SPECIAL REPORT

A Phoenix Capital Research Publication

Financial Crisis "Round Two" Survival Guide

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Many investors believe that the 2008 Crisis was THE Crisis of their lifetimes.

They are mistaken.

The 2008 Crisis was a stock and investment bank crisis. But it was not THE Crisis. It was just Round One.

Round Two, or THE Crisis, concerns the biggest bubble in financial history: the epic Bond bubble… which, as it stands, is north of $100 trillion.

To put this into perspective, the Tech Bubble was about $8 trillion in size. The Housing Bubble, which triggered the 2008 Crisis, was about $14 trillion in size.

The bond bubble today is over $100 trillion. And if you include derivatives that trade based on the prices of bonds, it's $555 trillion.

So we are talking about a problem that is exponentially larger than anything you or I have seen before.

How is this possible?

By way of explanation, let's consider how the current monetary system works…

The current global monetary system is based on debt. Governments issue sovereign bonds, which a select group of large banks and financial institutions (e.g. the Primary Dealers in the US) buy/sell/ and control via auctions.

In This Report

- An explanation of the REAL Crisis and what it will look like.
- The first sign that the next round of the Crisis has already begun.
- Three strategies to protect your wealth from this Crisis.
- How to take out "catastrophe insurance" on your portfolio (if you have to stay invested in stocks).

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These financial institutions list the bonds on their balance sheets as "assets," indeed, the *senior-most assets* that the banks own.

The banks then issue their own debt-based money via inter-bank loans, mortgages, credit cards, auto loans, and the like into the system. Thus, "money" enters the economy through loans or debt. In this sense, money is not actually capital but ***legal debt contracts.***

Because of this, the system is inherently leveraged (uses borrowed money).

Consider the following:

1) Total currency (actual cash in the form of bills and coins) in the US financial system is a little over $1.2 trillion.

2) If you want to include money sitting in short-term accounts and long-term accounts the amount of "Money" in the system is about $10 trillion.

3) In contrast, the US bond market is well over **$38 trillion.**

4) If you include derivatives based on these bonds, the US financial system is north of $191 trillion.

Bear in mind, ***this is just for the US.***

Indeed, globally there roughly $199 trillion in bonds in existence.

A little over a third of this is in the US. About half comes from developed nations outside of the US (Germany, Japan, etc.). And finally, emerging markets make up the remaining 14%.

The size of the *bond* bubble alone should be enough to give pause.

However, when you consider that these bonds are pledged as collateral for other securities (usually over-the-counter derivatives), the full impact of the bond bubble explodes higher to $555 TRILLION.

To put this into perspective, the Credit Default Swap (CDS) market that nearly took down the financial system in 2008 was only a tenth of this ($50-$60 trillion).

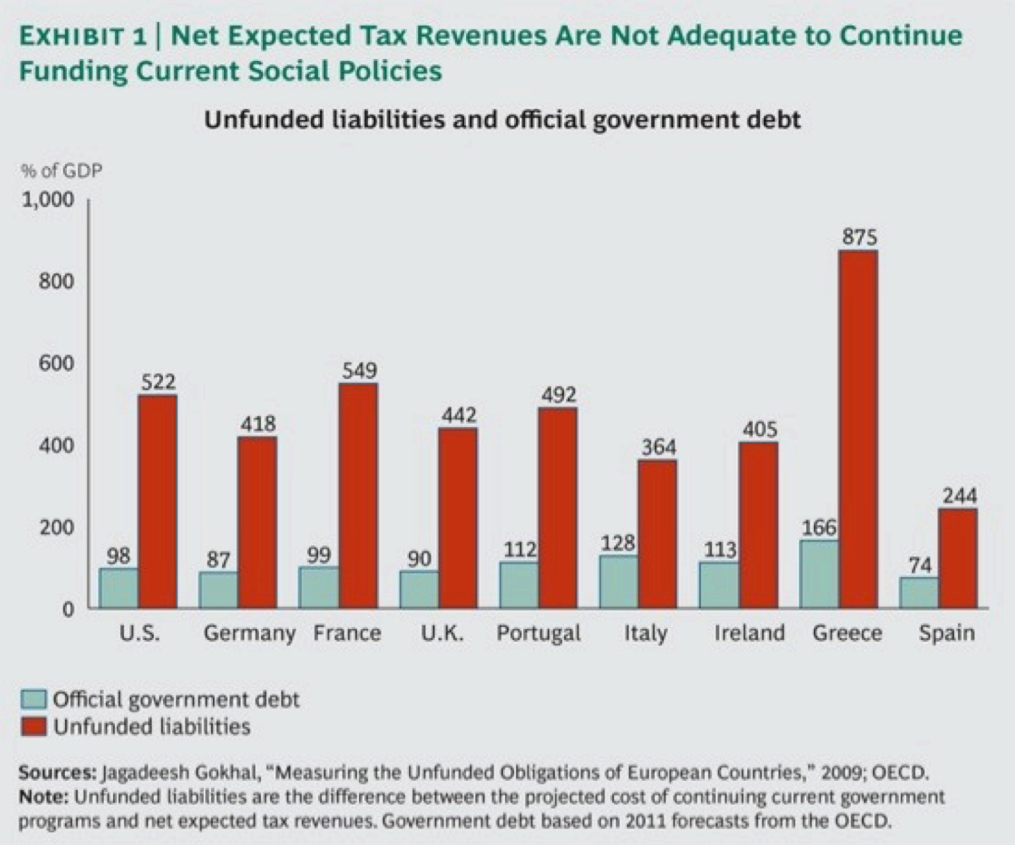
Moreover, you have to consider the *political* significance of this bubble.

For 30+ years, Western Governments have been papering over the decline in living standards by issuing debt. In its simplest rendering, sovereign nations spent more than they could collect in taxes, so they issued debt (borrowed money) to fund their various welfare schemes.

This was usually sold as a "temporary" issue. But as politicians have shown us time and again, overspending is *never* a temporary issue. This is compounded by the fact that the political process largely consists of promising various social spending programs/ entitlements to incentivize voters.

In the US today, a whopping 47% of American households receive some kind of Government benefit. This type of social spending is not temporary… this is endemic.

The US is not alone… Most major Western nations are completely bankrupt due to excessive social spending. And ALL of this spending has *<u>been fueled by bonds</u>*.



This is why Central Banks have done everything they can to stop any and all defaults from occurring in the sovereign bond space. Indeed, when you consider the bond bubble **<u>everything Central Banks have done since 2008 begins to make sense.</u>**

1) Central banks cut interest rates to make these gargantuan debts more serviceable.

2) Central banks want/target inflation because it makes the debts more serviceable and puts off the inevitable debt restructuring.

3) Central banks are terrified of *debt deflation* because it would burst the bond bubble and bankrupt sovereign nations.

So how will the bond bubble play out?

The first real sign of trouble has already emerged. That sign pertains to the US Dollar.

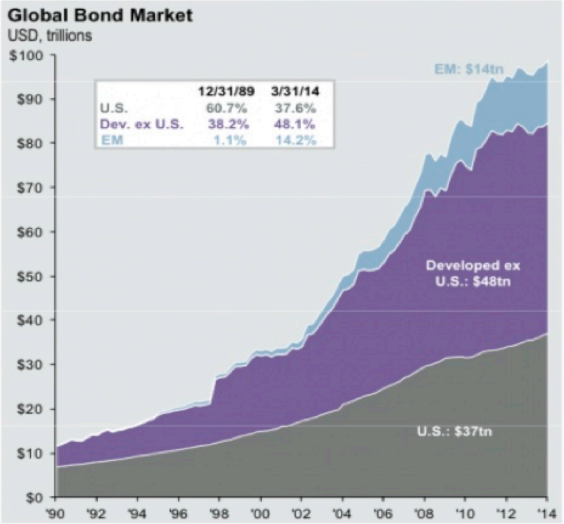
The blogosphere is rife with talk of the end of the Dollar. Everywhere you look, there is talk of the Dollar dying or being replaced as the global reserve currency.

The Dollar will end, as all fiat currencies do, but not until we reach the End Game of the current financial system. The US Dollar is the reserve currency of the world. Almost everything on the planet is priced in Dollars. The US Dollar is the single most liquid security **in the world.** And almost everyone in the world *borrows* in US Dollars.

When you borrow in US Dollars to invest in something else, you are effectively *shorting* the US Dollar. For this set-up, the less volatility the US Dollar has, the lower the risk of your position blowing up (if the US Dollar rallies, your potential returns erase very, very quickly).

With that in mind, between 1999 and 2014 the US Dollar was in a consolidation period. It is no coincidence that it was during this period that we began to experience one asset bubble after another culminating in the bond bubble.

In simple terms, as the Dollar's volatility *DECREASED*, global bond issuance ***INCREASED.***



As recently as the year 2000, the bond bubble was a mere $30 trillion. But as the Dollar weakened and became range bound, the global bond market <u>MORE THAN TRIPLED</u>

Indeed, investors were so excited about the US Dollar's lack of volatility that they borrowed an additional **$9 trillion** in US Dollars to invest into other asset classes.

This is called a **<u>carry trade</u>**. And it was literally the fuse for the global debt bomb. A carry trade only works as long as the currency in which you are borrowing remains stable or weakens. As soon as that currency **<u>strengthens</u>**, your investment blows up very quickly.

Which is precisely what happened in mid-2014.

In June 2014, the ECB cut interest rates to *negative* in the Eurozone. When this happened, everyone who had been borrowing US dollars to invest in Europe began to watch their gains evaporate. This forced capital to escape the EU and move back into the US Dollar.

<u>And that's when the $9+ TRILLION US Dollar carry trade began to blow up.</u>

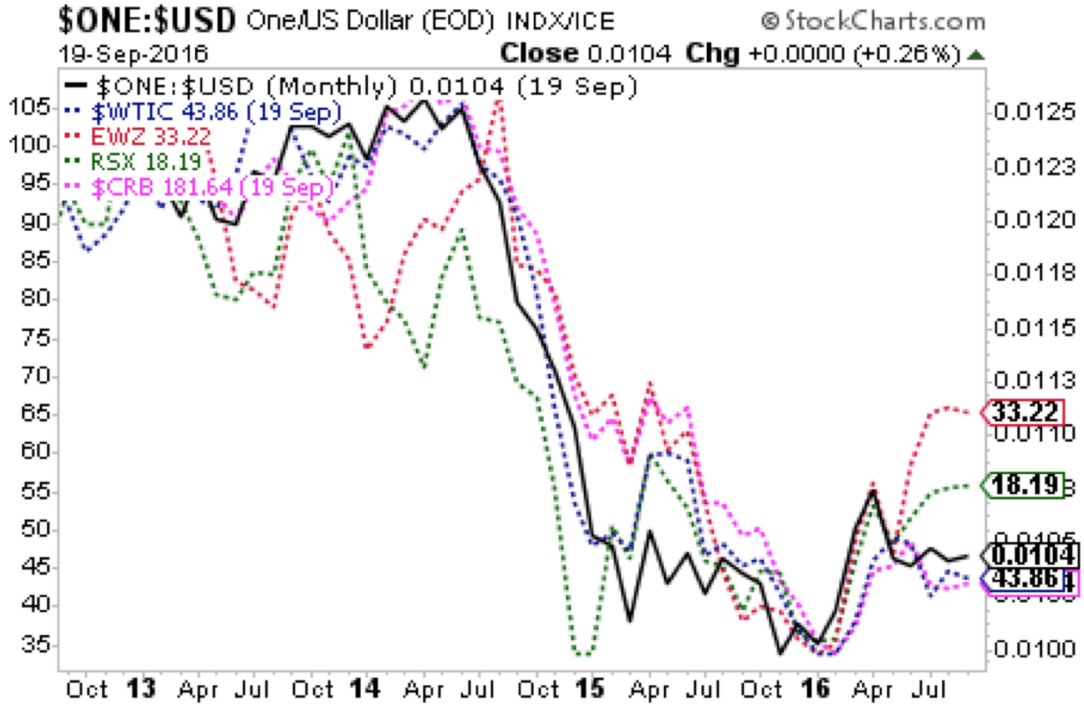
Soon after this, the US Dollar moved over 4% in a SINGLE MONTH. That was just the beginning. Within six months the US Dollar moved over 10%, then 20%.

This move coincided with the first wave of the riskiest bonds denominated in US Dollars (junk bonds) blowing up. THE TIMING OF **<u>THESE TWO ITEMS IS NOT COINCIDENTAL.</u>**

Indeed, as the US Dollar rally began to intensify, the emerging market space got crushed. Most commodities like Oil are priced in US Dollars. If you invert the US Dollar (meaning when it strengthens, the chart line falls), you'll see that Oil, and commodities in general got wiped out by the US Dollar rally.

The below chart shows an *inverted* US Dollar (meaning when the Dollar strengthens, the black line falls), Oil (blue line), Brazilian stocks (red line), Russian stocks (green line) and commodities in general (pink line).

As you can see, the US Dollar rally pulled down ALL of these assets almost tick-for-tick. Since that time these assets have been consolidating as they prepare for the next BIG move.



This situation will only be getting worse as the US Dollar carry trade continues to blow up in the coming months. Remember, when you borrow in US Dollars, you are effectively *shorting* US Dollars. In this scenario, when the US Dollar rallies, you get crushed and are forced to cover, default, refinance, etc.

All of these actions (repay your debt, default, or refinancing) **decrease the number of US Dollars in the system.** This in turn makes the US Dollar rally more. And thus begins the end game for the financial system.

Indeed, the long-term chart of the US Dollar indicates that we could very well see the last 30 years worth of leverage get eviscerated in the coming months.

This is the single largest chart formation **in modern financial history.** This is a 40+ year bullish falling wedge pattern. And the upside target is 130 or higher.

What does this mean?

Every single investment that is based on a cheap **US Dollar will be blowing up.**

This will not happen all at once. We are very likely entering a 5+ year US Dollar bull market. However, given what is at stake here (the financial system) Central banks and the political elite won't let this happen without a fight.

This is why I believe this process will likely take more than two years. Much like the Tech Bubble, there will be 20% crashes in asset prices (see the recent collapse of Oil and commodities), but there will also be rallies as well.

In simple terms, the $199 trillion bond bubble will implode. As it does, the financial system will begin to deleverage as debt is defaulted on or restructured (reducing the amount of US Dollars in the system, pushing the US Dollar higher).

By the time it's all over, I expect:

1) Numerous emerging market countries to default and most emerging market stocks to lose 50% of their value.

2) The Euro to break below parity before the Eurozone is broken up (eventually some new version of the Euro to be introduced and remain below parity with the US Dollar).

3) Japan to have defaulted and very likely enter hyperinflation.

4) US stocks to lose at least 50% of their value and possibly fall as far as 400 on the S&P 500.

5) Gold to break above $2,000 and likely go to $5,000 (only after Central Banks unveil the "nuclear" round of QE in response to the crisis).

6) Numerous "bail-ins" in which deposits are frozen and used to prop up insolvent banks.

7) The Too Big to Fail banks to ultimately go bankrupt and very likely be broken up.

This is indeed some scary stuff. However, fortunately there are some very basic strategies you can employ to preserve your wealth through this.

Strategy #1: Move Into US Dollars

Perhaps the easiest step you can take is to move a portion of your capital out of various risk assets and into US Dollars.

As I explained earlier, we are entering a stage of global deleveraging. This will reduce the amount of US Dollars in circulation. Between this and the US Dollar carry trade blowing up, the US Dollar is likely entering a multi-year bull market.

"*But wait,"* you say, "*what if you're early and the bubble hasn't burst yet? Won't I miss out on gains if I sell stocks and move into the US Dollar?"*

The US Dollar actually OUTPERFORMED the S&P 500 in 2014. You could have sat on the sidelines the whole year and seen a greater increase in your overall purchasing power than if you'd bought an index fund (which most investors can't beat anyway).

This trend has continued in 2015: the US Dollar has dramatically outperformed the stock market once again.

During the last two US Dollar bull markets, the US Dollar rose roughly 50%. During the same time periods, stocks fell over 20%. If we are in a multi-year US Dollar bull market as I believe we are, having your capital in US Dollars will not only reduce your portfolio risk but will actually GROW your purchasing power more rapidly than if you owned stocks!

Strategy #2: Buy Some Bullion (both Gold and Silver)

Another easy way to prepare for the bond bubble's bursting is to move a portion of your wealth into Gold or Silver bullion. Because many investors are unfamiliar with this asset class, I've arranged this strategy in a Question and Answer form.

What is bullion?

Bullion is simply another term for actual, physical Gold or Silver as opposed to "paper" Gold or Silver, which trades via either the futures market or in one of the various Gold-or Silver-based Exchange Traded Funds (ETFs).

Bullion comes in one of two forms: coins or bars. Coins typically contain an ounce of pure Gold or Silver. Bars range in size from one ounce up to 400+ ounces. You can buy either for a small premium over "spot" price or the current market value of Gold or Silver.

What are the most common forms of bullion?

In terms of gold coins, there are three coins that comprise the bulk of the bullion market. They are Kruggerands, Canadian Maple Leafs, and American Gold Eagles. We suggest avoiding Maple Leafs because they can easily be scratched which damages the gold and reduces the coin's value.

In terms of Silver coins, the easiest way to purchase bullion is via pre-1965 coins (often termed "junk" silver). However, you can also get silver one-ounce rounds (coin-like medallions) or Silver Eagle coins which also contain one ounce of Silver.

In terms of bars, you can buy either Gold or Silver bars in a variety for forms. However, they are much bulkier, usually weigh considerably more, and are harder to move around.

Why should I own bullion?

Historically, many investors have argued that there was no point to owning bullion since it didn't produce any cash flow. However, with the majority of Government bonds now yielding less than 1% and over $5 trillion sporting **negative** yields, this argument is no longer valid.

Owning bullion is a means of securing your wealth outside of "paper money" or the cash that the Central Banks want to tax. Provided you store it securely, it's a means of preserving your capital and keeping it under **your control**.

Why should I own bullion instead of an Exchange Traded Fund (ETF) that owns bullion?

There is considerable evidence to suggest that the Gold and Silver ETFs do not actually have all the Gold or Silver they claim to. However, regardless of whether this is completely true, at the end of the day it is much safer to have your own physical Gold or Silver *in hand* as opposed to buying a paper-based ETF run by a bank or other financial entity that *claims* it owns Gold and Silver.

After all, if the firm that owns the Gold goes bankrupt, there's no guarantee that you'll get your hands on your share of the bullion any time soon, if at all. This completely defeats the purpose of buying Gold or Silver: to store your wealth safely.

How much Gold or Silver bullion should I buy?

How much you purchase is up to you. We suggest having at least several months' worth of expenses in Gold *and* Silver bullion. Some investing legends have as much as 20% of their portfolios in bullion.

Why should I buy both Gold *and* Silver?

Because if a bank holiday is ever declared… or if paper money is worthless, you don't want to be walking around with an ounce of gold (worth $1k+) to buy groceries.

Instead, you will want some precious metals of smaller denomination to purchase goods or barter with, hence the need for some Silver.

How do I buy Gold or Silver bullion?

The safest way to buy bullion is from a dealer. There are literally hundreds of dealers to choose from. The US mint provides a list of authorized coin dealers on its website:

http://www.usmint.gov/mint_programs/american_eagles/?action=lookup

We cannot tell you which dealer to go with, but look for someone who's been dealing for years (not a newbie). You should ALWAYS ask for references from the dealer (former clients you can talk to about their purchases/ experiences).

Be sure to talk to the dealer for some time and ask him or her numerous questions about the industry, different types of coins, etc. (feel free to test him or her on the information we've provided you with above e.g. the three most liquid Gold coins, etc.).

If they can answer everything you ask in a knowledgeable fashion, their references check out, and you verify everything they say with a 3rd party, you should be OK.

Some warning signs to avoid are dealers who try to store your bullion. *Never*, *ever* store your bullion with someone else. *Always* store it yourself.

How should I store my bullion?

In terms of storing your bullion, you can store it in a safe deposit box at a bank or buy a home safe from Target or Wal-Mart (or a specific safe store). Personally, I distrust safe deposit boxes because part of the reason for having Gold or Silver on hand is in case there's a run on the banks or a bank holiday is declared. For that reason, I suggest having at least some bullion in a personal safe.

You can get a decent safe for anywhere between $100 and $1,000. Both Target and Wal-Mart sell decent models for $50-$300. However, there are plenty of other more sophisticated safes out there.

On a side note DO NOT tell people about your bullion stash OR your safe. Trust virtually NO ONE with this information except your closest loved ones (and we mean CLOSEST).

If I buy bullion and the crisis doesn't hit soon… won't I miss out on stocks' gains?

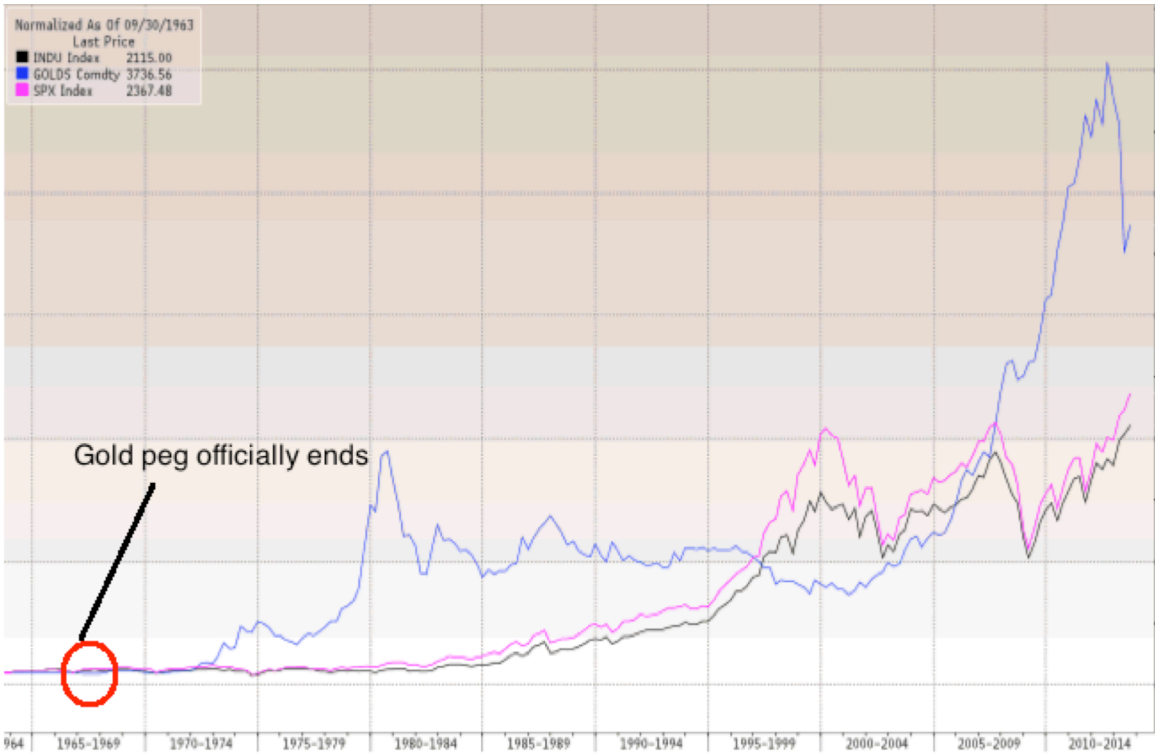
No. CNBC will never tell you this, but the fact of the matter is that Gold *has dramatically outperformed* the stock market for the better part of 40 years.

I say 40 years because there is no point comparing Gold to stocks during periods in which Gold was pegged to world currencies. Most of the analysis I see comparing the benefits of owning Gold to stocks goes back to the early 20th century.

However Gold was pegged to global currencies up until 1967. Stocks weren't. Comparing the two during this time period is just bad analysis.

Once the Gold peg officially ended with France dropping it in 1967, the precious metal has outperformed both the Dow and the S&P 500 by a massive margin.

See for yourself… the below chart is in normalized terms courtesy of Bill King's *The King Report.*



According to King, Gold has risen 37.43 fold since 1967. That is more than *twice the performance of the Dow over the same time period* (18.45 fold). So much for the claim that stocks are a better investment than Gold long-term.

Indeed, once Gold was no longer pegged to world currencies there was only a single period in which stocks outperformed the precious metal. That period was from 1997-2000 during the height of the Tech Bubble (the single biggest stock market bubble in over 100 years).

In simple terms, as a long-term investment, Gold has been better than stocks for over 40 years. So owning Gold bullion, like US Dollars, will not only shelter your capital from systemic risk, but will actually GROW your purchasing power more rapidly!

Strategy #3: If You Must Own Stocks, Move Into High Quality Companies

If you DO have to stay invested in stocks, you should shift into High Quality, Blue Chip companies.

The reasons for this are as follows:

1) High Quality, Blue Chip stocks will fall less than smaller, riskier companies when the Crisis hits.

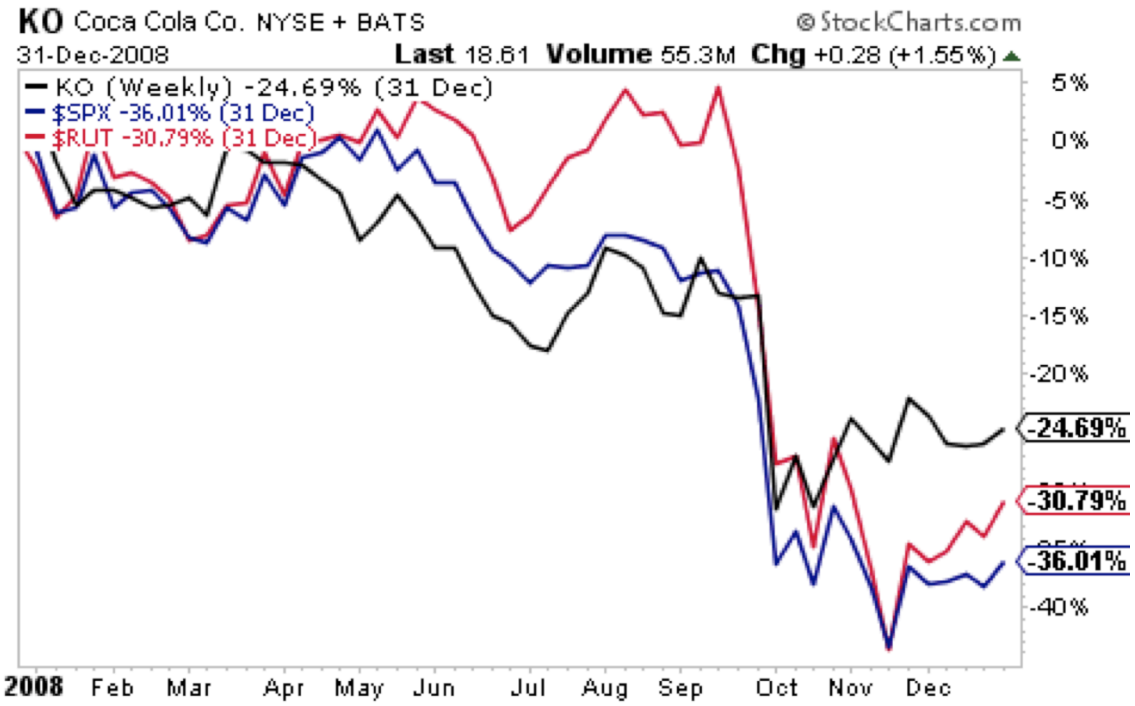
2) High Quality, Blue Chip companies have more stable profits and so will be able to pay out dividends during market downturns.

3) High Quality, Blue Chip companies are actually even MORE attractive when their prices fall.

Consider Coca-Cola (NYSE: KO) as an example.

KO is one of the best, most profitable brands in the world. The competitive moat around this business is extraordinary and it remains one of the most easily recognized franchises on the planet. You can drink six glasses of Coke a day and still enjoy it the next day. That quality is almost nowhere to be found in any other food/ beverage on the planet: even chocolate would get old after six bars a day.

The quality of this business shone during the 2008 Crisis, when KO's stock only fell 24% compared to the S&P 500's drop of 36% and the Russell 2000's drop of 30%.



Not only did KO actually grow profits during a year in which the global economy imploded, but it actually increased its dividend. So those investor who held throughout the crisis were actually paid to wait.

Moreover, when KO's stock fell it became even more attractive as an investment.

Let me explain.

Volatility can either hurt you or be your friend. Most people would sell a position if it fell 20-30%. This is wise if you're investing based on momentum. However, if you're investing based on value, then doing this is completely antithetical to attaining high returns.

Consider Coke. Let's say Coke's share price collapsed 50% from $40 to $20 per share. Most investors would panic and sell. A value investor, on the other hand, would be buying greedily.

Why?

Because Coke's business has a fundamental value. Even during a Financial Crisis and Depression, people will continue to drink soda.

So the opportunity to buy Coke at $20 a share would be truly an extraordinary opportunity. Indeed, from an income perspective alone, the investment potential here would be fantastic.

Consider that in 2008 when everyone thought the world was ending, Coke paid out $0.76 in dividends. With shares at $20, this meant a dividend yield of 3.8%, which is a very reasonable return.

However, let's say you were wise enough to recognize that Coke offered even MORE value at $18 and added to your position in Coke when its shares fell to $18.

If you did this, and held on to your position, you would currently be locking in a massive yield.

In 2014, KO paid out $1.22 per share in dividends. **Based on your buy price of $18 per share, you would be collecting a massive return of 6.7% per year ($1.22/ $18.00 = 6.7%) from your investment.**

Like I said before, High Quality Blue Chip companies like Coke are even MORE attractive when their share prices fall.

So, if you HAVE to remain invested in stocks to the long side for whatever reason, now is the time to be moving into high quality companies. This means finding companies with low debt,

lots of cash, strong results (KO actually GREW revenues in 2008), and significant competitive advantages.

Also, and this is critical, look for companies with strong balance sheets: companies that will still EXIST if there's another Crisis. Depression or no, people will still drink soda, alcohol, smoke cigarettes, and need medicine. I've compiled a list of companies you should consider if you need to remain involved in stocks going forward:

Company	**Symbol**	**Sector**
Coca-Cola	KO	Beverages
Budweiser	BUD	Alcohol
Johnson & Johnson	JNJ	Healthcare
Wal-Mart	WMT	General Retail
Exxon Mobil	XOM	Oil & Gas
Kraft Heinz	KHC	Food and Beverages
Microsoft	MSFT	Software
Pfizer	PFE	Pharmaceuticals
Intel	INTC	Microchips
Procter & Gamble	PG	Consumer Goods

I want to stress that these investments are only if you HAVE to stay in stocks for some reason. If there is another collapse these companies will fall like everything else. However, they will likely fall less than the rest of the market.

Strategy #4: Catastrophe Insurance: Trades For When the Collapse Hits

This final strategy is not without risk. You should only consider the investments detailed here if you are an active trader (someone who knows how to read market movements on a week by week basis).

The reason for this is that should the Crisis go systemic and begin to take down large banks, you could very well lose all of the capital you put into these trades (more on this later).

Having said that, there are a number of ways you can profit from the markets falling.

They include:

1) Buying puts (options that profit when the market falls).

2) Shorting futures

3) Buying UltraShort ETFs

Of these three, UltraShort ETFs are the most accessible to ordinary investors.

If you're unfamiliar with UltraShort ETFs, these are investments that return two times the inverse performance of a particular ETF. Consider the UltraShort Financials ETF (SKF) as an example.

SKF returns two times the inverse of the Financials ETF (IYF). So if IYF falls 5%, SKF rises 10%. If IYF falls 10%, SKF rises 20%. And so on.

There are quite a few UltraShort ETFs you can use to profit from a collapse in different market indexes or in individual sectors.

Below is a list of the most liquid, popular UltraShort ETFs.

1) **The UltraShort S&P 500 ETF (SDS)**

2) **The UltraShort Dow Jones Industrial Average (DXD)**

3) **The UltraShort Russell 2000 ETF (TWM)**

4) **The UltraShort Financials ETF (SKF)**

5) **The UltraShort Real Estate ETF (SRS)**

6) **The UltraShort Materials ETF (SMN)**

7) **The UltraShort Emerging markets ETF (EEV)**

8) **The UltraShort China ETF (FXP)**

9) **The UltraShort Brazil ETF (BZQ)**

As I stated before, these investments are not without their risk.

The reason is that they are in fact based on derivatives owned by the large banks.

Put another way, when you buy the UltraShort Financials ETF (SKF) you are not actually shorting all of the financial companies' stocks located in the Financials ETF (IYF).

Instead, you own the rights to derivatives that are meant to produce the intended return the UltraShort ETF promises. Because of this, should the bank or financial entity that issues the UltraShort ETF go bankrupt, **it's possible you could lose your position entirely.**

This would not happen instantly. All Crisis take time to unfold. The Tech Crash, for instance, took two years to complete.

So when the next Crisis hits, there will a window of time in which UltraShort ETFs will offer you the chance to see enormous returns. However, at some point, if the Crisis gets bad enough, it will be best to get out of these investments altogether.

I cannot tell you when this would be as it will all be contingent on how Central Banks react to the next round of the Crisis as well as your personal risk appetite.

All I can say is that when the markets take a nosedive, UltraShort ETFs will offer the potential for extraordinary gains. But once the Crisis becomes truly systemic (meaning banks are failing) UltraShort ETFs will no longer be safe to invest in.

This concludes this Special Report. In it, we've outlined the nature of the bond market bubble, explained how the US Dollar carry trade has already lit the fuse on the next Crisis, outlined three easy to implement strategies to protect your wealth from the coming Crisis, and detailed how you can use UltraShort ETFs to profit from a market collapse.

Thank you for reading…

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