

ANTI-FLARING: HOW TO PREVENT THE MARKET FROM OVERHEATING

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A new damping method for the rational exploitation of flaring-type economic phenomena is proposed. The steering parameter for Anti-Flaring is called the Livermore Indicator. The approach in general is described as endonomics.

1. Introduction

Considering the power of systems theory, there exists an opportunity for the central banks to avoid so-called bubbles or superflares in the economy. Economics shows a special type of instability which was called “flaring” by Georg Hartmann.¹ (For the mathematical gourmet: Flare Theory is a simplified version of Milnor Attractor Theory).

The best example of a flare attractor is to be found in a book by the Wienerwald founder Friedrich Jahn: “A life for the Wienerwald - From Waiter to Millionaire and Back.”² He followed the strategy of using a fixed percentage of his earnings for expanding his business by spawning new Wienerwalds all over the world. Any similarities with McDonalds are purely coincidental.

2. Timing

Anti-Flaring is a new phrase and a new strategy. If the desirable flaring process has got out of hand – due to overheating beyond the point

where the debt spiral that is part of it has reached a level that can't be healed anymore – then the idea of anti-flaring can be the method of last resort.³ Ideally, the Federal Reserve would adjust the interest rate and/or the money supply just in time, much as China is having to do at the time of writing. However, there is a special risk involved here. If the right moment has been allowed to pass inadvertently, the effect can be counterproductive and even disastrous (famous examples being the Great Crash of 1929, the Nikkei Crash in 1990 and the Nasdaq Bubble a decade later). But would not choosing the right moment amount to a miracle of clairvoyance?

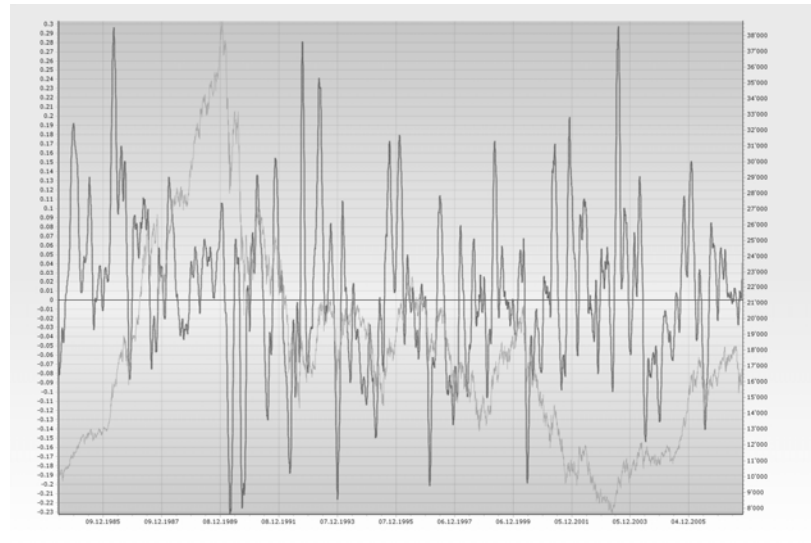


Fig. 1: Nikkei Livermore Indicator Flares 1984 - 2007; The dark line represents the Livermore Indicator, the grey line is the Nikkei Index.

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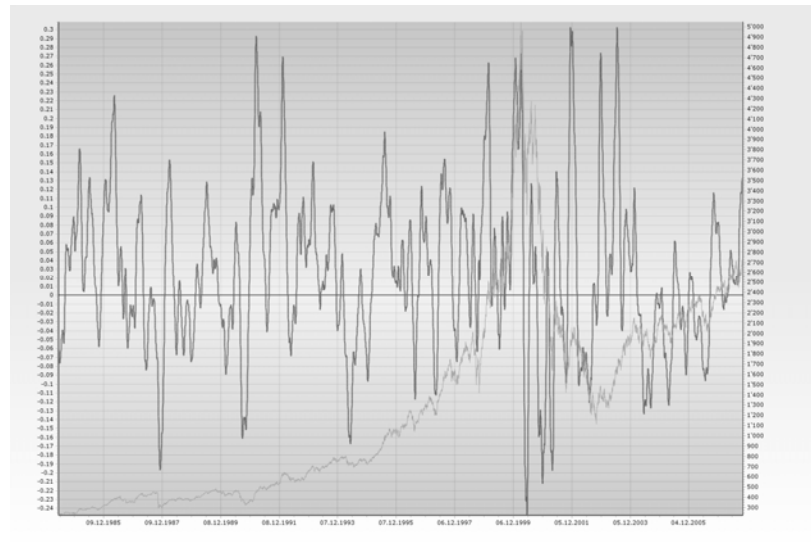


Fig. 2: Nasdaq Livermore Indicator Flares 1995 - 2007; The dark line represents the Livermore Indicator, the grey line is the Nasdaq Index.

Source: www.unternehmercockpit.com

3. Matrix Analysis

This miracle is to be described in the following - but please, do not tell anybody.

There exists a mathematical algorithm whose matrix-theoretical fundamentals are very simple but easy to be questioned by a specialist. The inventor discovered it on the basis of long empirical and theoretical practice, but non-cyberneticians cannot yet quite understand how it works.⁴ Nevertheless, the principle and the steering by the so-called Livermore Indicator is very simple.

It is based on the principle of autocatalysis in dynamical systems.⁵ The best introductory book is still Robert Rosen's 1971 international bestseller (especially in Japan) "Dynamical System Theory in Biology". The principle is based on Oscar Lange's 1969 book of Recursive Matrix Dynamics⁶, which was first implemented in an economic context by Michel Godet in the eighties.⁷ Autocatalysis is the one leg of the new

principle. The other is a superposition of differing time curves obtained in this fashion on different flaring-type time curves of the same variable of different length. This makes use of the self-similarity of flare theory.

This insight can be used to obtain a more reliable detection of and projection into the future of ongoing flares. Therefore, a big bubble can be recognized in time with an unprecedented early-detection margin.⁸ Remarkably, following-up a quite small number of variables suffices to diagnose a developing pathology in the market.

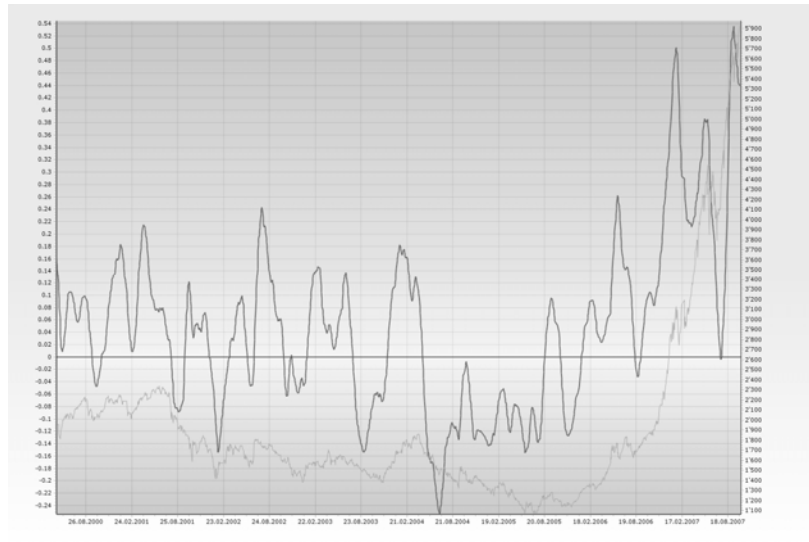


Figure 3: Chinese A-Share Livermore Indicator Flares 2005 – 2007⁹; The dark line represents the Livermore-Indicator, the grey line is the Chinese A-Share Index.

Source: www.unternehmercockpit.com

Why should you believe this claim of ours? An empirical proof could be seen to lie in the performance of the *Unternehmercockpit* (www.unternehmercockpit.com), which was founded by the first author. But of course, empirical success, with its necessarily finite time-base is no theoretical proof.

Without the new flare theory with its self-similar height-structure on all magnitudes, as described in Hartmann's thesis, a similar confidence

that this is really the structure of an economic system would not be possible to the same extent.

Flares also have a surprising implication: they are scale-free. Therefore, quite innocent short specimens can reveal an ongoing bigger process, formed by many little elements via summation. This confirms and supports the fractal economic theory of Benoit Mandelbrot, admittedly in an idiosyncratic manner.¹⁰

Another short observation. Adjusting the zero-level, through a kind of low-pass filter, allows us to eliminate the influence of negative/positive fluctuations – in the near-zero area.

4. Anti-Flaring

When these indicators are used, an overflow is successfully avoided and the corresponding sector of the partial or full economy in question can be steered much in accord with the early hopes of Norbert Wiener.

If this prediction were borne out, the main effect would be that speculation can effectively be taken out of the market. This is an apparently new option of Endo-Management, which, of course, comes ethymologically from end-o'-management, like in will-o'-the-wisp.¹¹

In this way, the Hedge Fund speculation can be reduced to absurdity, so that such funds cannot perturb the very system they prey on any longer. Helmut Schmidt's concern about the danger of uncontrolled hedging could thereby be mitigated. The new indicator, which allows a related second upturn to be distinguished from a transient last positive wave during a downturn, exposes the hidden structure of the market. Even before professionals in the market have any clue what's going on, the newly invented Livermore Indicator (www.unternehmercockpit.com) will show the new direction of a cybernetic trend.¹²

If everybody were in possession of this new diagnostic instrument - for example, if Google were to make it available - this would amount to a very effective artificial damping of non-productive fluctuations in the financial markets. If every movement of the market is based not on speculation but on effectiveness, the new indicator will push the whole economy towards entrepreneurship and knowledge orientation, as

anticipated in the book “Medium of Knowledge” by the present authors.¹³

The effect that can be achieved with this new method will be reminiscent of that which banker Alfred Herrhausen anticipated in 1989, along with his ‘unreasonable’ view of turning around the Third World economy by intelligent debt escape. This endo-approach also provides a philosophical background for a healthier economic future based on cybernetic risk management¹⁴ that allows an early anti-flaring course to be steered in the complex system known as the economy.¹⁵ We have named this new research field endonomics.¹⁶

5. Sum-up

Human activists in the market as described by Ludwig von Mises are pathological animals.¹⁷ They have a choice between positive and negative feedback loops, between flaring and anti-flaring. Endo-Management, the style of governance which allows complexity to be steered, shows a way toward a healthier and less erratic development of the global market. If applied correctly, the market participants, especially the Federal Reserve, have the choice of taking the red or the blue pill, as in the famous counterculture movie ‘Matrix’.

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