

# Debt Default and Today's Bail-Ins: Recalling the 1931 Austrian Credit Anstalt Financial Domino

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*The revelation over this past weekend by Hypo Alpe-Adria has been called by some as Austria's "Lehman moment". This may very well be on a micro scale, I believe it to be the Credit-Anstalt moment on a macro scale. If you recall history, Austrian bank Credit-Anstalt was the first domino to fall in 1931 which spread across the globe and tipped the banking system into default mode.*

There are many similarities to the world today as compared to that world of 1931. Debt had become prevalent leading into the stock market panics of 1929. Margin debt had exploded and caught many offside just as it did in 2007-2009. The more recent episode had even more leverage via the use of derivatives, I point this out because the "leverage ratios" are far higher today than they were 80 years ago.

The world was also in the midst of currency wars. Back in the 1930's, the global economy had slowed (just as it has today) and consumption was not keeping up with production. This same anomaly exists today in the zones (think China and Asia) where production has been moved to lower costs. What happened in the 1930's was considered a time of "beggar thy neighbor". Countries purposely weakened their own currencies in order to undercut the sales price of goods produced by other countries. This morphed into trade wars and ultimately WW II. Other similarities were the fact that after 1929, unemployment rose, economic activity slowed and the financial sector was being squeezed with weakening and defaulting loans. Current day by no means is a carbon copy to where it was back in 1931, but there is a definite "rhyme" to it.

So, what exactly does the current "Hypo moment" mean? For one thing, it means that nothing was really fixed from the last episode. If "things" were good and getting better, how could a bank which was recapitalized (at the bottom) ...fall even further? The answer of course is the economy and financial systems are not "better". As I have tried to write all along, the problems were glossed over and dead bodies swept under the rug. Hypo, is simply the tip of the iceberg and a harbinger of more, similar things to come.

I would be remiss if I did not mention one major difference between the 1930's, the days of Lehman collapsing ...and now. The most dangerous "cure" undertaken in 2008 and onward is governments and their central banks putting their own balance sheets on the line. You see, this did not happen in the 1930's, if a bank went bad ...it went under. Yes, captains of industry did make efforts to save things but the federal government largely stayed out of it. Not so today. Almost nothing was allowed to go under up and until Lehman was "allowed" to fail. No one (very few) dreamed how quickly and completely credit dried up after Lehman failed. THIS is the reason nothing else was allowed to fail afterward, fear of a domino effect

taking everything with it.

Last year, the U.S., Europe, Britain, Canada and others all figured out they could not go another round of bailouts. It is not that they had a come to Jesus moment and decided to let losers, lose. No, these governments ALL figured out the simple math they could no longer AFFORD to bailout insolvent institutions, especially the behemoths. This is why the legislation of “bail ins” came forth. But, there is still a big problem with governments allowing market forces to cleanse bad debt and bad banks ... the size and scope of the losses involved!

I am not just talking about the size of the losses although this is certainly important. No, I am speaking of the “number” of losses and what “investors” will then decide to do. Allowing bail ins to occur will mobilize investors in a hurry. Once people figure out they are creditors of their bank, they will begin to move. Even though the bail in laws were passed last year, publicized and known about ...no one cared because it hadn't happened to anyone. This will now most likely change with Hypo and people will see a real case of real losses!

A move to “safety” is what we should begin to see shortly. The previous moves had been that of moving to yield because very little was available. Safety, or “risk” did not matter because no one was ever allowed to lose. This of course has changed with the Hypo moment. If made to wager, the Hypo moment may be very much like the Lehman moment in that it may be the last insolvency allowed. This is a very hard one to call because both choices lead to the very same “death” though by different means. We can go the route of bail ins where depositors are spooked into bank runs all over the world ...or, resume more bailouts and fund them with QE.

In reality, the original questions back in 2008-09 have not been answered nor really even addressed. Nothing has been fixed, nothing has improved and truth is, nothing has changed. The question, or more to the point the reality of “inflate or die” is still there. Though we watched this fade into the background by the “inflations” of the various and global QE undertakings, the choice must be again made ...inflate (again) or die... which poison will be chosen?!

This is a very interesting crossroads because given the choice, inflation will be chosen and thus further currency debasement and destruction. The problem is deflation continues to gnaw away at bank “assets”, Hypo being the first admission. If there are losses taken and “creditors” made to pay, masses will decide they do not want to be in “creditor status”. Bank runs will (and the sale of all sorts of financial credits) follow. The global banking system will become unfunded so to speak in very rapid fashion. All this boils down to is one very simple choice, “choosing your poison”. The only question remaining is whether the choice is allowed or do market forces rule and decide for the central bankers?

What does this mean to you? It means you need to decide whether you want to be a creditor, or whether you want to be an asset holder. Currencies, and the institutions that “hold them” for you will be weakened and “run”. Your obvious alternative is to become your own bank ...holding real money that cannot default. The key to this game is not to be defaulted upon. The only way to do this is by having no counterparty risk to your account nor your currency. Gold in hand is your obvious solution, this decision will be obvious very soon.

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Bill Holter writes and is partnered with Jim Sinclair at the newly formed Holter/Sinclair collaboration. Prior, he wrote for Miles Franklin from 2012-15. Bill worked as a retail stockbroker for 23 years, including 12 as a branch manager at A.G. Edwards. He left Wall Street in late 2006 to avoid potential liabilities related to management of paper assets. In retirement he and his family moved to Costa Rica where he lived until 2011 when he moved back to the United States. Bill was a well-known contributor to the Gold Anti-Trust Action Committee (GATA) commentaries from 2007-present.

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