, and Greece again), along with the creation of two major bailout funds (the European Financial Stability Fund and the European Stability Mechanism).

Last year alone, there were well over a dozen emergency meetings of European leaders (I stopped counting at 19), along with an endless stream of reassurances and promises that the PIIGS will never default and the EU will never be broken.

There have also been a countless number of banking interventions to buy toxic PIIGS bonds and prop up their 'value'. And I won't even discuss the quiet involvement of the US Federal Reserve in much of this, both directly and indirectly.

But despite all of these bailouts, debt market interventions, debt relief plans, austerity measures, and 'this time will fix it for sure' deals…

The Danger of Collapse Has Never Been Greater

I've written before about why even a single PIGGS default will trigger cascading cross-defaults within the European banking system.

This is widely recognized. For example, there was a recent warning from Robert Shapiro (the co-founder and chairman of Sonecon, former US Undersecretary of Commerce, and Fellow at Harvard and the National Bureau of Economic Research). Here's what he said during a BBC interview:

"If they can not address [the financial crisis] in a credible way… we will have a meltdown in sovereign debt which will produce a meltdown across the European banking system. We are not just talking about a relatively small Belgian bank, we are talking about the largest banks in the world, the largest banks in Germany, the largest banks in France, that will spread to the United Kingdom… it will spread everywhere because the global financial system is so interconnected. All those banks are counterparties to every significant bank in the United States, and in Britain, and in Japan, and around the world.

"This would be a crisis that would be in my view more serious than the crisis in 2008."

And then there are other officials like Josef Ackermann, the CEO of Deutsche Bank. He said, "It is an open secret that <u>numerous European banks would not survive</u> having to revalue sovereign debt held on the banking book at market levels."

But those comments were made before the new deal that just got signed, and before the new LTRO (Long Term Refinancing Operation, meant to put a firewall around Europe's banking system) was created. Does this mean we're safe now?

No. In many ways, as I said, the danger has never been greater. There are at least seven reasons for this.

Reason #1: Same Story, Different Day

The new deal is just the latest version of the cycle I described earlier.

The only things that are different are the numbers, both good and bad (but mostly bad). They're all bigger than before.

Europe's fundamental problems have not been solved. In fact, they're getting worse instead of better.

For example, when the Greek crisis started in early 2010, Greek debt was about 120 percent of GDP. Despite subsequent debt-relief plans, the debt-to-GDP ratio has gotten far worse, because the Greek economy is imploding under the strain of the austerity measures (and bond yields have skyrocketed).

Today, Greek debt stands at 170 percent of GDP—40 percent higher than it was at the beginning of the crisis.

Reason #2: The EU's economy is shrinking.

Europe needs to grow its way out of its problems, but the opposite is occurring. As the World Bank recently warned, the EU is now mired in a recession.

Capital flows to developed countries have been chopped almost in half in just the last year.

Meanwhile, the US and Japan are still wallowing in debt and could trigger worldwide shocks. Overall, the global economy is at risk of a worldwide crisis even worse than 2008-2009.

Reason #3: Desperate Money-Printing

The European Central Bank (ECB) is trying to print its way out of the problem.

So far, it has printed a jaw-dropping $3 trillion in new money, along with the new $650 billion for the LTRO.

As a result, the central bank's balance sheet has ballooned to obscene levels.

This is a sign of desperation: an all-in play from European officials. If this doesn't work, nothing will.

And so far, it's not working.

Reason #4: European bankers, who know more about their situation than anybody else, are terrified.

Most of the ECB's newly-created cash was meant to 'juice' the European banking system, and get the banks lending. As the liquidity flowed out into the economy, the financial pressures would ease.

Specifically, the banks were supposed to go out and buy junk debt from the PIIGS.

Unsurprisingly, the bankers don't want to lend any more money to bankrupt countries. Nor to anybody else, for that matter.

Instead of lending out the cash, the bankers are squirreling it away. The *Wall Street Journal* recently pointed out that the eight leading European banks now have some $816 billion deposited with the Western central banks.

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As of last month, there was an all-time record of 453 billion euros deposited in the ECB's deposit facility. Eurobanks are sitting on mountains of cash.

You would think that if things were getting better, European banks would start lending. That's their business model, after all. That's how they make money.

But the bankers aren't fools (their previous loans to the PIIGS notwithstanding).

They know that European banks, European corporations, and (especially) European countries simply owe too much money to too many creditors. Realistically, the debtors can't pay their existing debts, never mind any new ones.

As a result, the bankers aren't lending out the new money. The ECB is pushing on a string here: it can create the money, but it can't force banks to lend it out.

This tells us how grim the situation is in Europe. If the banks, which have financial incentives to lend money (it's how they make their profits), and which are under growing political pressure to lend, are still <u>refusing</u> to lend, Europe is in far worse shape than we think.

Reason #5: According to the insurance markets, the danger of sovereign debt default is sky-high.

Back in 2007, before the global financial crisis began, European sovereign debt was considered rock-solid.

If you had a $50 million portfolio in European bonds (equally distributed among the bonds of Germany, France, Italy, Spain, and Belgium), you could have insured it against default for merely $28,649 per year.

Today, that same portfolio would cost you $2,258,200 per year. That's almost 80 times more than before.

(Notice also that this doesn't even include Greek bonds!)

The insurance industry—which lives and dies on its ability to accurately assess risks—is judging the danger in Europe to be sky-high.

Reason #6: A Greek Default Seems Inevitable

The Greek economy is imploding.

Despite the deals that have relieved some of their debt obligations, the Greeks still can't pay their bills.

The *New York Times* recently ran a story showing what life is like in Greece now. A typical situation was that of Aris Hadjigeorgiou, a middle-aged man who faithfully went to work every day, but hadn't received a paycheck in four months.

Neither had any of his coworkers.

But they kept going to their jobs anyway, "for the good reason that there was nowhere else to go."

As the article noted:

"By many indicators, Greece is devolving into something unprecedented in modern Western experience. A quarter of all Greek companies have gone out of business since 2009, and half of all small businesses in the country say they are unable to meet payroll. The suicide rate increased by 40 percent in the first half of 2011. A barter economy has sprung up, as people try to work around a broken financial system. Nearly half the population under 25 is unemployed… It's not uncommon to see decently dressed Greeks discreetly rummaging through garbage bins for food."

The reporter interviewed "one of the top bankers in Greece," who needed to stay anonymous. She warned, "You can't see the crisis results fully yet because people have been living off their savings. Soon the savings will end. I believe that by the end of 2012, you will see a different Greece, a different country, with real poverty."

Many Greeks are already asking why they must endure this suffering. The Greeks are making tremendous financial sacrifices, and for what?

Merely to make things easier for foreign creditors and bankers?

Merely to meet some arbitrary financial

goals, that they were forced to agree to, and which (even if met) would still leave Greece over its head in debt 10 years from now?

Merely so the northern Europeans will begrudgingly give them a few more installments of bailout money—a few more crumbs from their tables—which the Greeks were forced to grovel for?

There's a growing public rage against the whole situation, and a growing desire to defy the world and reject Greece's international debt obligations.

I would not be surprised if the current government in Athens falls in the next year or two. It would probably be replaced by a defiant, populist government that repudiates all its foreign debt.

If and when that happens, Europe's banking system will be in serious trouble. As noted earlier, so will the American banking system.

Reason #7: Even if Greece Doesn't Default, Italy Probably Will

Italy's new prime minister has forced through an austerity plan called "Save Italy." He claims its spending cuts and tax hikes will raise €30 billion ($41 billion). This is in addition to the €24 billion austerity plan that the previous prime minister created.

That's still a drop in the bucket compared to the ocean of red ink that Italy is drowning in. The Italians will need a projected €300 billion in financing this year alone, in order to survive.

The rest of Europe is understandably reluctant to pour this money into Italy without the Italians fixing their dysfunctional, disastrous economy. Thus the austerity plans.

But there are some diseases that just can't be cured. Like Greece, Italy seems too far gone to be saved. And like Greece, the "cure" will make Italy's disease worse.

We've seen this scenario play out already. In 2010, Greece was approximately where Italy is now. Its debt was about 120 percent of

Portfolio Update

In Update #1267, we recommended opening a position on Sandridge Energy (symbol SD). We sold the June $7.00 put (symbol SD120616P7).

In Update #1271, we took profits on our short puts on Hess Corp. (HES), Magellan Midstream Partners LP (MMP), and Sandridge Energy (SD). On HES, we bought to close the short March $57.50 put (HES120317P57.50). On MMP, we bought to close the short April $62.5 put (MMP120421P62.5). On SD, we bought to close the short June $7.00 put (SD120616P7). Our total profits were $210.

In Update #1272, we opened a position on the Energy Exploration & Production ETF (XOP). We sold short the March $55 put (XOP120317P55).

In Update #1274, we noted that our profits taken and expired options in February netted us $687.

In Update #1275, we issued new recommendations on British Petroleum (BP), Conocophillips (COP), and Chevron Corp. (CVX). On BP, we sold the Feb. $43 put (BP120421P43). On COP, we sold the Apr. $70 put (COP120421P70). On CVX, we sold the Apr. $97.50 put (CVX120421P97.50).

In Update #1277, we issued new recommendations on Hess Corp. (HES) and Stone Energy (SGY). On HES, we sold the Apr. $57.50 put (HES120421P57.50). On SGY, we sold the Apr. $29 put (SGY120421P29).

In Update #1279, we took profits on our short puts on Canadian Natural Resources (CNQ), Devon Energy (DVN), and Energy Exploration & Production ETF (XOP). On CNQ, we bought to close the Mar. $35 put (CNQ120317P35). On DVN, we bought to close the $62.50 put (DVN120317P62.50). On XOP, we bought to close the March $55 put (XOP120317P55). Our total profits were close to $300.

In Update #1280, we noted that tensions are rising in the Middle East. We recommended buying three June 128 puts (SPY120616P128) on the S&P 500 ETF.

GDP, and its 10-year bond yields were about 8 percent. That's where Greece was when the austerity plans started, with spending cuts and tax hikes to clean up its economy.

Today, even after two massive infusions of cash and partial debt forgiveness, Greece's debt is 170 percent of GDP, and its 10-year bond yield has soared to 30 percent.

Italy is starting from the same place Greece started from, but on a much bigger scale.

However, as the third-largest economy in Europe, Italy is too large to be bailed out.

Nor does the EU have any money left anyway, after bailing out Portugal, Ireland, and Greece (twice).

I discussed the scale of the Italian disaster in last September's issue. You might remember this picturesque quote from John Browne of Euro Pacific Capital:

"Italy is simply too big to bail out. Its collapse, like the sinking of a great ship, could create a vortex that drowns Europe's major banks in red ink."

In a sense, Greece was merely a 'preview of coming attractions'. It showed us the road that

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Chinese Buying Record Quantities of Gold

Forbes recently reported on record purchases of gold by the Chinese—as much as 490 tons in 2011.

That's double the estimated 245 tons bought in 2010, and it represents a "massive increase in Chinese buying," according to a London gold broker.

The Chinese are tight-lipped about who exactly is doing all that buying. No doubt, private investors are accounting for much of it.

But there are strong rumors swirling about the identity of the largest buyer—rumors which, if true, could blast the price of gold up by hundreds of dollars per ounce.

I'm talking about the Chinese government itself, via its central bank (the People's Bank of China, or PBOC).

China's highest financial officials have been warning the US for years that they're fed up with America's blowout deficits. The US is already $15 trillion in debt, and plunging further into the hole every day.

By any reasonable measure, the US is broke, and will be unable to repay its debts <u>at today's value of the dollar</u>.

If we remain on our current path, the US will be forced to devalue its way out of its debt. Yes, eventually we'll pay back all 15 trillion of those dollars. But each dollar will be worth far less than today.

As the largest foreign owner of our debt (with over $1.1 trillion in Treasuries), China will take massive losses when this happens.

They know this, of course. And they aren't going to sit passively and wait to get steamrolled.

Instead, they're going to diversify into other assets. For years now, they've been quietly warning the US that their days of funding America's no-limit credit card are coming to a close.

They've also said that they would start buying gold.

That day has arrived. As the PBOC's Zhang Jianhua said in December, "No asset is safe now"—except for one. He continued, **"The only choice to hedge risks is to hold hard currency—gold."**

He also said it was smart strategy to buy gold on market dips.

Let's think about this. China wants to get rid of over $1 trillion in US Treasuries. It wants to shift at least some—maybe even most—of that money into gold.

Even if China only used 40 percent of that money to buy gold, **it would be <u>double the entire global gold demand</u> last year** (about $200 billion).

At today's prices, it would also be <u>triple the entire world's gold mining production</u> last year.

Of course, it won't happen at today's prices. That's not how the market works.

When the Chinese start buying in earnest, gold will blast up to multiples of today's price.

"US Headed for Cyberwar Showdown with China"

Chinese attacks on US government computers are now in the millions per month.

I've written in past issues about the long list of military technologies that China has stolen from defense firms and the US government itself. As bad as that is, military officials are warning that China appears to be preparing for even worse attacks.

Forbes described the crisis in a recent article ("US Headed For Cyberwar Showdown With China In 2012"). It quoted General Keith Alexander, head of the Pentagon's joint Cyber Command, who said, "We see a disturbing track from exploitation to disruption to destruction."

When a hacker breaks into a computer system, he can do much more than just stealing information. It's also common to install "back doors" in the system—giving him the ability to return again later, quickly and secretly, to do whatever he wants.

Back doors allow hackers to harvest a continual flow of information from the compromised system. Worse, the hackers can also cripple or destroy the systems remotely. This can be done as simply as deleting all the files on the systems. Or, depending on the nature of the systems, actual physical damage can occur as well. For example, hackers recently broke into the control system of the water utility for Springfield, Illinois. They destroyed a water pump by turning it on and off continuously, burning it out.

That was a minor attack. Imagine what thousands of organized hackers could do, if they struck utilities across the US simultaneously.

China is also waging an escalating campaign of economic attacks on the US. *Bloomberg* reported that at least 760 companies, universities, and government agencies have been attacked by the Chinese.

The victim companies range from large multi-national corporations to niche firms, in a wide variety of industries. The list of victims includes Google, Intel, Adobe Systems, Hewlett-Packard Co, Volkswagen AG, Boston Scientific, and Wyeth (the drug maker that's now part of Pfizer). Chinese hackers even broke into the computing center of the Food and Drug Administration, which stores chemical formulas and other information for almost every important drug sold in the US.

Other victims include government entities, think-tanks, and non-profit groups, energy companies, semiconductor firms, telecommunications companies, and sensitive targets like Aerospace Corp., which is a large part of the US military space program.

Bloomberg quoted Richard Clarke, former special adviser on cybersecurity to US President George W. Bush. He said, "What has been happening over the course of the last five years is that China—let's call it for what it is—has been hacking its way into every corporation it can find listed in Dun & Bradstreet… Every corporation in the US, every corporation in Asia, every corporation in Germany. And using a vacuum cleaner to suck data out in terabytes and petabytes. I don't think you can overstate the damage to this country that has already been done."

Scott Borg, an economist and director of the US Cyber Consequences Unit said, "We're talking about stealing entire industries… This may be the biggest transfer of wealth in a short period of time that the world has ever seen."

Let there be no doubt. This is not the work of a few bored teenagers, or even corporate spies. The overwhelming majority of the attacks are coming from Chinese military computers, especially those of the People's Liberation Army's 'Third Department' (a unit responsible for cyber operations).

We know this because the hackers sometimes act carelessly. In one incident, a ranking officer in the People's Liberation Army used a server that was just used in cyberspying operations to communicate with his mistress.

Representative Mike Rogers, chairman of the Permanent Select Committee on Intelligence, has said, "Some notion that this isn't nation-state driven is just false."

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far-bigger Italy is now beginning to travel.

And it's a road that will bring disaster upon all of Europe, and by extension, the world.

Conclusion: Europe is a clear and present danger to the world economy, including the US.

How do we protect ourselves from all this?

Clearly, currency-related assets are at risk. Dollars and euros will be printed with abandon as the crisis progresses.

That means counter-currency assets have tremendous potential.

And that's one of the reasons why…

The Precious-Metals Market Is Red Hot

Last year, gold shattered its price record, blasting up to $1,895 per ounce.

Meanwhile, silver hit $50.35 per ounce—just a few pennies shy of its all-time record of $50.45. Platinum hit almost $1,900.

In 2011, the US Mint produced a record number of coins. 2012 will probably follow suit. Among other things, investors are eagerly awaiting the Mint's first-ever palladium bullion coins.

The coin market overall is booming. Last month at the Heritage Numismatic Auctions, over $53 million in coins were sold. This includes two coins which sold for $1.38 million each.

Central Bank Gold Purchases Surge Up

On a net basis, the world's central banks (excluding China) bought an impressive 440 metric tons of gold last year.

When even the central bankers—the issuers of global currencies—prefer gold to currencies, what should the rest of us be doing?

Here in *Gold & Energy Advisor*, I'm extremely proud of our track record trading energy stocks (an average return of 29.1 percent per year since inception eight years ago). But we've made equally stunning returns in gold, silver, and platinum; I started recommending these metals to readers when gold was $398, silver was $7, and platinum was $913.

There are excellent reasons why precious metals have skyrocketed like this. As hard physical assets, precious metals hold their value when paper assets crash and burn.

Even though the metals have risen so far in the last eight years, I expect to see them rise for several more years at least. There are just two primary scenarios where this wouldn't occur:

If the entire world plunges into deep recession or depression, or…

If the US stops borrowing money and starts repaying its monstrous debts, while Greece and Italy make strong recoveries and repay <u>their</u> debts. Meanwhile, Iran peacefully gives up its nuclear ambitions and embraces the existence of Israel, the spreading civil war in Syria doesn't spill out into surrounding countries, India and Pakistan make peace, the Taliban in Pakistan give up their desire to overthrow the government (and take control of its nukes), and China stops its escalating cyberwar on the US.

The first scenario is possible but unlikely. (The world's central bankers will print money until it turns into toilet paper, before they let this scenario occur.) And the second scenario is flat-out impossible.

In most conceivable scenarios, we'll continue to see soaring metal prices. Even if this were not true, I'd still urge you to protect your wealth with a strong position in precious metals if you haven't already done so.

Wealth preservation should be one of our primary concerns today. Economic calamity in Europe, looming wars elsewhere, the monstrous debt levels of the US, and other growing dangers are all serious threats to your wealth.

Precious metals, especially gold, stand tall when other assets collapse. They're the kings of wealth preservation, and are the best way to profit when fiat currencies are burning.

Make sure your "wealth insurance" is in place!