

# The Great Simplification - Frankly #1

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Nate Hagens (00:00):

Okay. Ukraine situation. I believe this has, even in the best of cases, shortened the runway leading to The Great Simplification. Our society, for those who have followed my work, has four pillars of subsidies that support our modern living standards and expectations that are kind of hidden, or at least not talked about. One is energy. We are subsidized by energy like a fish in water and we don't even see its ubiquitousness. We are energy blind. Number two is credit. Freely available, low cost, credit for pretty much anyone who's of credit worthiness, a nation's municipalities, et cetera. Number three is complexity. We have a six continent supply chain that has Byzantine complexity of little spark plugs and tiny components that we ship around the world that we take for granted will always continue. And then the fourth pillar is trust and peace generally. And it's my opinion that in the best outcome of what's happening in Ukraine right now, those four things will become more recognized by the general public and in the worst case, those things will shrivel and get smaller, which has large implications.

Nate Hagens (01:38):

So, what I like to do now is just give a one or two minute overview of a bunch of different topics related to the Ukraine situation. I think the best case outcome militarily and geopolitically, and I'm not an expert on either of those things, but I have a lot of close friends that are following this closely, I think the best case is Ukraine is going to be split like World War II Germany was into the East and West, there's a new stable military border between NATO and Russia and this begins Cold War 2.0. They'll probably militarize the entire country and then pull back to the Eastern oblasts and there's some sort of natural détente that happens there. But that is, on the surface, the best outcome. But there are all kinds of economic, financial and other externalities that would happen from that. It would change the world order as far as geopolitical partners, like we would probably start to use China more as a bridge to get fuel energy commodities into the world economy via China instead of directly via Russia.

Nate Hagens (03:09):

So in that sense, it might not be a terrible blow to the global economy, but I think what it's going to do is start choosing sides for the new multipolar society and it's possible Russia, China, India are all vectors versus the West on how the economic system functions. Here's why this is so important. Longtime followers of my story know that energy is fundamental to our economies. A barrel of oil does around five years labor potential of a human. We use a hundred billion barrel of coal oil and gas natural equivalent every year so we get this subsidy of 500 billion human workers that we create monetary markers for. And the US has the world's reserve currency. We benefit from the seigniorage, which is the trade and commerce benefits from other countries having to denominate their trade in our currency.

Nate Hagens (04:16):

And so there's this giant chess match and paradigm shift that's happening behind the scenes right now because Russia is a very small economy by measured by GDP, but they're energy superpower by any metric. So Russia produces around 11 million barrels of oil a day and they only use three and a half million. Russia produces 700 billion cubic meters of gas every year, but only uses about half of that. Russia mines 800 million tons of coal every year, but only uses 300. So in contrast, Europe produces

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only three and a half million barrels of oil every day, but they use almost five times that, over 15 million barrels. They produce 230 billion cubic meters of gas every year, but they use 560 billion. They use almost a billion tons of coal a year, and they produce only a half of that. But they have the Euro and they're trading partners with the United States and they have the military support of the United States. So this giant inflection where we are trying to put sanctions on a country that has some of the fundamental inputs that make the world economy go round.

Nate Hagens (05:48):

So I think we're going to find new partnerships and alliances and a possible new Bretton Woods agreement, Bretton Woods three, because how can the West still try to financially crush Russia when Russia has its own energy independence that many of these other countries don't have? I think it's a real scary issue. And here's the scariest issue of all, of course. There is a chance that this escalates. The best case is that it's split Ukraine into two pieces and NATO and Russia are kind of at some sort of détente. I think we have a month or longer before that happens and everyone in the world has an opinion about what's happening in Ukraine and Russia and I'm no different and I'm going to tell you why I've become a little humble on that in a second. But let's talk about the worst case.

Nate Hagens (07:00):

Some of my friends who are very much in the know are telling me there's a one in five to one in three chance of nuclear war right now. And the reason is is that if they engage NATO or the United States, there is no off-ramp then, because what ends up happening is this network effect of higher level escalations, where will the adult in the room or the relief valve happen if we start to engage, if we have planes going via Poland, or if some Americans get killed or something like that? Who will stop the escalation there? And you should go back and listen to the podcast I did with Chuck Watson, we talked about the concept of risk homeostasis, which is that if you perform a risk several times that has a one in 10 chance of happening, and it never happens, you behaviorally go in the opposite direction because your mind thinks you're taking less risk than you actually are. And there have been estimates that showed during the Cold War, there was a 70% chance of a nuclear war.

Nate Hagens (08:14):

Well, there was a 0% actual outcome of nuclear war, so we overestimate how... we underestimate the risk of a nuclear exchange because it's never happened before. And I think there's a complacency in our culture, maybe it's because we watch all these movies on Netflix and at the last minute crisis is averted and we just assume that nothing so horrible could happen, but where are the peace activists? Where are people in the streets saying no nuclear war? It's like people are so complacent about this because it is civilization ending. If there is... a tactical nuke is one thing where there would be damage and casualties and it would be horrific, but strategic nukes would... we might not die from radiation, but the complexity risks of the global system would unravel very quickly. This is something I have perpetually worried about and I think the phase shift away from economic growth, a big war is an eminent possibility given our species' history. And I am not an expert on this. I just think we need to be talking about this and downplaying the rhetoric on what's happening.

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Nate Hagens (09:44):

You see Sean Hannity just being all belligerent, "We should take out this, take out that." I think these people having to clue of the wider boundary risks. So I think that's a big risk. Let me talk about humility for a second. I was in California last week for some meetings and I was fortunate to sit in on some discussions with people very close to military and geopolitical intelligence on this stuff and I realized, I'm a smart guy, I have a PhD, I have a podcast talking to systems leaders around the world on all these topics. I don't know shit about nuclear situation or what's going on and I think there's so many people that have gotten into this armchair quarterback situation where they read a few expert blogs and they get some Tweets and watch CNN or Fox and now they have an opinion on Ukraine and Russia. I was humbled by how little I know on what's going on. I don't want to get into details, but, "Russia did this." "Well, no, it might have been Ukraine that did that."

Nate Hagens (11:00):

And I think we are being very quickly persuaded that Russia and Putin are the only evil in the world, and I'm sure they are evil in many ways, but they're not the reason that we consume 21 million barrels a day of oil or that Europe consumes 15 million barrels a day of oil. In any case, I know what I know and I know that I don't know what's going on on the ground in Ukraine and why should I? What I do know is the context of how finance is this giant Leviathan of claims on the physical world and we are growing our financial claims while our physical claims are declining in quality and quantity. And that Delta, the gap between the two, is widening by the year and we're papering it over with more claims and now there's geopolitics thrown into the mix.

Nate Hagens (12:11):

So what I see is the possibility of a new financial, economic, multipolar, both economic and geopolitical, regime, which changes everything. It accelerates the timeline of the risks that I'm talking about on this podcast and I think China very likely could become a bridge by which Russia's products end up on the world stage. I think we also, at some point, are at another inflection point of 2008, 2009, financial crisis, 2020 COVID financial crisis, where all of a sudden the amount of economic needs are greater than the income stream, which is GDP needed to support them, and so we have to print more money and offset what's happening with financial guarantees, artificially low interest rates, bazooka actions by the central banks.

Nate Hagens (13:22):

And at some point this decade, I fear and expect that we will go from a too big to fail situation, like AIG and some other financial firms in 2009, to a too big to save situation. That a central bank will print too much and the bond markets will call their bluff and we have currency reform or some sort of a musical chair situation, that our financial system can no longer kick the can on and that is the fundamental logic of the great simplification. We're going to have a smaller economy as the financial world and its claims recalibrate to the underlying physical world. And this is... one of the best energy sources is conservation, which is using less. But in this situation, using less, tightening our belts, would directly reduce the income stream to pay back our debts, which is GDP. So conservation is what we

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should be doing, but in doing that, we also, unless it's managed and planned, we also cascade the financial system down, which then crimps complexity and all kinds of other things.

Nate Hagens (14:51):

A word about Europe. I think this fundamentally changes Europe. The United States still produces 85% of our own energy, at least for now. Europe is far less. Germany in particular gets 50% of its coal, 55% of its gas and 35% of its oil from Russia. So no wonder Germany is not going to put direct sanctions on and stop their imports, their economy would implode. So I think this entire war has changed not only the geopolitical, the financial and the economic game board, but also the climate and the energy game boards. First of all, in energy, especially in Europe, I think the energy wind or the energy transition movement in Germany is now going to go more towards energy security. If they have a extra 10 billion dollars are they going to build more wind turbines and solar panels or are they going to be more concerned about energy security? Not only the flick of a switch that natural gas can give us to meet the daily demand fluctuations that solar and wind cannot, but also the complex supply chains needed to construct these rebuildable technologies.

Nate Hagens (16:12):

I also think credit is going to be an increasing limit and the knee jerk reaction for people that don't follow this closely is, "Oh my gosh, this country, Russia, produces all this energy. We should do our own energy like solar and wind." Well, oil can't... the properties that we use oil and gasoline for can't easily be swapped out with solar and wind. So I think this changes the renewable discussion. I also think it changes the climate situation because this war could do more for climate than any activism over the last 50 years. At least in the moderate to worst cases, this is going to be a huge carbon tax for Europe and indirectly the world and I think that's going to change our emissions. It probably additionally cemented fourth quarter 2019 as global peak oil.

Nate Hagens (17:15):

So, there's a lot going on here. That's it for a short off the cuff update. Let's all root for the best case outcome, but even that is going to have repercussions for our lives. If there's a one in five chance of nuclear war in the coming six months, I'm going to now go do what every normal human would do in that situation, I'm going to go watch college basketball and try to get some relaxation, meditation, play with my dogs, be out in nature this weekend and I hope you're all doing well in your corner of the world and to be continued on this channel. Thank you.