



2009 – A YEAR OF MONEY PRINTING, INFLATION AND FINANCIAL TURMOIL

“Paper money eventually returns to its intrinsic value – ZERO”

Voltaire 1729

In our December 2007 report we forecast *“a major recession or depression for the world economy in the coming years”* as well as *“serious problems in the world’s financial markets with the banking system fighting for survival.”*

Sadly this has all come to pass but the trend that started in 2008 is only the very beginning of a major reversal that will dominate the world economy for years to come. It will be distressing and life changing for many people but there are ways of easing the pain for investors which we will discuss later in this report.

The most likely scenario in the next few years will be first a period of high inflation in most countries leading to hyperinflation in many economies. This will be a hyperinflationary depression fuelled by unlimited money printing. But like most hyperinflationary periods this one will also eventually lead to a deflationary collapse with an implosion of the financial system.

The above scenario might be difficult to accept for most individuals but in our opinion it is inevitable and cannot be changed by any government or central bank action, regardless of who the leaders are. The Rubicon has already been crossed and there is no return. Thus *“the die is cast”*.

The world’s biggest Ponzi scheme

No, we are not talking about Bernie Madoff and his alleged \$ 50 billion swindle. As devastating as this scheme was for many investors, it is small fry compared to what governments and central banks and the banking system have done for years and are now doing at an ever accelerating pace. **Namely, to print unlimited amounts of money based on power**

and greed. The purchasing power of the US dollar and most other currencies has declined by around 95% in the last 60 years. This is the amount of wealth destruction that has taken place until now. But this is nothing compared to what is now happening. Only in the last few months the USA has printed or committed to print \$ 8.5 trillion to save its collapsing economy. But this is just the beginning and will be nowhere near sufficient to save the banking system, mortgage loans, personal credit, government and local government deficits, pension funds, insurance companies car manufacturers, other industries etc, etc. To this we will have to add the staggering amount of \$ 700 trillion to \$ 1 quadrillion derivatives outstanding, a major percentage of which is totally worthless.

Remember that most of these debts so far have been created in so called "good times". **So now when debts are escalating at exponential rates and times turning bad, it is an absolute certainty that these debts will never be repaid. This is why all the money printing that has taken place and is now taking place is the biggest swindle or Ponzi scheme ever, especially since governments know that the astronomical debts can never be repaid. This will lead to the destruction of the value of most currencies.**

So also this time, the wise words of Voltaire in 1729 will come true that:
"Paper money eventually returns to its intrinsic value – ZERO.

Deflation will turn to inflation in 2009 and later into hyperinflation

Bank write-offs to escalate

We have had a temporary period of deflation in 2008 due to falling asset and commodity prices. This will change during 2009. The massive money printing by most countries, led by the USA will see to that.

So far the US has created and committed \$ 8.5 trillion and other countries additional trillions. These amounts have temporarily stopped the banking system from going under. **But to save just the US banking system will probably require \$ 20-30 trillion, at least,** with proportionately similar amount in other countries. Until now our estimates of write-offs, although higher than virtually any forecaster's, have been exceeded so we might be too conservative also this time.

The 25 biggest financial institutions in the US have a total equity of around \$ 1 trillion. It is no mean feat that the potential capital requirements to prop up the US financial system is circa \$ 20-30 trillion or 20-30 times equity, if our estimate is correct.

Massive government deficits

The requirements for the survival of financial markets will soon start competing with massive government deficits due to significantly reduced tax revenues and massive increases in outgoings. Already in 2009 the US budget deficit could be at least \$ 2-3 trillion which is 15-25% of GDP. The UK will also have record budget deficits on 2009 and most other countries will follow. These deficits are likely to increase in the following years with increasing unemployment. Also, at some point governments will be forced to write off the worthless loans/investments made to financial institutions.

Pension fund deficits

The decline of financial assets (including a coming bond market collapse) combined with falling or negative corporate profits will lead to major deficits in all pension funds. Also, in many countries a major part of the population doesn't have a pension or the pension funds are unfunded. This will lead to a major pressure for the baby boomers that are now starting to retire. Also these shortfalls will be funded by governments leading to more money printing and bigger deficits.

Zimbabwe and Iceland first – UK and the USA next

We said in a report last year that Iceland was a microcosm of things to come with massive borrowings, current account deficits and budget deficits. This led to a collapse of the Icelandic economy and financial system. The currency has collapsed and Iceland is on its way to hyperinflation. Zimbabwe is an even more flagrant example.

The UK is starting to go the same way with the world now concerned about the UK government's immense money printing leading to a collapsing pound. **The pound has in the last 1 ½ years declined by circa 35% against the Euro and the Swiss Franc and 30% against the Dollar.** This will lead to a major increase in inflation in the UK in 2009 and eventually probable hyperinflation.

Next is the USA. The US dollar was temporarily strong during 2008 due to the forced liquidation and repatriation of foreign investments by US institutions/investors. But as we forecast, this was a passing event and the US dollar has now resumed its decline. This, combined with the money printing, will lead to increasing inflation also in the US during 2009 leading later to hyperinflation.

The important point we are making above is that hyperinflation is a currency event. Money printing leads to declining purchasing power and to a falling value of the exchange rate eventually creating hyperinflation.

This phenomenon is likely to take place in many other countries leading to competitive devaluations. So what happens if many major economies devalue their currencies? Well, first of all some will be a lot worse than others leading to a greater relative fall of their currency. **But secondly and more importantly, the only currency which cannot be printed and which has no debts attached to it is gold. This is why gold will be a major beneficiary of the continuing currency devaluations. Investors in Iceland who had their assets in gold would have made more than 100% return in 2008. A UK investor made over 40% on his gold investments in 2008 and in Zimbabwe the rise of the gold price is exponential. This is just the beginning of things to come.**

Don't trust biased governments, bankers or economists

We have warned investors in the past not to believe what they hear or read. Remember that with very few exceptions (one of them being ourselves) no one has forecast the current crisis and very few of the so called experts understand what will happen next.

Until a year ago every government and central bank had one major objective – to fight inflation. One year later trillions of dollars have been printed worldwide and not one government official or central banker talks about or understands the **consequences**. Politicians only have one principle that they follow without fail – **TO STAY IN POWER**. They will do whatever is required to attain this goal.

The current crisis and bubbles have arisen as a result of decades of financial mismanagement and money printing by governments. But the crisis could probably have been solved without major consequences in the early 1990's. But instead Greenspan and other central bankers reduced interest rates and increased the speed of debt creation. Today, sadly nothing can be done to rescue the situation. All the money printing that is taking place is only making the system more unstable leading to a greater and more devastating collapse.

Bank bonuses – the unacceptable face of capitalism

Governments have created the current problems and bankers have used the system, exacerbating the problems manifold. They have created credit and derivative instruments valued at over \$ 1 quadrillion and a substantial part of this is worthless. This is what we call collusive back scratching. Collusion between power hungry governments and bankers driven by greed has created the biggest financial bubble known to mankind.

Not only have bankers been allowed to create these instruments and benefit from it in bonuses to the extent of \$ 100's of billions with individual bankers earning up to \$ 100's of millions. But the world has now discovered that a major part of what the bankers have created is just a worthless Ponzi scheme. So what do governments do? They spend, currently, in excess of \$ 10 trillion of printed or taxpayers' money to rescue the banks and the fraudulent Ponzi schemes created by bankers. And what do banks do? They continue to pay out almost the same size bonuses to their employees in spite of the fact that the whole financial system has only survived (temporarily?) due to massive injections of government/taxpayer money. **THIS IS THE UNACCEPTABLE FACE OF CAPITALISM.** We are surprised that this has not generated a bigger uproar by the public and media.

Geopolitics

The major areas that will affect the world political situation in the coming years will be Pakistan, India and the Middle East. The situation in Pakistan is extremely serious with a government that has lost control of major areas of the country to the Taliban, especially near the border to Afghanistan. There is a serious risk is that the Taliban will dominate major strategic parts of Pakistan and eventually get access to the country's nuclear weapons. This will have major repercussions for the rest of the world and terrorism. The risks of a nuclear conflict between India and Pakistan are also high.

The Middle East situation although also very serious is not of the same magnitude as the problems in Pakistan.

Financial forecast for 2009

Stockmarkets

We warned investors last year not to be invested in the stockmarket and this has been correct advice. Most markets have fallen at least 40% in 2008 and many a lot more. We have written in a recent report that we expect a bear market (corrective) rally in the beginning of 2009. This is still our forecast. It could be like in 1930 when the market in the USA rallied 50% for six months after the 1929 fall. Thereafter it continued to fall a total of 90% from the top. But markets seldom repeat themselves. It would be much too easy. The consensus is currently that such a rally will take place and this concerns us somewhat. The masses are seldom right. Therefore our fear is that the rally will be shorter in time and less in price than the market is expecting. Thus, expect a rally but use it to get out of any remaining positions and don't be too greedy.

However, we expect precious metals mining shares to go up substantially in 2009 as well as certain commodity shares.

Currencies

We expect the dollar fall to accelerate during 2009 against most currencies. The Euro and the Swiss Franc should go well past their highs against the dollar. The Pound will continue to be weak against most currencies but could appreciate against the dollar.

Bond Markets

Short term interest rates are virtually at zero in many countries. There is nowhere to go but up from here. Longer rates could go down marginally early in 2009 but the big surprise in the coming year will be longer rates going up and bond markets falling rapidly. Governments will continue to try to keep short rates down but the markets will push long rates up. With the massive financing requirements of many countries (e.g. USA, UK), their currencies will fall and investors will sell their holdings of these bonds and or demand much higher interest rates on their risky investments. We could easily see bond rates go to double digit figures in the next couple of years. This is clearly part of the hyperinflationary scenario.

Commodities

Most commodities have probably reached a bottom especially in dollar terms. With commodities priced in dollars, the falling dollar will make them more expensive. The continued downturn of the world economy will reduce production of most commodities, making them much scarcer and more expensive.

Precious Metals

This continues to be our favourite area of investment for 2009 and beyond. Since 1999 gold has appreciated between 152% (in Swiss Francs) and 285% (in Pounds) or an average of 17-32 % per annum. Matterhorn recommended to investors in late 2002 to put up to 50% of their liquid assets into gold. Since then the gains have been 110% or 18% per annum in Swiss Francs and 200% in Pounds or 33% per annum.

The above returns outperform most other investments during the same period. But the most important point is that we believe that the big move in gold is still to come.

If we are wrong in our inflation/hyperinflation forecast, the only alternative would be a deflationary implosion of the financial system which would also be very bullish for gold.

Silver, platinum and palladium will also appreciate during 2009 but since they are also industrial metals and therefore more volatile, investing in

these metals will not be covered in this report but discussed with investors separately.

SUMMARY

2009 and beyond will probably be the most difficult period in the world economy since the 1720's and thus worse than the 1930's. We see inflation increasing during 2009 eventually leading to a hyperinflationary depression in many parts of the world.

The best way that investors can protect themselves financially in this scenario is to invest in physical gold and store it in secure vaults outside the banking system.

Matterhorn Asset Management based in Zurich, Switzerland specialises in wealth management and wealth preservation with particular emphasis on gold bullion and other precious metals stored safely in the investor's name outside the banking system.

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