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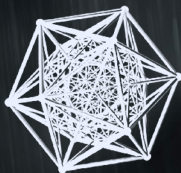

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Turbulence

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by
Anthony Patch

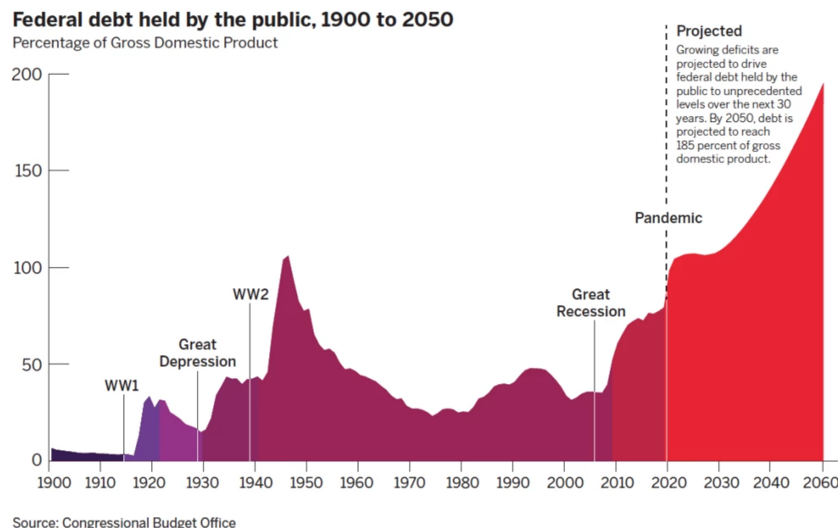
"For there is nothing hidden that will not be disclosed, and nothing concealed that will not be made known and brought to light."

Luke 8:17

According to the document entitled, Bank For International Settlement Review of December 2022, the derivatives market is set to detonate. This will trigger the "Great Reset".

In this first issue of Entangled magazine for 2023, we report on the unseen corruption within the global derivatives market. The off-balance sheet data remains unseen by economic analysts.

On the other hand, the growing U.S. Federal debt, on display to the general public, reflects a significantly smaller portion of the overall global derivatives debt.



Turbulence

: the quality or state of being turbulent: such as

a

: great commotion or agitation

emotional *turbulence*

b

: irregular atmospheric motion especially when characterized by up-and-down currents

Merriam-Webster

The cover of this month's Entangled magazine displays a plane flying through a storm. Understood, inside, the passengers experience turbulence. This can become very unsettling. Fear sets in, and panic ensues. Not so on "Patch Air". We are determined to face this storm, not in our own strength, but with the grace and wisdom granted to us through the Holy Spirit.

Within the pages of this 68th edition of Entangled magazine, we are focusing singularly on the fast-approaching financial turbulence.

We will reveal through the Bank For International Settlement Review for 2022 source document the hidden causes for the present and worsening economic turbulence, leading to the imminent global "Great Reset."

Historically speaking, the Great Financial Crisis (GFC) of 2007-8 served as the repackaging of existing debt instruments and the continued rolling over of the derivatives markets. The losses measured in loan defaults of all types: depletion of pension funds, evaporation of 401k accounts, Credit Default Swaps (CDSs), and unpaid insurance liabilities, exceeded $5 trillion in 2008 (5 x 7.1% inflation = $35.5 trillion today).

In 2023, it will become too expensive to rollover the derivative debt. According to a review published in December 2022 by the Bank For International Settlements (BIS), the derivatives futures and options are estimated by the BIS at over $97 trillion, 80% of which is denominated in US dollars. Systematically, derivatives are set to expire on the last Thursday of every month. Typically, a rollover decision is made based upon an assumption as to whether an existing market momentum to the positive would continue.

Bank For International Settlements, Basel, Switzerland

At the present time, it is not, and will continue downward. At the end of June 2022, four fifths of outstanding amounts matured in less than one year. In addition, the BIS $97 trillion estimate represents only what is known, what *has been recorded on balance sheets.*

The BIS review further cautions an overly conservative estimate of $65 trillion of foreign currency exchange (FX) dollar debt is held by non-US institutions in currency derivatives. This is coupled with an additional $25 trillion held by non-banking institutions. The BIS Quarterly Review highlights FX debt *as going unrecorded on balance sheets* due to an *inability to track* derivative positions.

In my view, 'expensive' can be viewed as all the profits that can be realized from a debt-based system. A new system of profiteering must, by design, take its place. This new system is not actually new at all. It has been done before under the guise of monarchies and dictatorships. A feudal system, built upon the backs of the serf class. In the contemporary, a system referred to as "The Great Reset."

This inability to extract further profits from the existing global economies is driven by purposeful central bank interest rate increases and inflationary pressures initiated with the so-called "Covid Crash" in May 2020. In one aspect, inflation is a direct result of supply chain disruption. In another, the ever-increasing sovereign-nation deficit spending, especially by the U.S. government, has impacted the value of the US dollar.

Attempts by the US government at mitigating the Great Financial Crisis (GFC) of 2007-8 (historically referred to as the subprime mortgage crisis) came in the form of so-called taxpayer bailouts of institutions (banks, non-banks, hedge funds, insurance companies) deemed "too big to fail".

Federal Reserve Chairman, Ben Bernanke, also defined the term in 2010: ***"A too-big-to-fail firm is one whose size, complexity, inter-connectedness, and critical functions are such that, should the firm go unexpectedly into liquidation, the rest of the financial system and the economy would face severe adverse consequences."*** **He continued,** ***"Governments provide support to too-big-to-fail firms in a crisis not out of favoritism or particular concern for the management, owners, or creditors of the firm, but because they recognize that the consequences for the broader economy of allowing a disorderly failure greatly outweigh the costs of avoiding the failure in some way. Common means of avoiding failure include facilitating a merger, providing credit, or injecting government capital, all of which protect at least some creditors who otherwise would have suffered losses. ... If the subprime mortgage crisis has a single lesson, it is that the too-big-to-fail problem must be solved."***

https://en.wikipedia.org/wiki/Too_big_to_fail

Treasury Secretary Henry Paulson and President Bush, 2008

Imagine for a moment, you failed to pay your debts on time, even to the extent you are more than a year in arrears, and to compound the problem, you've lost track of the accounts to which payments are overdue. Additionally, the majority of your own debt payments are derived from payments *owed to you*, yet remain unpaid, and as well, you've lost track of these accounts. Thus, you have no idea what is due to you, nor what you owe to others.

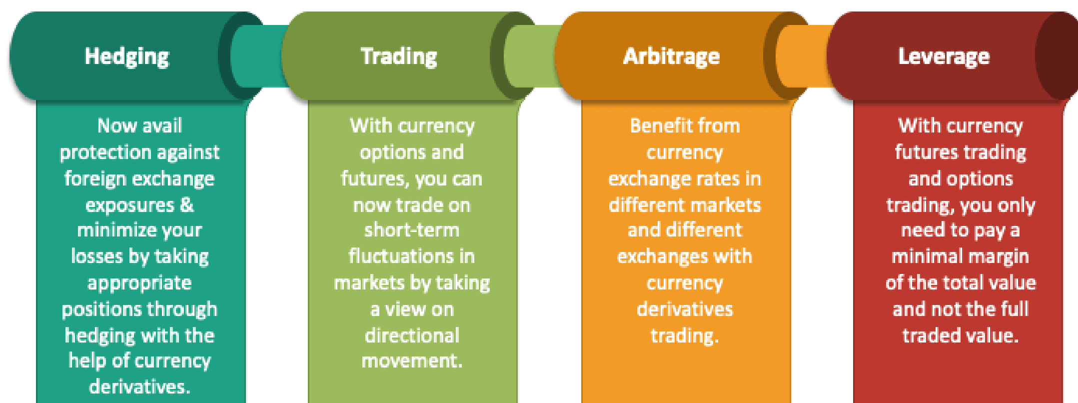
This is the present state of not only a handful of sovereign national debts, or groups of financial institutions, but rather, the entire debt-based global economy. A system of derivatives comprised mainly of the foreign currency exchange market and its attendant settlement banking system. This will be defined and detailed following an examination of the current risk profile of the global markets.

As the basis for its operation, risk has always been a part of the global financial system. Leveraged collateralized risk versus reward is built upon the back of debt servicing through payments on both principal and interest. An assessment of multi-sector risks is outlined in the December 2022 Bank For International Settlements (BIS) Quarterly Review of International banking and financial market developments.

The BIS review stipulates a *hidden* risk, including language such as "huge, missing and growing", all based upon a significant *lack of available information* emanating from the derivatives and foreign currency exchange (FOREX, FX) market.

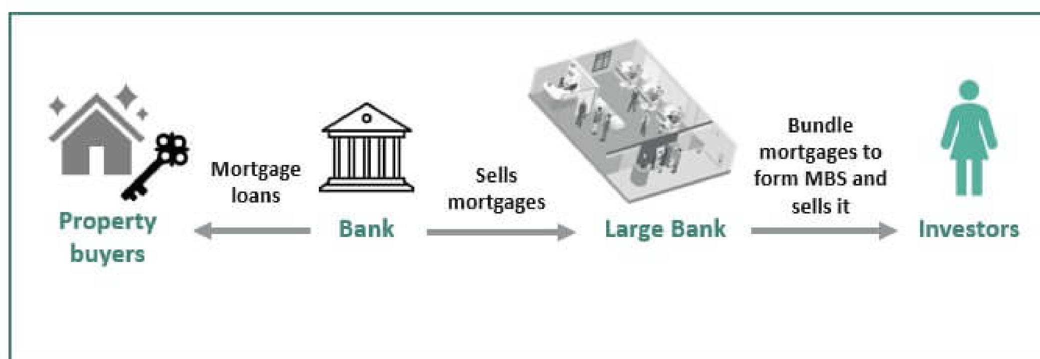
Specific foreign exchange derivatives include foreign currency forward contracts, foreign currency futures, foreign currency swaps, currency options, and foreign exchange binary options. These instruments are called derivatives because their value is derived from an underlying asset. In the case of the FX, the asset is a foreign currency.

It bears repeating, the BIS review provides an overly conservative estimate of $65 trillion of dollar debt held by non-US institutions in currency derivatives, coupled with an additional $25 trillion held by non-banking institutions. The BIS review includes the fact that the debt is going *unrecorded on balance sheets* due to an *inability to track derivative positions.*



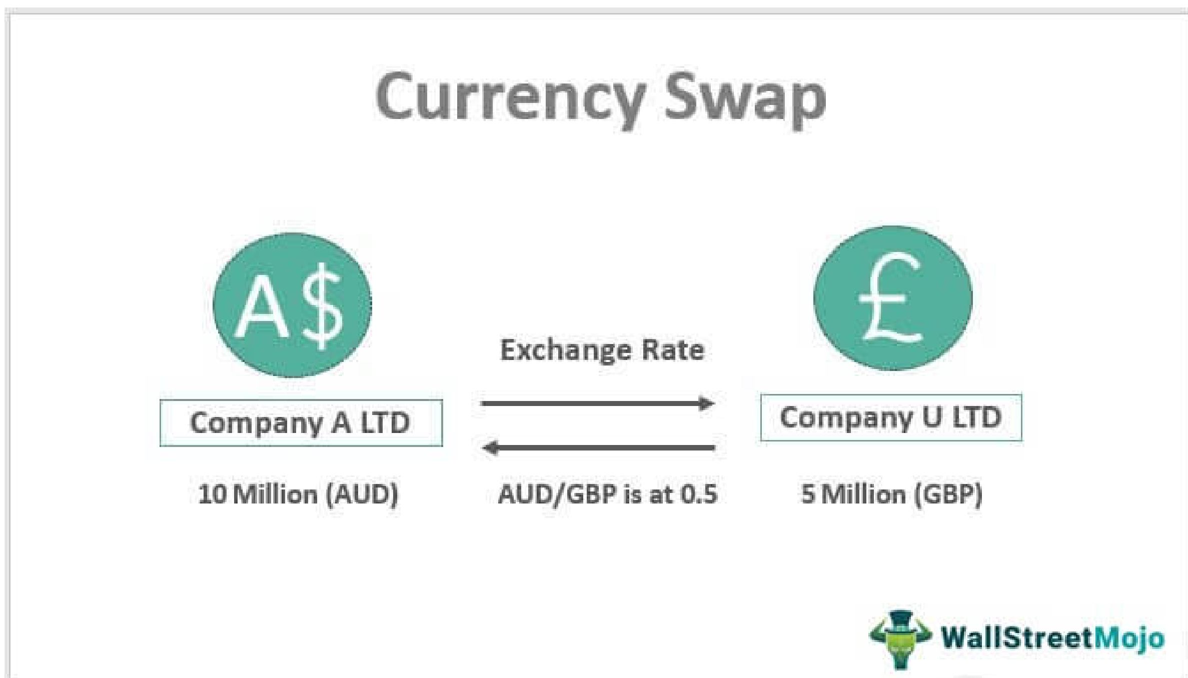
These derivatives are based upon leverage, *hidden* leverage, the borrowing of currencies (the FX) based upon reserves of collateral. A significant question that is left unanswered is the identification of the leveraged collateral used in the borrowing of exchanged currencies. Unanswered, due to the acknowledged lack of available information coming from these markets.

Mortgage-Backed Securities (MBS)



Historically, for example, similar collateral based on grossly overrated mortgage backed securities (MBS) with banks collating all of the subprime mortgages into AAA-rated portfolios, occurred during the Great Financial Crisis (GFC) of 2007-8. These exchanges of currencies are referred to as 'swaps', and contributed heavily to the advent of the GFC, leading to central banks bailing out institutions deemed 'too-big-to-fail' by the Federal Reserve and their foreign counterparts.

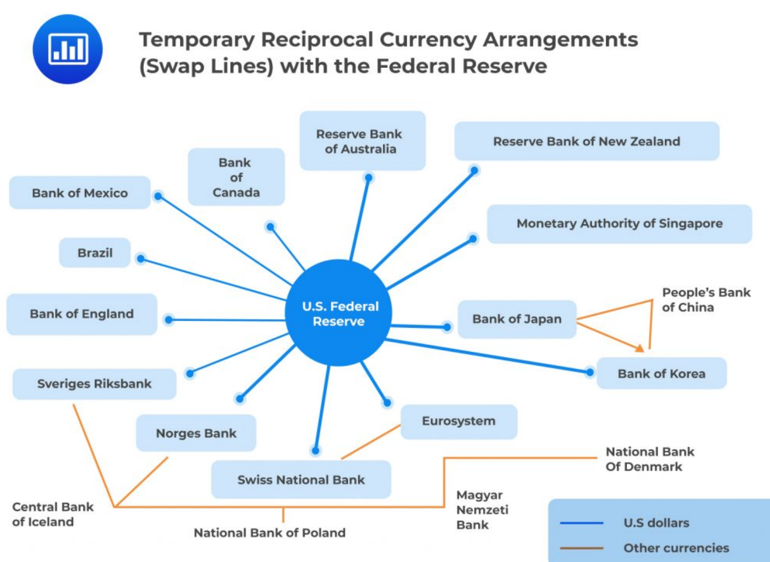
How these derivative currency 'swaps' operate can be summarized by this example: A EU-based company is purchasing products from a U.S. manufacturer. The EU company utilizes a foreign-currency swap to exchange euros for dollars. Initially, this EU company borrows the euros from a bank, then swaps them for dollars. The purchase is made from the U.S. manufacturer in dollars, however, during the time frame required to complete this purchase, the payment obligation (in U.S. dollars) is recorded *'off-balance sheet'*. This is what the BIS refers to in its review as a*"blind spot"* in the global financial system.



Researchers at the BIS, Claudio Borio, Robert McCauley, and Patrick McGuire wrote: *"It is not even clear how many analysts are aware of the existence of the large off-balance sheet obligations. In times of crises, policies to restore the smooth flow of short-term dollars in the financial system — for instance, central bank swap lines — are set in a fog."* In this case, 'fog' refers to a lack of off-balance sheet information for guidance in determining monetary policies regulating central bank swap lines.

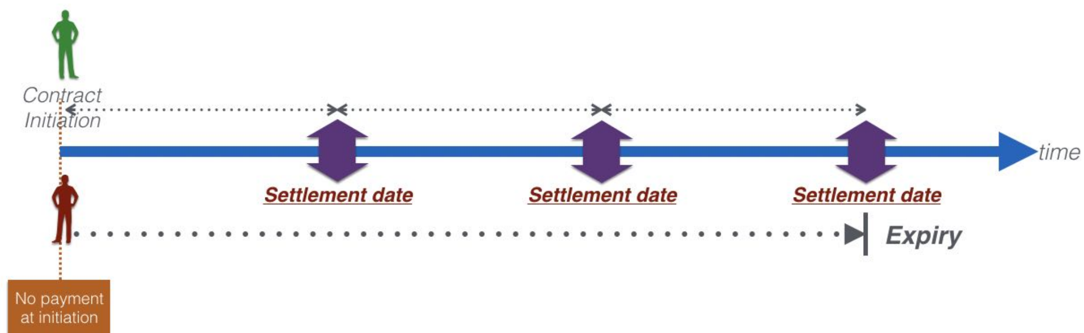
These swap lines are lines of credit established by the Federal Reserve and offered to the central banks of U.S. ally nations. Typically, the length of these loans are either seven-day or ninety-day with terms at predetermined interest rates set by the Federal Reserve. Any remaining unused principle can be refinanced for use at a later date, so long as the total debt (loan/swap) continues being serviced (payments on principal and interest).

The BIS estimates non-US banks are servicing over $39 trillion of these swaps (loans), over *twice* the amount recorded as on-balance sheet debts and *ten times* their required capital reserves. Adding to this 'fog', the amount of U.S. dollars denominating these swaps *is not reflected on any balance sheet* ('off-balance sheet'), referred to by the BIS as a "blind spot" in the global financial system. Adding to this dilemma is the poorly defined or even *missing collateral* needed to secure these loans, also referred to as 'derivative currency swaps', creating a situation known as 'settlement risk'.



This is an estimate of the relative risk of one party's failure to meet their obligations. In their review, the BIS cited *settlement risk* as the primary source of instability in the foreign exchange market, commonly referred to as the Forex or FX. It is the global marketplace for the trading of one nation's currency for another. The BIS estimates the daily turnover of U.S. dollars at $2.2 trillion as subject to *settlement risk.*

The U.S. Federal Reserve (U.S. Central Bank) initiated swap lines during the early 1990s, and expanded the program during the Great Financial Crisis (GFC) of 2007-8, reaching a maximum of over $580 billion. This figure again grew to nearly $450 billion during the so-called "Covid crash" in May 2020. The numbers dropped to somewhere between $17 billion and $800 million until April 2021.

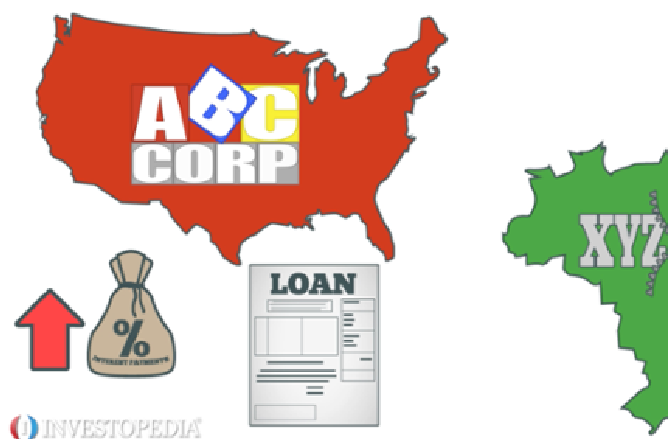


Swap Contract: An agreement between two parties to exchange a series of future cash flows, on periodic **settlement dates**, over a certain period.

A **swap contract** can be decomposed into a series of off-market forward contracts.

In 2022, over 90% of all Forex (FX) transactions were denominated in U.S. dollars. The result is a *continual demand* due to a Fed-imposed worldwide shortage of U.S. dollars, a demand that is being serviced through the Federal Reserve's swap line program. A program inherently subject to settlement risk.

The BIS review indicates it is *not clear* how many financial analysts are *even aware* of the existence of these large off-balance sheet obligations, thus, impacting their ability to accurately determine swap line settlement risk. As stated, these swap lines were a response by the Federal Reserve to disruptions in dollar funding markets during the GFC of 2007-8 and the "Covid Crash" in May 2020. This *lack of awareness* demonstrates the need for statistics tracking the geography of outstanding short-term dollar payment obligations.



Historically, analysts have relied upon benchmark international statistical collections covering only on-balance sheet positions. The BIS "blind spot" is due to a *lack of statistical reporting of off-balance sheet positions.* This results in an inability by analysts to forecast the scale and geography of dollar *rollover* requirements needed to meet a Fed-imposed ever-decreasing availability of dollar funding liquidity.

According to the BIS review, the Forex (FX) *swap markets are vulnerable to funding squeezes*, the availability or liquidity of U.S. dollars for use in the financial markets. This results in vast, *unseen dollar borrowing* within the FX market, and only recorded off-balance sheet in a "blind spot".

Currently, there remains over $80 trillion in outstanding obligations to pay U.S. dollars in FX swaps, predominantly in *very short-term agreements exceeding the stocks of dollar Treasury bills, repo and commercial paper combined*. The BIS estimates the turnover of these agreements approached $5 trillion per day in April 2022, two thirds of the daily global FX turnover.

FX swaps, forwards, and currency swaps give rise to dollar obligations that were backstopped in 2007-8 and 2020 by central banks *acting on little information about who owed the debt.*

- **For non-banks outside the United States, dollar obligations from FX swaps, forwards, and currency swaps have grown fast, reaching $26 trillion or *double their on-balance sheet dollar debt.***
- **In mid-2022, non-US banks with direct access to Federal Reserve credit only in their US operations owed an estimated $39 trillion in dollars from FX swaps, forwards, and currency swaps.**

Excerpts From The BIS Review:

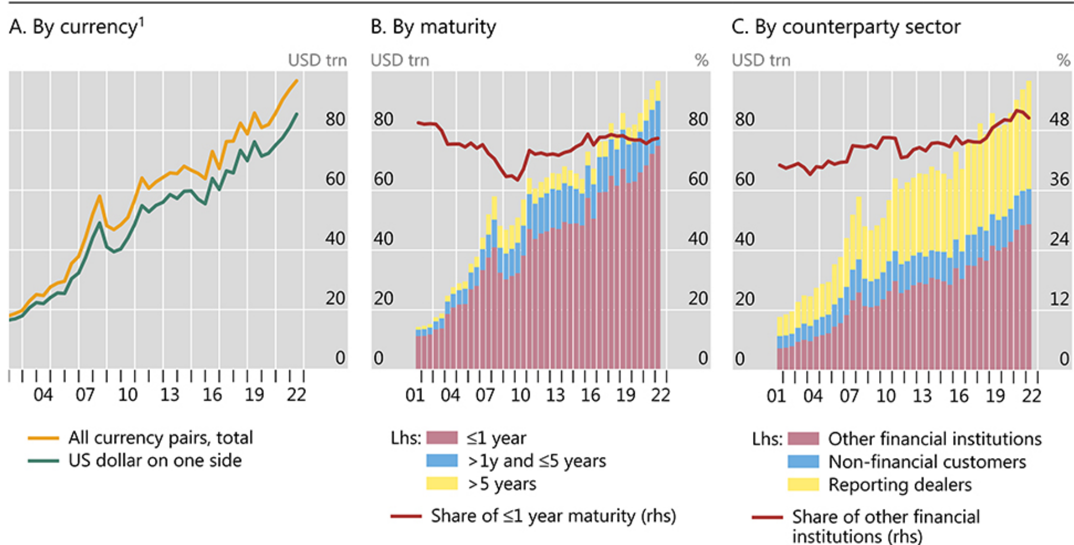
For all the differences between 2008 and 2020, swaps emerged in both episodes as flash points, with dollar borrowers forced to pay high rates if they could borrow at all. To restore market functioning, central bank swap lines funneled dollars to non-US banks offshore, which on-lent to those scrambling for dollars.

This off-balance sheet dollar debt poses particular policy challenges because standard debt statistics miss it. The lack of direct information makes it harder for policymakers to anticipate the scale and geography of dollar rollover needs. Thus, in times of crisis, policies to restore the smooth flow of short-term dollars in the financial system (eg central bank swap lines) are set in a fog.

The missing dollar debt from FX swaps/forwards and currency swaps is huge, adding to the vulnerabilities created by on-balance sheet dollar debts of non-US borrowers

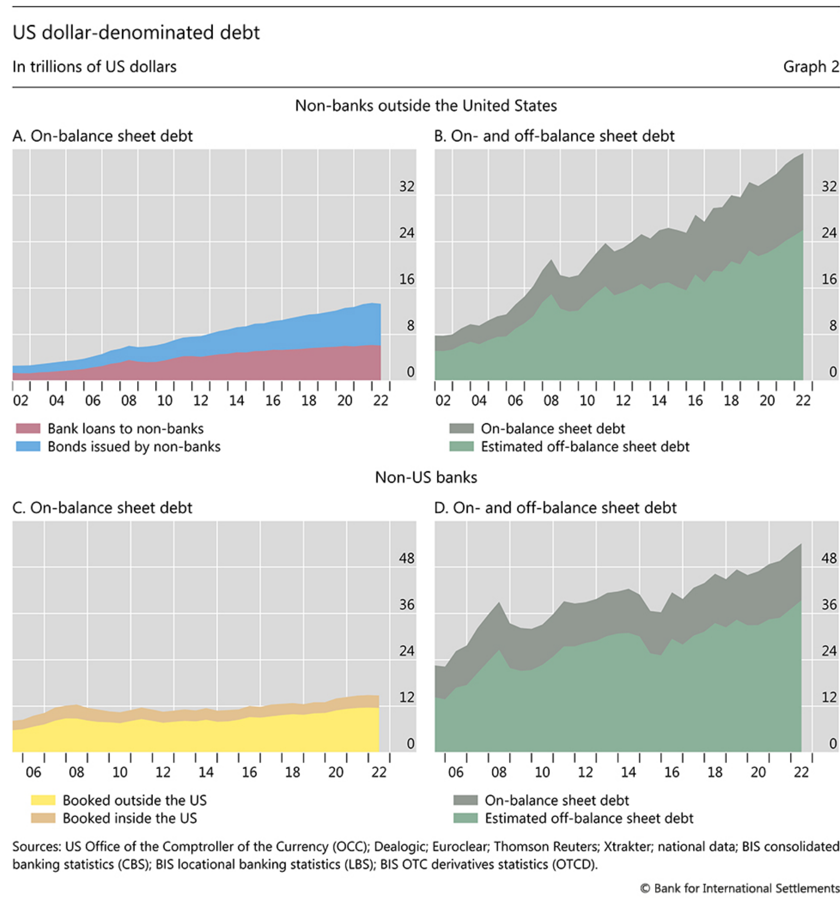
Payment obligations arising from FX swaps/forwards and currency swaps are staggering. Considering all currencies, outstanding amounts at end-June 2022 reached $97 trillion, up from $67 trillion in 2016 (Graph 1.A). This matched global GDP in 2021 ($96 trillion) and was three times global trade ($29 trillion). And it exceeded both global external portfolio investment ($81 trillion) and international bank claims ($40 trillion) at end-2021.

Dollar dominance is striking in this FX market segment, greater than in any other aspect of dollar use. As a vehicle currency, the US dollar is on one side of 88% of outstanding positions – or $85 trillion (Graph 1.A



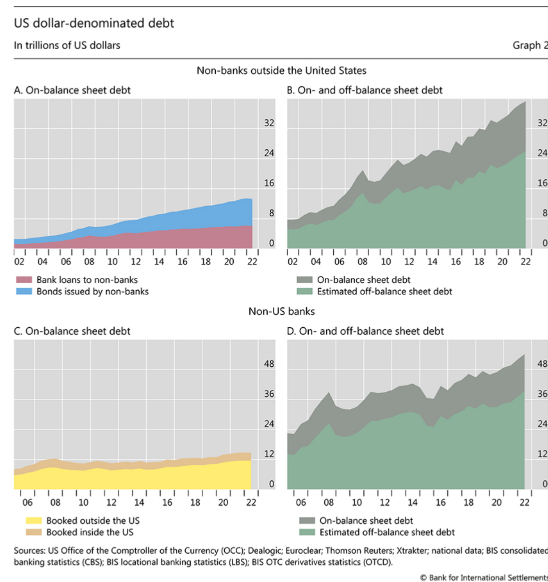
The very short maturity of the typical FX swap/forward creates potential for liquidity squeezes. Almost four fifths of outstanding amounts at end-June 2022 in Graph 1.B matured in less than one year. Data from the April 2022 Triennial Survey show not only that instruments maturing within a week accounted for some 70% of FX swaps turnover, but also that those maturing overnight accounted for more than 30%. When dollar lenders step back from the FX swap market, the squeeze follows immediately.

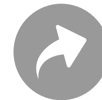
Just how large is the missing dollar debt from FX swaps/forwards and currency swaps? At end-June 2022, dealer banks had $52 trillion in outstanding dollar positions with customers. Non-banks had dollar obligations of half of this amount, $26 trillion. This sum has been growing strongly, from $17 trillion in 2016 (Graph 2.B).



This $26 trillion dollar debt is likely owed by entities outside the United States, for which the dollar is a foreign currency. They borrow dollars largely to hedge their dollar receivables and investments in a world in which the dollar is the dominant international currency.

The off-balance sheet US dollar debt of non-banks outside the United States substantially exceeds their on-balance sheet debt and has been growing faster. At end-June 2022, the missing debt amounted to as much as double the on-balance sheet component (Graph 2.B), which was estimated at "only" $13 trillion (Graph 2.A). Moreover, the missing debt was "only" 1.6 times larger in 2016.





For their part, banks headquartered outside the United States, including some dealers in FX swaps, have even larger missing dollar obligations. These banks deserve focus because of their limited access to the Federal Reserve's discount window for dollars. Their estimated off-balance sheet dollar obligations of $39 trillion at end-June 2022 were much higher than the $15 trillion in on-balance sheet dollar debt (Graph 2.C) and almost half as big as their combined total liabilities, adding to the problem of settlement risk.

• In April 2022, $2.2 trillion of daily FX turnover was subject to settlement risk, up from an estimated $1.9 trillion in April 2019.

• FX settlement risk, the risk that one party in a currency trade fails to deliver the currency owed, remains because existing settlement arrangements to mitigate risk are unavailable, or unsuitable for settling certain trades, or market participants find them too expensive.

Tipping Point

The tipping point for the global economy will be a liquidity squeeze due to a lack of lenders, such as the Swiss National Bank, in a planned shortfall of reserve dollars issued by the US Federal Reserve for currency auctions. Presently, over 20 major banks are participating in currency auctions through the Swiss National Bank. As recently as August 2022, there were *zero* banks involved in such auctions.

With 70% of FX swaps typically maturing within a week and 30% overnight, there is a *continuing exponential demand* for reserve dollars, something that has a deliberate, *planned-for limit*. It is this limit that will trigger the cascading of the world into a turbulent storm called the “Great Reset.”

The blame for this reset will be placed squarely upon the inability of the present system to continue in its decades-long rolling over of the derivatives debt market. **A market consisting of all known debt instruments rolled into one. The global economic system has always been based upon debt. It is only in the more contemporary of times debt has been relabeled as "derivatives". Therefore, man's economics have always been about derivatives and as such, its Achilles heel.**

> [19] **They will throw their silver into the streets, and their gold will seem unclean.**
> **Their silver and gold cannot save them**
> **in the day of the wrath of the LORD.**
> **They cannot satisfy their appetites**
> **or fill their stomachs with wealth,**
> **for it became the stumbling block**
> **that brought their iniquity.** Ezekiel 7:19 BSB

16 **But blessed are your eyes because they see, and your ears because they hear.** 17 **For truly I tell you, many prophets and righteous men longed to see what you see but did not see it, and to hear what you hear but did not hear it.** Matthew 13:16-17 BSB

21 **For at that time there will be great tribulation, unmatched from the beginning of the world until now, and never to be seen again.** 22 **If those days had not been cut short, nobody would be saved. But for the sake of the elect, those days will be cut short.** Matthew 13:16-17 BSB

11 **Let the unrighteous continue to be unrighteous, and the vile continue to be vile; let the righteous continue to practice righteousness, and the holy continue to be holy."**

12 **"Behold, I am coming soon, and My reward is with Me, to give to each one according to what he has done.** 13 **I am the Alpha and the Omega, the First and the Last, the Beginning and the End."**

Revelation 22:11-13 BSB

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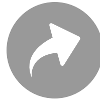

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