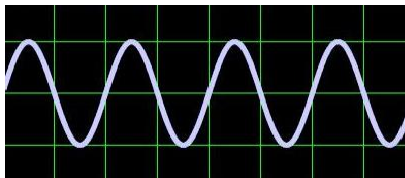




THE SEQUENCE OF EVENTS IN THE CYCLE

"Those who fail to learn from history are doomed to repeat it"



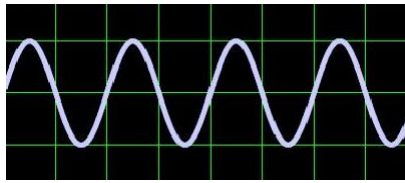
"THE IMPLICATIONS OF THE CURRENT LIFE CYCLE"

OCTOBER 2013

Garrett Jones

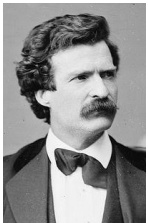
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The Sequence of Events in the Cycle

"Owners of capital will stimulate the working class to buy more and more of expensive goods, houses and technology, pushing them to take more and more expensive credits, until their debt becomes unbearable. The unpaid debt will lead to bankruptcy of banks, which will have to be nationalized, and the State will have to take the road which will eventually lead to communism." Karl Marx (Das Kapital, 1867)



"By the Law of Periodical Repetition, everything which has happened once must happen again, and again, and again -- and not capriciously, but at regular periods, and each thing in its own period, not another's, and each obeying its own law... The same Nature which delights in periodical repetition in the sky is the Nature which orders the affairs of the earth. Let us not underrate the value of that hint." Mark Twain

Mayan religion grew primarily out of the milpas agriculture which required accurate predictions of time and accommodation to the cycles of life in the rain-forest. There is one overwhelming aspect to Mayan religion: it is based on accommodating humanity to the cycles of the universe. The universe functions in a logical, cyclical, and predictable way; human beings can exploit that cyclical nature by accommodating themselves to these cycles.

Richard Hooker (Civilizations in America, 1996)



"All through time, people have basically acted and reacted the same way in the market as a result of: greed, fear, ignorance, and hope. That is why the numerical formations and patterns recur on a constant basis." Jesse Livermore (How to Trade in Stocks)

"The Kondratieff Wave is the single most important tool in economic prognostication."

Joseph A. Schumpeter (Economist and Harvard Professor)



"A prudent man foresees the difficulties ahead and prepares for them; the simpleton goes blindly on and suffers the consequences."
Proverbs 22:3

Aren't we all like a bunch of ants on a log going down the Mississippi River ... all arguing who is steering?

THE SEQUENCE OF EVENTS IN THE LONG WAVE CYCLE

“Studying the sequence of events in the Long Wave (Kondratieff Wave) cycle allows the practitioner to have a great advantage. By knowing the sequence of events in the cycle one can easily determine where we are in the cycle. If you know where you are, then you know what economic events should follow. If you know what is coming, you can plan for it and use it to your advantage rather than having it take advantage of you. It's really that simple.” GJ

In covering the sequence of events in the Long Wave cycle, we need a starting point. A logical point would be the absolute economic bottom that would define the beginning of the cycle we are currently in. The nation-wide bank holiday mandated by FDR from March 6 through March 13, 1933, would seem to best define that event.

At the bottom of the cycle, we slowly begin to rebuild a devastated economy. After the crash (1929 to 1932), debt is wiped out because most of it results in default. People are hungry and desperate -- so they are willing to work hard to get a job. There are no "slackers" because slackers don't get hired. The work that is produced is of the highest quality because there are few jobs available and only the best workers are hired. In time, this “work hard for a day's wages” permeates the society and replaced the loose attitude that was prevalent prior to the peak when most felt entitled to a job and didn't feel the need to expend any more effort than absolutely necessary. Depressions tend to improve attitudes. In a depression, if you want a job, you've got to work hard and produce a top quality product.

The process is slow, but once the economy begins to grow, debt creeps back into the picture. As businesses grow and seek expansion, the most logical and efficient method for acquiring capital is to get a loan. As the cycle progresses, business begins to boom and debt increases at a much faster rate to compensate for the demand (1960s). Demand then translates into necessity. The necessity brings on inflation and the inflation begins to rise at an increasing rate (late 1970s). Inflation then peaks due to leverage, reduced returns and increased debt (1980). The peak in inflation is usually followed by a recession lasting a year or two. This is followed by the Plateau Period which is the period following the peak in inflation. I'm sure you have heard the term “necessity is the mother of invention” – the increased demand of the period leading into the peak in inflation brings about a new technology in the Plateau Period. The semiconductor boom of the late 60s led to the computer craze of the 1980s and 1990s – the New Technology.

This ushered in the Information Age at the expense of the Industrial Age. The Plateau Period is characterized by declining rates of inflation; declining interest rates; a psychological return to "normalcy" and a roaring bull market in paper assets. The plateau period is a period of disinflation -- initially, this is inflation where the rate of inflation is declining. This new technology enhances production and, ultimately, leads to overproduction. The high debt and overproduction set the stage for deflation after many years of disinflation during the Plateau Period. The breadth of the stock market peaks (1998) which ultimately predicts a peak in stock prices (2000). This sets up a crash in the stock market (2000 to 2002). At this point in the cycle the stock market is the market of choice (technology stocks) and is the vehicle where the vast majority of investment funds reside. Later, this trend changes from disinflation to deflation.

When the stock market peaks and ultimately crashes, it puts extreme pressure on all other investments – such as real estate (2005-2008) and blue chips stocks (2007). At this point, due to the high level of debt and unemployment, people are forced into liquidation -- initially liquidating their investments, but later their homes and other valued possessions. This ultimate liquidation in society brings us to the bottom and completes the cycle. As you can see, each separate phase of the cycle sets up the next. It is perfectly logical -- it should be, Mother Nature doesn't make many mistakes.

Note: After the 2008 real estate and stock market collapses, the government chose to artificially stimulate the economy via QE1 (2008), QE2 (2010), Operation Twist (2011) and QE3 (2012), etc. This caused a rally in real estate and stock prices, but the internal deterioration continues at an accelerated rate and the events in the cycle will still continue to unfold in the same manner.

Once you know the sequence of these events, you gain a very serious advantage. The following page lists the sequence of events in the Long Wave cycle in a bullet format:

THE SEQUENCE OF EVENTS IN THE CYCLE

- The Ultimate Economic Bottom (DEBT DEFAULT; BANKRUPTCIES; BANKS CLOSED; ETC.)
- Slow Rebuilding Process (LITTLE DEBT; QUALITY WORK; DEBT SLOWLY CREEPS BACK)
- Business Expands (LOANS ARE THE MOST EFFICIENT WAY TO FUEL THE GROWTH)
- Business Booms (DEBT EXPANDS AT MUCH GREATER RATE TO MEET DEMAND)
- Increasing Inflation (DEMAND becomes NECESSITY brings on INFLATION)
- Inflation Peak (SHORTAGES; LOWER RETURNS; LEVERAGE; INCREASED DEBT)
- Plateau Period (RECESSION; DECLINING INTEREST RATES; DECLINING RATE OF INFLATION; PSYCHOLOGICAL RETURN TO NORMALCY; ROARING BULL MARKET)
- New Technology (NECESSITY is the MOTHER of INVENTION-COMPUTERS-INFORMATION AGE)
- Overproduction (NEW TECHNOLOGY enhances production and, ultimately, OVERPRODUCTION)
- Stock Market Peak (FOLLOWS PEAK IN BREADTH)
- Stock Market Crash (PARTICULARLY IN THE AREA OF THE NEW TECHNOLOGY) THERE IS AN INITIAL CRASH IN THE FAVORED MARKET SECTOR FOLLOWED BY A RECOVERY IN STOCK PRICES. LATER THE SECOND DECLINE BEGINS WHERE THE REAL SHARE DEVASTATION OCCURS
- Disinflation becomes Deflation (PRICES OF ASSETS FALL)
- Bankruptcies and Liquidation (DUE TO DEFLATION, UNEMPLOYMENT & HIGH DEBT LEVEL)
- Debt Default (INDIVIDUALS AND CORPORATIONS BELLY UP ON DEBT)
- Stock Market Bottom (TOTAL CAPITULATION) AT THIS POINT PEOPLE LITERALLY HATE STOCKS AS THEY HAVE FALLEN TO AN EXTREME LEVEL OF UNDERVALUATION
- Economic Bottom (BANK CLOSINGS; DEBT RESTRUCTURING; REMONETIZATION; NEW CURRENCY)

NOTE: WAR IS A PART OF THIS PROCESS, AS WELL. PEAK WARS OCCUR DURING PERIODS OF STRONG ECONOMIC EXPANSION (VIETNAM, WORLD WAR I); ARE A BURDEN ON THE ECONOMY; AND ARE UNPOPULAR. TROUGH WARS FOLLOW A DEPRESSION; HELP THE ECONOMY DUE TO UNEMPLOYMENT AND UNDERCAPACITY; AND ARE POPULAR (WORLD WAR II, THE CIVIL WAR, THE AMERICAN REVOLUTION). TERRORISM AND OTHER SUCH 'WILD CARDS' ENTER THE CYCLE AT VARIOUS STAGES. THIS TIME AROUND IT BEGAN IN 1970 WHEN 3 ARAB TERRORISTS ATTEMPTED TO HIJACK AN EL AL BOEING 707 AT MUNICH AIRPORT IN GERMANY AND INCREASED WITH THE EVENTS LEADING UP TO AND INCLUDING 911.



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