

The Metrical Equilibrium of Housing

The Inevitability and Imperative of Deflation

The Red Herring

Much Debate is occurring about the decline in Housing Values in various parts of the World. Most believe and accept the declines are because of the “Credit Crisis” or a convexity of selected negative forces. This is a complete fallacy and the real issues are not even being discussed much less understood. The infamous “Credit Crisis” is merely a huge Red Herring.

The decline in Housing Values is the result of Housing having reached what I call “Maximum Differential”. That is the “Maximum Differential” between Wages and the Value of a Home.

What you can't read in any book or find in any intellectual dialogue:

The True Housing Metric – 3 Times Wages/Earning Capacity.

A House cannot have a Value more than approximately 3 times the Wage/Earnings. However, this Metric has reached 5, 6, 7 and even 8 times Median Wages in some places in the World – in short, a secular and exponential increase in the metric.

Laying the Foundation

The reason this was able to occur was through calculated and intentional policies of Central Bankers in creating artificially low interest rates below the true inflation rate, which was the financial equivalent of adding gasoline to a fire.

With this Monetary backdrop, through the complexities and subtleties of so-called “Financial Innovation”, Housing Demand was artificially stimulated to a level far in excess of Natural Organic Demand.

The purpose of which was to achieve short term political gain and a longer term Redistribution of Wealth. This massive increase in Housing Values in turn created an Artificial Prosperity.

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Housing Values served as the *Transmission Mechanism* throughout economies of the World. It also created a massive increase in Government revenue as well, as housing is taxed *ad valorem*.

It has resulted in the greatest misallocation of Capital in the History of the World through widespread ignorance of what was really occurring. The "*New Paradigm*" thinking once again subdued the intellectual elite.

Amazingly - but not surprisingly - once again despite the absolute and equivocal historical proof to the contrary, even the smartest people bought into the belief that the Road to Prosperity can be paved with Debt.

This misallocation was understood and intended by those causing it.

Why ?

Because the end result will be a massive *Redistribution of Wealth* as the unwinding takes place.

Redistribution of Wealth

What occurred in Housing as well in all other "Assets" was "Inflation" of values (*Stocks, Commercial Real Estate, Art, etc.*) This "Inflation" in reality was funded through "Debt" built on simple but false premises i.e., that the underlying valuation metrics were both valid and sustainable. Meanwhile, "Cash" itself was devalued – as a natural and concomitant result of Interest Rates being forced below the true Inflation Rate (most notably evinced by the decline in the Dollar). Asset Inflation was the natural, foreseeable and proximate result of this.

Now "Assets" will all lose value through Deflation. *Deflation* causes the real value of Debt to rise while simultaneously the buying power of Cash is rising.

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The Debt serves as the Mechanism for the *Redistribution of Wealth* as Deflation gradually makes the Debt unsustainable hence forcing a relinquishment of the Asset at a much lower value. Debt is the operative mechanism - Cash is the Means.

Those with the Cash are thus able to acquire the asset at a distressed and artificially low value (which is now Inflated in its Value *and* Buying Power). It is this cold, greedy and cynical political calculus that drove policy – nothing else. But there was also another Demographic and Fiscal imperative.

Demographics & “Unfunded Liabilities”

Everyone keeps talking about the unfunded liabilities and precarious fiscal situation of the United States. However, that entire dialogue is based on fiscal math which in turn is based on a wave of millions of “Baby Boomers” retiring – and millions after them based on the Pensions of today.

First, the coming Deflation is going to force millions of Baby Boomers back into the workforce for many years. Second, by keeping interest rates below the true inflation rate for so long, the future Pension system is going to collapse [the big “Crisis” of the next period] – because the interest rates have been too low for too long to sustain the long term return necessary to fully fund them.

The math is unequivocal in this regard, despite the spurious “models” of annualized and compound 10 % + annual return. Parenthetically, it is ironic and poetic justice – because the dialogue of today is the accepted notion that we are creating debts “our children will have to pay” – yet there is no outcry or effort to remedy this plainly wrong societal conduct.

The confluence of these elements cannot be understated.

This is how the tax revenue to meet the “unfunded liabilities” will be extracted from the People. The end result will be tens of millions more workers contributing to the tax system – a factor not in the calculus of the pundits or doomsayers.

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Protectionism and "New Deal" type policies will provide the structural backstop for these jobs.

This is why a bet against the Dollar is a big mistake.

These events will be politically packaged and sold to the masses as an Epic Economic Downturn that will resonate for a Generation. The perceived "catalyst" may be "Oil" (an easy and timely one – the political and economic contours of which we are observing develop presently), or some other element – certainly not one which imputes culpability on the part of policymakers.

A Pie Divided

The so-called "*Inflationist's*" are going to find themselves sadly on the wrong side all the way down - of the Controlled – but *Secular Deflation*. Similarly, those who believe the financial woes of the Banking/Credit System are "largely behind us" will likewise be disillusioned.

This "Metrical Equilibrium" – and the Deflation as a whole - has just begun its reverberation through financial markets.

It is akin to a 9 inch Pie being divided and allocated – except after the allocation of which each party has their "rights" irrevocably vested on paper - it is determined that the Pie can never exceed 6 inches.

However, in the financial system, that 3 inches around the circumference amounts to literally trillions of dollars on balance sheets throughout the financial world that are fallacious. Regardless of what games, obfuscation and delay that occur, the Marking to Market of that financial reality is inevitable.

What we've seen Marked to Market to date, is a mere fraction of the fallacious value on balance sheets worldwide, in all the various aspects, like layers of an onion.

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“It’s Different this Time”

For those saying it is “ Different this time ” from the Stagflation of the 1970’s – they are right, it is different – *it’s much worse*.

At least in the 70’s we had the Wage Spiral – as maligned as it was and is by both pundits and academics, the Wage Spiral had a key ameliorative effect: it kept an Economic Equilibrium. As Prices rose, so too did Wages.

The difference now is that we have all of the Inflationary Attributes of the 1970’s – markedly amplified through Globalization - but Wages can’t rise.

The ‘*New Paradigm*’ isn’t some Economic Miracle, but rather in the *Ratio Attributes* of the employment base of the World through “Globalization”. The *Ratio Attributes* of China and India standing alone act as a concrete ceiling on worldwide wages – and thus concomitantly as a limit on Inflationary Monetary Policies – a critical dichotomy the “Inflationist’s” and other pundits fail to apprehend.

The Dichotomy of History and Geopolitics

The most amazing delusion and deviation from the plain lessons of history is the belief that “Hyperinflation” is unfolding. What events in *Germany* and the *Great Depression* proved respectively, is that a society will accept and can survive Deflation – not Hyperinflation.

Indeed, why would Central Bankers destroy the very source of their power – the currency system - by Hyperinflation - when history already gives us the answer ? This is the inexplicable circular logic of the “Inflationist’s” and the “Gold Bugs”. Central Bankers are going to commit political and economic suicide to avert Deflation ?

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America didn't get to where it's at today by fortuity. There is and does exist a "Collective of Power". America will not be permitted to collapse – indeed most of the free world has every interest in that not occurring, just as do we, as Americans.

Despite anything said to the contrary, the reality is that without America, either Russia or China would dominate the World. The majority of the World doesn't want that by a long shot – much less the huge economic burden of self defense – a certainly if the dollar lost reserve status.

The fall of the Soviet Union represented much more than the simple demise of a Nation – or the success of American Policy – it represented the World's unequivocal rejection of Communist Leadership. That ideological question has been asked and answered.

That has laid the foundation for America's Primacy in the 21st Century. Though there are myriad other reasons, it is for this reason alone that China poses no threat to American Primacy.

Self-Interest is the true driver of Geopolitical Power. And ultimately, Geopolitics, not currencies, determines the rise and fall of Nations. America has that geopolitical power solidly.

This definitive Geopolitical Calculus is what the Dollar Doomsayers fail to grasp. China didn't give the US Reserve Currency status – nor can they take it. The Nations that did and could, won't. The "*Dollar*" is not the issue – and never was.

To paraphrase JP Morgan, "*A Bet against America is a bet you will lose*".

America can and will survive Deflation – it cannot survive Hyperinflation. These are the reasons why *Deflation* and *Protectionism* are necessary and inevitable.

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The *Chinese Stock Market* and *Bond Markets* are confirming these economic and political realities – yet the pundits are reading them with Rose Colored glasses and deluding themselves. The “Inflationist’s” and “Gold Bugs” will join the vaunted company of Irving Fischer.

The Oldest Game in the World

These events are not occurring in the abstract or by happenstance.

Ben Bernanke says “ *We got it wrong in the 1930’s and in 1970’s – but we’ve got it right now*”. He waxed infamously early in the decade that the FRB would do anything to ensure Deflation didn’t happen here, while laying the foundation for just that occurrence.

They’ll be saying the same after he’s long gone – and that period’s cycle of Inflation and Deflation are occurring. Just as then, Central Banks know exactly what they are doing – they had every intention of events occurring this way.

Inflation followed by *Deflation* is the means by which they exercise the Control to take and Redistribute Wealth as they please. It is also the means by which to countenance forces they cannot control – such as Demographics in this era that threaten the US Fiscal House.

This is the oldest game in the World – The transfer of *Wealth from the Hands of the Many to the Hands of the Few*. Central Banks are Masters of the Universe in this game – and have proven eminently that the Pen is indeed mightier than the Sword.

It is the timeless and unchanging elements of Human Behavior – *Greed, Arrogance, Fear, Hope and Self-Delusion* that permit this – and for history to repeat itself, as it is doing now.

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Maximum Differential & The Metrical Equilibrium of Housing

The *Transmission Mechanism* in the center of these Economic Machinations is Housing.

There is and does exist a Natural Economic Force which I call “Maximum Differential”, in an intangible form equal to that of Natural Physical Forces. This differential is not determinable by any calculus or methodology – but it does exist at all levels of economic activity.

It manifests itself in various forms, most notably with the onset of a general cessation of price appreciation. It is a necessary and inherent force in any economic system, and occurs through its own force once the Differential has been reached.

With respect to Housing, that differential is susceptible to a general calculus – and that is the Metrical Equilibrium of Housing vis-à-vis Wages, as set forth herein.

This is what we’ve been observing worldwide – and why it is occurring at different intervals of onset as Maximum Differential is reached in various economies of the world.

A Housing Metric of 5, 6, 7 or 8 Times Wages is *Economically Impossible*.

A person cannot earn enough money over the life of the Loan to sustain those Metrics.

This is crux of it all – and what is neither being understood nor discussed. No Government action or financial intervention can ultimately change that core reality.

It is a Metric applicable without regard to Location. This is the faux pas of the entire Housing Dialogue – and makes the entire dialogue akin to arguing “Why” the World is Flat.

Housing Values therefore can, must and will fall dramatically (*by my reckoning a Mean of 50 % or more*) to restore *Metrical Equilibrium* from having reached *Maximum Differential*.

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Trillions of Dollars in Economic Infrastructure throughout the world have been built around these faulty metrics – the unwinding of which will be epochal. More money has been created via credit than can be paid back – to the tune of trillions – and that simple fact makes Deflation both imperative and inevitable.

“Cash” will be “King” again.

Generalized Life Expenses over 30 Years

Median Annual Wages @ 50k x 30	1500k
Cost of House at Metric of 6 Times Wages w/6.5 % Note:	683k
Taxes @ Aggregate Annualized rate of 25%:	375k
Single Child @ Estimated Annualized @ 10k x 18 yrs:	180k
Automobile (1 ea 10 years at avg. of 40k)	120k
Food (300. per mo x 12 = 3600 x 30)	108k
Gasoline (Avg 15k Annual Miles Mile x .15 ea. x 30):	68k
Energy (100. per mo x 12 = 1200 x 36)	36k
Total of these Items alone:	1570k
	-70k

These are Conservative, and do not including Clothing, Healthcare, Travel, Entertainment, etc.

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Bio

Carlos is American in his mid forties living in Mexico, Privately Managing Capital for select Clients.

Carlos is a self-made Man who retired independently wealthy some 10 years ago, using that wealth to buy the most valuable commodity in the World: *Time*.

With it he pursued his Vision of Mastering the Game commonly known as “Wall Street”.

He is a Man who has the *Vision* to see what is possible and the *Confidence* to make it a reality.

He started with these simple premises: The fact that 99 % of Participants fail to beat an indexed position over time, is proof that conventional wisdom and education could not hold the keys to the Mastery of Markets; and that the Human Mind standing alone is Superior to any technology, mathematical model or degree of any kind.

Through the teachings and principles of the Great Jesse Livermore, Time, and his own Capital as Tuition, he has achieved that Vision, doubling Capital approximately every 4 years with no more than 15 % risk at any given time.

In addition to Observing the Game, Carlos is a Father, Writes, provides informal Political Perspectives to select Leaders here, is writing a book “*Ideology of Liberty*”, and is working to implement a Project to amend the *Constitution of Mexico* through the Repeal of *Article 117, Section 8*.

This Repeal will shift political and economic power to the Governors of Mexico in order to prevent the fiscal and social disaster of Oil Depletion.

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