Run on the U.S. Dollar ....Soon

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By: DailyWealth

Porter Stansberry writes: It's one of those numbers that's so unbelievable you have to actually think about it for a while...

Within the next 12 months, the U.S. Treasury will have to refinance $2 trillion in short-term debt. And that's not counting any additional deficit spending, which is estimated to be around $1.5 trillion.

Put the two numbers together. Then ask yourself, how in the world can the Treasury borrow $3.5 trillion in only one year? That's an amount equal to nearly 30% of our entire GDP. And we're the world's biggest economy. Where will the money come from?

How did we end up with so much short-term debt? Like most entities that have far too much debt – whether subprime borrowers, GM, Fannie, or GE – the U.S. Treasury has tried to minimize its interest burden by borrowing for short durations and then "rolling over" the loans when they come due. As they say on Wall Street, "a rolling debt collects no moss."

What they mean is, as long as you can extend the debt, you have no problem. Unfortunately, that leads folks to take on ever greater amounts of debt... at ever shorter durations... at ever lower interest rates. Sooner or later, the creditors wake up and ask themselves: What are the chances I will ever actually be repaid? And that's when the trouble starts. Interest rates go up dramatically. Funding costs soar. The party is over. Bankruptcy is next.

When governments go bankrupt, it's called a "default." Currency speculators figured out how to accurately predict when a country would default. Two well-known economists – Alan Greenspan and Pablo Guidotti – published the secret formula in a 1999 academic paper. The formula is called the Greenspan-Guidotti rule.

The rule states: To avoid a default, countries should maintain hard currency reserves equal to at least 100% of their short-term foreign debt maturities. The world's largest money-management firm, PIMCO, explains the rule this way: "The minimum benchmark of reserves equal to at least 100% of short-term external debt is known as the Greenspan-Guidotti rule. Greenspan-Guidotti is perhaps the single concept of reserve adequacy that has the most adherents and empirical support."

The principle behind the rule is simple. If you can't pay off all of your foreign debts in the next 12 months, you're a terrible credit risk. Speculators are going to target your bonds and your currency, making it impossible to refinance your debts. A default is assured.

So how does America rank on the Greenspan-Guidotti scale? It's a guaranteed default.

The U.S. holds gold, oil, and foreign currency in reserve. It has 8,133.5 metric tonnes of gold (it is the world's largest holder). At current dollar values, it's worth around $300 billion. The U.S. strategic petroleum reserve shows a current total position of 725 million barrels. At current dollar prices, that's roughly $58 billion worth of oil. And according to the IMF, the U.S. has $136 billion in foreign currency reserves. So altogether... that's around $500 billion of reserves. Our short-term foreign debts are far bigger.

According to the U.S. Treasury, $2 trillion worth of debt will mature in the next 12 months. So looking only at short-term debt, we know the Treasury will have to finance at least $2 trillion worth of maturing debt in the next 12 months. That might not cause a crisis if we were still funding our national debt internally. But since 1985, we've been a net debtor to the world. Today, foreigners own 44% of all our debts, which means we owe foreign creditors at least $880 billion in the next 12 months – an amount far larger than our reserves.

Keep in mind, this only covers our existing debts. The Office of Management and Budget is predicting a $1.5 trillion budget deficit over the next year. That puts our total funding requirements on the order of $3.5 trillion over the next 12 months.

So... where will the money come from? Total domestic savings in the U.S. are only around $600 billion annually. Even if we all put every penny of our savings into U.S. Treasury debt, we're still going to come up nearly $3 trillion short. That's an annual funding requirement equal to roughly 40% of GDP.

Where is the money going to come from? From our foreign creditors? Not according to Greenspan-Guidotti. And not according to the Indian or Russian central banks, which have stopped buying Treasury bills and begun to buy enormous amounts of gold. The Indians bought 200 metric tonnes this month. Sources in Russia say the central bank there will double its gold reserves.

So where will the money come from? The printing press. The Federal Reserve has already monetized nearly $2 trillion worth of Treasury debt and mortgage debt. This weakens the value of the dollar and devalues our existing Treasury bonds. Sooner or later, our creditors will face a stark choice: Hold our bonds and continue to see the value diminish slowly, or try to escape to gold and see the value of their U.S. bonds plummet.

One thing they're not going to do is buy more of our debt. Which central banks will abandon the dollar next? Brazil, Korea, and Chile. These are the three largest central banks that own the least amount of gold. None owns even 1% of its total reserves in gold.

All of this is going to lead to a severe devaluation of the U.S. dollar... Which I expect to happen within 18 months. I examined these issues in much greater detail in the most recent issue of my newsletter, Porter Stansberry's Investment Advisory, which was published last week. Coincidentally, America's paper of record – the New York Times – repeated our warnings (nearly word for word) last weekend. Word is getting out.

If you haven't taken steps to protect yourself from the coming devaluation – like owning gold and silver bullion, foreign real estate, and farmland – make sure you do it soon. The dollar rout is coming.

http://www.marketoracle.co.uk/Article15449.html