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How the Depression Settling Amongst Us is Reshaping Our Living Styles — As Did Its Predecessor of the 1930s

To deal with our problem it would be logical to start with babies, but the statistics of childbirths in years good and bad contradict one another. Demographers, however, have not developed the knack of flipping social data as have official economists. They grasp the fact that there are fistfuls of different causal factors that can appear when you turn a proposition around. Accordingly, babies are born in greater or lesser numbers for many very different reasons, some of which are not reversible.

Our source for the bare bones of our reflections is *The Wall Street Journal* (30/9).

Iceland is in a class by itself. The depth of its economic crisis outpaced that of any other land. It could well have been that with the price of oil to feed the furnaces soaring, couples, married or not, spent more time in bed together to keep warm. But there were other things more likely to happen, especially when the price of contraceptives had risen beyond the reach of many Icelanders.

"Iceland is an island of rotten figures. The stock market is off 87% in the past year. Real wages are down 8%. The poor krona has slumped by half since the beginning of last year.

"But births through mid-August at Reykjavik's biggest hospital, which delivers 70% of Iceland's babies, rose 3.5% over the same period last year. By the hospital's projections, 2009 is shaping up to be the best years for little Sigurdurs and Gudruns in decades. Hospital staff are looking forward to more 'crisis babies' this year and next…. Wrote Alda Sigmundsdottir: 'I think many of us must have sought solace in love and sex and all that good stuff.'

"That got attention, and soon stories about an Iceland crisis-baby boom started bubbling overseas. Hospital birth numbers have risen in some parts of Italy this year, too, prompting speculation that Italians were rediscovering the simple joys of family in unsettled years. In the dark days of the winter recession, US papers pointed out that condom sales were brisk.

"So, is economic chaos really the ultimate aphrodisiac?

"Probably not.

"In fact, it is more likely that prosperity, not poverty, is good for baby-making.

"Geroge Udny Yule, an early British statistician, noticed the pattern a century ago. In 1941, two economists reported an 80% correlation between employment and next year's births during the inter-war period in the US.

"The historical reason was age of marriage, says Brian J.L. Berry of the University of Texas at Dallas, who has looked all the way back to 17th-century New England. When times were good, a young man could get a job to support a family and marry earlier.

"Of course, notes Mr. Berry, times have changed. Lower infant mortality, changing social mores and – above all – contraception have pushed the fertility rate down for decades in industrialized countries.

"But Carl Haub, a demographer at the Population Reference Bureau, a Washington think tank, points to modern examples of the economy's impact on the stork's deliv-

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Depression *from page 1*

eries, many fewer births in former Eastern bloc countries, which suffered economic doldrums after the fall of the Soviet Union.

"'Those were countries with modestly high birth rates,' Mr. Haub said. 'They just collapsed.'

"So, too, did birth rates in the US during the Great Depression. 'Total fertility – roughly, the average number of children per woman during her childbearing years – was 2.53 in 1929 and had slid to 2.15 by 1936. Then came the baby boom of postwar prosperity. The birth rate crossed 3 in 1947 and remained above that threshold until the mid-1960s. The next trough, 1.74, came in 1976 – a year earlier, unemployment had hit a postwar peak of 8.5%.

"Some research suggests wealth, not poverty, may improve one's sex life. Two British researchers at Newcastle University found Chinese women reported more pleasurable sex when their partners were richer.

"To be sure, fertility is a many-splendored thing, and attempts for economic explanations are bound to come up short. During the Roaring Twenties, for example, the birth rate in the US actually declined, an effect attributed to wider use of contraception. Mr. Berry says the downward push of contraception on fertility over the ensuing decades 'masks everything' else that might play a role.

"Some economists have suggested that birth rates sometimes move in opposite direction to that of the economy, on the theory that when times are bad a woman leaves less on the table by quitting the work force to have a child.

"Many things besides money go into decisions to have a child, and, of course, sometimes there isn't much of a decision at all. Changes in government policies – parental leave, child benefits – tug on fertility, too. All these things can play a greater role the tos-and-fros of the economy."

An Unresolved Depression Can Cause the Drooping of Martial Moustaches, and Push the World Into Its Terminal War When Other Alternatives are Ignored

"Odierno Says Troop Pullout from Iraq Is on Track" by Yochi J. Dreazen: "Washington – The top US commander in Iraq says the US is on pace to withdraw tens of thousands of troops in Iraq in coming months despite a spate of recent attacks there.

"In an interview, Gen. Raymond Odierno, who is due to testify on Capitol Hill about the war Wednesday, said American troop levels in Iraq will fall to roughly 50,000 by mid-2010. A bilateral security accord between Washington and Baghdad calls for the remaining troops to leave Iraq by the end of 2011.

"The comments from Gen. Odierno offer the clearest indication to date of how senior commanders in Baghdad envision winding down the long US-led war in Iraq, which the Obama administration sees as a lower national-security priority than the war in Afghanistan.

"They come as the Pentagon holds on to a request from the top American commander in Afghanistan, Gen. Stanley McChrystal, for up to 40,000 reinforcements. The Obama administration is revaluating its entire Afghan strategy in the wake of flawed presidential elections there and a wave of Taliban violence.

"Gen. Odierno warned that the war in Iraq is far from over, with political challenges – such as unresolved Kurdish-Arab tensions over oil and control of northern Iraq – posing serious challenges to the country's future stability. 'It's not so much about an insurgency anymore,' said he in the interview at the Pentagon. 'The disputes are about the very nature of the Iraqi state.'"

With a deepening economic crisis at home, flashes of realization that Washington needs those home-coming body bags like a hole in the head. That, however, in no way removes the fact that the deepening economic world crisis is pushing the powers in the general direction of a world war, as a final gamble when all the others have been played and lost. Anything, but the most obvious of the clearest way out of the world crisis, that our entire suppressed history dangles before our governments' nose without causing them to respond with anything more drastic than to sneeze.

"Gen. Odierno arrived in Iraq in April 2003 with the Fourth Infantry Division, and has spent a total of nearly four years in the country. Gen. Odierno said remnants of al Quaeda in Iraq and other militant groups were carrying out some operations in Baghdad, but had been unable to re-create the sophisticated bomb-making networks they used to destabilize the Iraqi capital during the bloodiest days of Iraqi's civil war.

"The militants are instead working to expand their foothold in the volatile city of Mosul and carry out new bombings in northern Iraq to acerbate Kurdish-Arab tensions there, the commander said.

"'That's the No. 1 potential driver of instability,' he said. 'I worry that the political rhetoric can lead to violence and real problems in northern Iraq.'

"Gen. Odierno said the country was facing political uncertainty in advance of the parliamentary elections scheduled for January. The most intensive jockeying is taking place within the country's Shiite Arab majority, whose two parties are likely to abandon a longstanding alliance to run against each other.

"Gen. Odierno said Iran was working to influence the election by funneling financial aid to some of the Shiite groups, but said the overall aid of Iranian military involvement inside Iraq had fallen in recent months. 'They're focused more on the politics,' he said. They want to influence the potential outcome of the elections.

"At the American high command in Baghdad, senior officials are continuing to hone their withdrawal plans. The US has closed or relinquished more than 100 small bases, and plans to leave dozens of other small outposts in coming months.

"Gen. Odierno said the US planned to keep control of large US bases such as Contingency Operating Base Speicher near Tikrit. Other senior US commanders said in recent days that the US also planned to retain the Victory Base Complex in Baghdad and the sprawling air base at Balad.

"Odierno said more than 20,000 US forces have left the country in recent months without incident, leaving him confident that the US could safely withdraw the 65,000 troops slated to leave Iraq by the second half of 2010.

"Still, he acknowledged that some insurgents might try to disrupt the withdrawal or inflict casualties on the departing American forces.

"'Ask me again in six months,' he said. 'I may have a different viewpoint.'"

White House Leaps Into Afghan Review

By Peter Spiegel and Jonathan Weisman

"Washington – The White House began its review of Afghan war strategy in earnest Tuesday, with senior administration officials meetings via video conference with the top commander in Kabul, Gen. Stanley McChrystal, at the start of what could be weeks of debate over whether to send thousands of reinforcements.

"White House officials said President Barack Obama will join in the discussions Wednesday, when he is expected to meet with Vice President Joe Biden and Secretary of Defense Robert Gates, among other top officials.

"The White House unexpectedly decided to review its strategy in Afghanistan after a series of recent setbacks in the war, including allegations of fraud following last month's presidential elections and surging violence throughout the country. It begins just days after Gen. McChrystal submitted his request for as many as 400,000 additional troops to the Pentagon.

"Some in the administration, notably Mr. Biden, have argued for a smaller military footprint and a tighter focus on counter-terrorism as the best way forward.

"Advocates of such a shift point to the effective use of Predator drone strikes to kill Taliban leaders in Pakistan. Two additional Predators are expected to patrol the Afghanistan-Pakistan border, according to people familiar with the decision, a move that would bring the total drones in the theater to a number the military wanted for years.

"Mr. Obama gave voice to a possible shift in emphasis on Tuesday when he spoke of 'dismantling, disrupting, destroying the al Quaeda network' as the mission, without mentioning the Taliban. He also said the US is working with the Afghans to bring security to the country.

"Senate Foreign Relations Committee Chairman John Kerry (D., Mass), who is emerging as an influential choice in debate, was at the White House on Thursday to meet with the vice president. He, too, said he is leaning toward a smaller counter-terrorism strategy to supplant a larger military counterinsurgency effort.

"After an Oval Office meeting Tuesday with the new secretary general of the North Atlantic Treaty Organization, Mr. Obama said the review will also include regular consultations with the US's NATO allies.

"'This is not an American battle; this is a NATO mission as well,' Mr. Obama said following his meeting with Anders Fogh Rasmussen, the former Danish prime minister, who assumed the helm of NATO last month.

"Robert Gibbs, the White House spokesman, said the early meetings are unlikely to include specific options for Mr. Obama to consider. Instead, he said, they will likely start with a discussion of Gen. McChrystal's dire assessment of the current war effort, compiled last month separately from his troop request.

"This will take place over the course of several meetings and a number of weeks as we look at where we are, what's happened in the intervening months since the president made a decision in March, the president said.

"After years of pressing European allies for additional forces in Afghanistan, Mr. Obama made no mention of having discussed NATO contributions to the war effort after his meeting with Mr. Rasmussen.

"But in an address Monday night to the Atlantic Council in Washington, the NATO secretary general said he believed the alliance must send more trainers to Afghanistan quickly or it will be impossible to draw down foreign troops in the future."

That Brings Us to the Final Inconclusive Answer — Is the World Economy Getting Out of the Depression? — May Be

The Globe and Mail (10/1, "After The Fall, The slow Climb to Recovery, but IMF Predicts Rebound Will Outpace Rest of G7" by Kevin Carmichael): "Istanbul – Canada is on track to lead the world's wealthiest countries out of recession next year, a testament to sound economic policy and weak competition, according to the International Monetary Fund's latest outlook.

"The world's gross domestic product will expand 3.1 in 2010, compared with a July estimate for growth of 2.5%, the IMF says in its biannual report on the economy, providing further evidence that governments have successfully arrested the worst global recession since the Second World War.

"Still, the fund economists who wrote the latest World Economic Outlook aren't exactly enthusiastic about their upwardly revised forecast. While better than the projected 1.1% contraction of 2009, the 2010 forecast compares with global growth of about 5% before the financial crisis hit. The rebound from recession foreseen by the IMF is slow by historic standards and built on shaky foundations.

"'According to these forecasts, the current rebound will be sluggish, credit-constrained, and for quite some time, jobless,' the report says."

In short, though sold as a chicken, it toddles and quacks like a duck.

"Sluggish or not, the IMF report reinforces Prime Minister Stephen Harper's boast that his and Finance Minister Jim Flaherty's policies have helped the Canadian economy weather the financial crisis better than most. Going into the financial crisis, Canada enjoyed a relatively strong fiscal picture, with federal budget surpluses and debt levels below many other nations, though Canada now expects deficits for several years."

However, these are grave issues, important enough to call in another witness, before putting the world's future on the executioner's block. So we will put *The Wall Street Journal* in the dock (29/09, "China Inc. Looks Homeward as US Shoppers Turn Frugal" by Andrew Batson and here is what we are told: "Shunde, China – With the longtime engine of global growth, the American Consumer, pummeled by recession, some of China's hugely productive exporters are eyeing a new market: the Chinese. Bicycle manufacturer Tandem Industries has long supplied big overseas retailers such as Wal-Mart Stores Inc. But Tandem's American sales have tumbled 40% since September 2008, the month a US credit squeeze turned into a US credit panic. So Tandem is about to offer its bikes to riders in its home province, Guangdong, under its own brand and at its own stores."

So you may say, "But, of course, the Chinese have been known for the crowds of bikes on their city roads." So back to *The Globe and Mail* (1/10, "Bombardier laid track long ago for deal in China" by Carolyne Wheeler): "Beijing – It was Montreal-based Bombardier Inc.'s biggest win yet in China. [Says 52-year-old Bombardier Zhang Jianwei who has no time for a day off.] 'This is the largest order we've ever had in China and one of the largest in the world also,' Mr. Zhang said in an interview yesterday: 'Though China's stimulus has been credited for the trains' purchase, the work for this tender has been going on for years,' he said. The planning has been in the works since well before the Chinese state National Development and Reform Commission gave the Ministry of Railways permission to issue 100 billion yuan ($14.6 billion) in bonds to finance new railway construction and locomotive purchases…. State media have reported that China plans to extend its rail network to 100,000 kilometers by 2020 from 76,600 km. in 2006, including some very high-speed lines, an undertaking expected to cost around two trillion yuan…. Helping Bombardier's case are the more than 1,000 of its cars already in service, on intercity lines, urban transit systems, and a high-altitude line serving the western autonomous region of Tibet.

"Mr. Zhang is tight-lipped when discussing Bombardier's next deal, though he alludes to more contract discussions under way. However, he can name almost all of China's 37 cities working on urban transit plans where opportunities are likely to arise."

And now back to the *G&M* (10/1, "China's birthday present: more resources" by Barrie McKenna): "Washington – China may be spending a lot of cash on resource assets. But Mr. Hughes of the Woodrow Wilson International Center said that doesn't necessarily mean Beijing controls the price or supply of the underlying commodities. 'They don't really control those assets,' Mr. Hughes said. 'They have a financial claim over the companies that control those assets It's quite different from buying up all the platinum in the world and storing it in a warehouse outside Shanghai.'"

Ponder that. What China must have gotten right, or, more correctly, what is right lies outside short-term market speculation and must have to do with its grasp of what money and currency are about. And that is where our Western governments clearly have slammed their minds shut to the slightest inkling of how they got into the present mess or how to get out of it.

For the answers are readily found in our history, just as the Chinese found them in theirs.

Having reached this point in my tale of what our neglect of the lessons that only history teach us, I chanced to be editing Volume 4 of *Meltdown. Money, Debt and the Wealth of Nations* and being lazy by nature, even as I may be working through the wee hours of night, I grabbed this passage on this long-forgotten performance of Theodore Schultz, as something that I could not improve on.

"At the end of World War II the US government looking ahead, sent many [hundreds of] economists to Japan and Germany to predict how long it would take for those countries to make good the devastation of the war and emerge again as formidable competitors on the world market. One of these, Theodore E. Schultz, of the University of Chicago, years later in 1961, wrote: 'Having had a small hand in this effort, I have had a special reason for wondering why the judgments that we formed soon after the war proved so wide from the mark. The explanation that now is clear is that we gave altogether too much weight to non-human capital. We fell into this error, because we did not have a concept of all capital goods and therefore failed to take account of human capital and the important part it plays in a modern economy.'"

Material Investment Never Clogs Up Human Investment

"We were taught to believe that a country which amassed more reproducible capital relative to its land and labour would employ such capital in greater 'depth' because of its growing abundance. But apparently, on the contrary, the estimates now available show that less of such capital tends to be employed relative to income as economic growth proceeds. For my purpose all that needs said is that these estimates of capital-income refer only to a part of all capital. Human capital has surely been increasing at a rate substantially greater than reproducible (non-human) capital. We cannot, therefore infer from these estimates that the stock of *all* capital has been decreasing relative to income.

"The income of the US grows at a much higher rate than the combined amount of land, man-hours worked and the stock of reproducible capital used to produce the income. Moreover, the discrepancy between the two rates has become larger from one business cycle to the next in recent decades.

"To call this discrepancy a 'measure of resource productivity' gives a name to our ignorance, but does not dispel it.

"In quoting these passages from Schultz in [his] *Human Capital* (Columbia University Press, 1971, p. 51 et seq.) in my *Price in a Mixed Economy – Our Record of Disaster* (Toronto, 1975), I added: 'Not only is education capital, but it is the most dynamic of all capital categories, endlessly revolutionary in its effect. The typical capital accumulation of earlier generations – railways, factories, machines – served as repository of society's inertia; its growth gave rise to spreading ranks of bondholders, rentiers, and passive stockholders. Over long periods its increase seemed to blunt the economy's hunger for more capital – to hold back technical innovation at times. Capital placed in education has quite opposite effect. It speeds the rhythms of change, shrinks write-off schedules, hastens obsolescence. It consigns machines, which had been regarded as provident investments par excellence, to the scrap heap.'

"Nor does misrepresentation stop there. If education must be considered an investment, then health and welfare of those in whom that investment is stored cannot be less important."

What Governments Forget in their Debt Collection Fervour

"All this seems to have been forgotten, from the evidence of *The Wall Street Journal* (6/01/05, 'US Gets Tough on Failure to Repay Student Loans' by John Hechinger): 'In dealing with material investments of the public sector, our governments were so carefree that until recently (2002 in Canada, 1996 in the US), when it recognized them as "savings" in their statistics. Yet "savings" they certainly were not, they were not in cash [or near-cash form that] this implied. Canada, though it has agreed under pressure from the previous Auditor General to recognize physical investments of the federal government as capital, has still done little to revise its books accordingly….

"There is not among investments in the private sector any known guarantee against investments going sour for quite irreproachable reasons. That is why the institution of protection against bankruptcy was devised. But Mr. Hechninger writes: Years after a political outcry over high levels of student loan defaults, the Education Department has become one of the toughest debt collectors around. A 1998 change in federal law, for instance, made it extremely difficult for people to escape student loans through personal bankruptcy. The Education Department also can now seize parts of borrowers' paychecks, tax refunds and Social Security payments without a court order, a power that only the Internal Revenue Service, among federal agencies regularly wields….

"In the mid-1990s, abuses cited by lawmakers were infrequent: 'More perception than reality.'

"But not long after, in 1998, Congress tightened the bankruptcy treatment of student loans. The changes resulted from wrangling over an education bill, says Harry Sommer, editor-chief of *Collier on Bankruptcy*, a legal reference work. The Clinton administration was seeking a reduction in student-loan interest rates, a move lenders opposed.

"A trouble with the politics of compromise is there is rarely room or insight left for the deeper perceptions of social-minded thinkers, who may have been honored for their highly esteemed work, but have no pres-

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A Tale Not Fully Told

As usual Paul Krugman, in his *New York Times* column (09/10, "The Uneducated American") comes up with a very basic problem that is threatening the unique master role that the United States occupied since World War I. Instead, however, of pursuing the problem to its logical conclusion, he merely tweaks it.

"If you had to explain America's economic success with one word, that word would be 'education.' In the 19th century, America led the way in universal basic education. Then, as other nations followed suit, the 'high school revolution' of the early 20th century took us to a whole new level. And in the years after World War II, America established a commanding position in higher education.

"But that was then. The rise of American education was overwhelmingly, the rise of public education. – and for the past 30 years our political scene has been dominated by the view that any and all government spending is a waste of taxpayer dollars. Education, as one of the largest components of public spending has inevitably suffered.

"Until now, the result of educational neglect have been gradual – a slow-motion erosion of America's relative position. But things are about to get much worse, as the economic crisis – its effects exacerbated by the penny-wise pound behavior that passes for 'fiscal responsibility in Washington – deals a severe blow to education across the board.

"About that erosion: there has been a flurry of reporting recently about threats to the dominance of America's elite universities. What hasn't been reported to the same extent, is our relative decline in more mundane matters. America, which used to take the lead in educating its young, has been falling behind other advanced countries.

"These days young Americans are less likely than people in many other countries to graduate from college. In fact, we have a college graduation rate that's slightly below the average across all advanced economies….

"In America, with its weak social safety net and limited student aid, students are far more likely than their counterparts in, say, France to hold part-time jobs while still attending classes. Not surprisingly, given the financial pressures, young Americans are also less likely to stay in school and more likely to become full-time workers instead.

"According to the Bureau of Labor Statistics, the US economy lost 273,000 jobs last month. Of those lost jobs, 29,000 were in state and local education, bringing the total losses in that category over the past five months to 143,000…. Yet markets may be troubled, but that's no reason to stop teaching our children. Yet that's exactly what we're doing.

"There's no mystery about what is going on: education is mainly the responsibility of state and local; governments, which are in dire fiscal straits. Adequate federal aid could have made a big difference. But while some aid has been provided, it has made up only a fraction of the shortfall. In part, that's because back in February centrist senators insisted on stripping much of that aid from the *American Recovery and Reinvestment Act*, a.k.a. the stimulus bill."

Education Is on the Chopping Block

"As a result, education is on the chopping block. And laid-off teachers are only part of the story. For example, the Chronicle of Higher Education recently reported on the plight of California's community college students. For generations, talented students from less affluent families have used those colleges as a stepping stone to the state's public universities.

"But in the face of the state's budget crisis those universities have been forced to slam the door on this year's potential transfer students. One result, almost surely will be lifetime damage to many students' prospects – and a large gratuitous waste of human potential."

First of all, Congress needs to undo the sins of February, and approve another big round of aid to state governments. We don't have to call it stimulus, but it would be a very effective way of creating or saving thousands of jobs. And beside it would be, at the same time an investment in our future.

But that must not only be done in columns and speeches, but in our government's accountancy. It was after all undoubtedly the greatest lesson to come out of the Second World War. Since COMER is about the only organization that refers to the stroke of genius of Theodore Schultz, let us repeat the story yet once more.

At the end of the war Washington sent

hundreds of economists to Japan and Germany to study the damage of the war and predict how long it would take those two once formidable trading nations to resume their past trading might.

And some sixteen years later, Schultz wrote a book saying it was amazing how wide of the mark their predictions were. This he explained because they concentrated on the physical destruction and paid little attention to the fact that the highly disciplined, trained and motivated labour force had come out of the struggle virtually intact. From that he concluded the investment in human capital is the most rewarding a government can make. For a very few years Schultz was celebrated and then as though someone had opened a trapdoor in the floor he and his great conclusion completely disappeared.

Proof of that is a distinguished economist like Paul Krugman, writing a column in what is likely the best newspaper in the world, dare not mention the name of a great innovative thinker who almost a half century ago salvaged a great principle that might have prevented humanity dipping into a bloodbath once again. Today that name – Theodore Schultz, though it could hardly be forgotten by Paul Krugman, is beyond his daring to mention.

We have been deprived of our history at a time when we stand in need of its lessons. We are not referring to general educational levels but precisely to the essence of what we need to emerge from the present world crisis before it has plunged us into what threatens to become the final folly of our species.

W.K.

Language of Deceit on the Tongues of the Mighty

The most flattering thing that can be said of our brand new Prime Minister Stephen Harper is that he has a way with words, neoconning them into quite the polar opposite of their accepted meaning. Even a right-inclining columnist like John Ibbitson of *The Globe and Mail* (11/10, "Clean-air pledge is just political smog") draws an unflattering conclusion: "Two months ago, Intergovernmental Affairs Minister Michael Chong said Canadians would be "pleasantly surprised" by his government's autumn proposals to improve air quality. He may have been right about the adjective; but there's nothing to justify the adverb. Stephen Harper's announcement that his government will introduce a Clean Air Act next week was simply a political mirage.

"When the Conservatives declared earlier this year that Canada would fail to meet its Kyoto targets, they were simply speaking the truth. The Liberal government signed the protocol committing Canada to reducing carbon-dioxide emissions, then failed to live up to that undertaking.

"But the Tories had another calculation in mind: Most Canadians were confused about global warming, which may or may not be linked to increased carbon-dioxide emissions, and which may or may not be reversible.

"But urban Canadians are very aware that smog is getting worse. The government's strategy was simple: Shift from greenhouse gases to smog. Produce a program that toughens automobile emissions and reduces the pollution from coal-fired generating stations. Ignore environmental zealots such as those at the David Suzuki Foundation, but aim for at least a partial endorsement from the moderates in the environmental movement.

"Nice plan. Isn't working.

"To reduce urban smog, the Tories needed to achieve several goals all at once : to work with the Americans to establish continental targets for reducing harmful emissions from coal-fired generating plants. And they needed to toughen emission standards at home. But there was neither time nor sufficient political capital to achieve the first goal, while the second would decrease business competitiveness and require Draconian increases in the price of cars and fuel.

"And the electorate, when it isn't demanding cleaner air, is buying stupidly huge trucks while protesting against rising gas prices. The Liberals, to their sorrow, know all about this.

"Stephen Harper wants to be known as the prime minister who tackled smog. But nothing he has offered thus far suggests that, when it comes to fighting bad air, he is anything other than just another disappointment."

However, his greatest misstep that concerns the environment, has to do with greenhouse-gas targets under the Kyoto Protocol. In the same issue of the *G&M* ("PM plans 'intensity alternative' to Kyoto" by Bill Curry and Mark Hume) we read: "Mr. Harper said his government will introduce next week its *Clean Air Act*, legislation that will trigger at least a year of talks with industry and the provinces to set mandatory reduction targets for pollution and greenhouse gases. But in responding to questions in Vancouver, Mr. Harper uttered a phrase that had the opposition fuming. 'We will produce intensity-based targets over the short range and long term and they will cover a range of emissions, not just carbon dioxide, but nitrous oxide, sulphur oxide, sulphur dioxide, and it will be a comprehensive plan.' It marked the first time the Harper government has said its plan to address global warming would be 'intensity-based'. This means industries would have to reduce emissions per unit of production, such as per barrel of oil. "Lowering emissions per unit, however, does not mean that Canada's total output of greenhouse gases will decline. If, for example, there is an expansion in the oil sands, total levels of emissions would increase even if per unit emissions decrease.

"Such an approach runs contrary to Canada's commitments under Kyoto, which calls for the country's total output of greenhouse gases to decline. Last month's report from federal Environmental Commissioner Johanne Gelinas warned that, left unchecked, greenhouse gas emissions from Alberta's oil sands could double between 2004 and 2015. But Mr. Harper said yesterday technology improvements will ultimately reduce total reductions over the long term. He cited a recent federal report that says emerging technologies – such as injecting carbon emissions back into the ground – could reduce emissions by 60% in 2050."

In short, the PM is evading the issue with a plethora of "mays" and "mights" decades ahead. From this there is a lesson to be learned. Once a political leader has done a masterful job in evading one important issue, he forfeits his conscientious use of language in dealing with other key issues that may arise. He acquires, as it were, a forked tongue that wraps itself around the very words of the issue and twists language to cover up rather than to clarify. Mr. Harper's "intensity-based" emission programs warns us of what lies ahead with Mr. Harper in office.

W.K.

Reforming Economics — Ten Quick Steps towards Reality Economics[1]

Emphasize that Social Costs are systemically generated and, generally, bend what is done in teaching and research to be explicitly relevant in socially progressive ways. That is, like good medical practitioners, try to make things better (as opposed to *market regressive* solutions that *make things worse*).

Mainstream economics was an *invention.* The major *entrepreneurs* contributing to "the theory" have long ago confessed that what they created was of bad design, inadequate and wrong. More than a few have said that economists have to go back to what Adam Smith, and others, really said about the system. Economists have to be concerned about economic and political power of the many visible hands that Smith discussed and not the mad-metaphor of an invisible hand.

Economic realists were doubters and disbelievers in the mainstream project long before the *entrepreneur's confessions.* A list of descriptions of mainstream or neo-classical economics includes: "a joke," "hot air," "witchcraft," "a para-science," "little boys sandbox games," "lacks vision," "autistic," and "truth distortion." A reformed economics would set out to avoid such descriptors. Economics administrators ought not to leave a scientific legacy of econometrics, statistics and mathematical economics none of which can go anywhere without adequate interpretations of systemic realities to fuel inquiry.

The *post-autistic economics* movement has contributed much to solidifying doubt and disbelief in the mainstream, and has assisted in making *the death of economics* a popular topic. All suggestions for reform involve getting beyond displinolatry and free market god worship. Nevertheless, the business mangers in charge of the discipline, and many in charge of economic policy at federal and provincial levels, with little interest in disturbing feathered nests, and probably not knowing what to do anyway, seem to hang on to past litanies of the orthodox faith that run in terms of leaving it to the market to solve all problems. This seems like avoidance of the truth that the system is dysfunctional. Moreover, truth avoidance confounds the historical big-picture project of the University. Upper level administrators seem complicit for they quickly surrender to the immediate "faddishness" of globalization, internationalization of operations, trade and even entrepreneurship. And so the discipline and the university are in the saddest of states and much in need of reform. And the market doesn't help progressive reform at all; it wasn't designed to foster social responsibility – the market's businesses shirk social responsibility.

What follows is a suggestion for a quick way to change what is done in socially responsible ways. Overall the suggestion is to deal explicitly with Social Costs in *all courses* beginning with the introductory elements dealt with in both Micro and Macro – through to courses in graduate programs. Some of this is under way now.

Some Necessary Systemic Reforms

But generally, even with an emphasis on systemically generated social costs mainstream economics requires systemic reforms along the following lines:

1. Fulfill the obligation *we have* to discuss and make known the United Nations Universal Declaration of Human Rights. Economic matters are central in the Declaration's last few articles. One can go on to the related covenants. This is a matter of equality rights of citizenship at home and abroad. The citizen has to be front and centre; democracy is advanced with the advance of human rights.

2. Be sure to always deal with factual reality along side the truth/untruth of mainstream theory. Since *reality* is different from mainstream theory one will finally be led to ask: Why hang onto a theory that doesn't explain anything but itself and that fails in its own logic anyway? J. Rawls – "…A theory however elegant and economical must be rejected or revised if it is untrue; likewise laws and institutions no matter how efficient and well-arranged must be reformed or abolished if they are unjust." (See S. Keen, W. Krehm.)

3. Make the capitalist system the subject of investigation. Do not take the system as a *not even defined, given.* In the sense of John Dewey, make the discipline of economics scientific. "The transition from an ordinary to a scientific attitude of mind coincides with ceasing to take certain things for granted and assuming a critical or inquiring and testing attitude." The work of P. Sweezy, C.B. MacPherson and S. Bowles and H. Gintis will assist in system definition and exploration in scientific terms.

4. Introduce power and institutional power in particular (power of the minority over others implies limiting freedom for otherwise equal citizens, the majority) as a unifying concept. (See J.K. Galbraith and R. Parker on Galbraith; also S. Marglin's, *What do Bosses Do?*)

5. Deal with law and property rights. Particularly use H. Glasbeek's *Wealth by Stealth: Corporate Crime, Corporate Law and the Perversion of Democracy.* Written by a corporate lawyer and Professor of Corporate Law at Osgoode Hall, Glasbeek's book should be of particular relevance in dealing with reality in courses in Industrial Organization. But no restrictions should apply; simply make it required reading. Glasbeek's book can be used at all levels.

6. Introduce pricing through markups on costs. Generally, prices are administered to all markets with demand determining supply and supply costs determining prices. While this generalization is close to reality, in some cases, however, prices are set, *customized to the customer,* without any reference to costs. The aim as to extract the largest incomes as possible from unsuspecting consumers who are kept ignorant of what is happening to them. The markup then falls out after the fact on each order that is placed.

7. Dispense with diminishing returns (at least put it on a hot back burner). Instead put increasing returns and declining average costs up front. Joined with power and administered prices competition quickly disappears as "capitalists eat capitalists" and force a private inter-sectoral and indeed international collectivization of industry. This is real *economic power in motion* and it is the on-going or evolving reality that everyone faces. (See the discussion of Schumpeter and McCluhan in *Profit as the Root of All Evil.*) Is

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it any wonder that unemployment, poverty, homelessness, environmental destruction, deaths in the work place, etc., are systemic social costs calling for *education, agitation and legislation*, to reform the system. Economics and economists can and should lead in contributing to that reform – but the mainstream seems to cower with collective heads in the sand.

8. Take scarcity as primarily a concept relevant to an inadequate distribution of income for many. That is, *scarcity* means scarcity of commodities for those for whom their poverty is systemically explained. This is related to all of the above through gross inequalities in the distribution of income. This is perhaps the point at which one should introduce the idea of providing income to all as a right of citizenship thus stripping the normal mainstream tie between income and work. A universal basic income (UBI) puts the citizen at the heart of public policy and the extension of democracy and freedom.

9. Introduce institutions such as banking, finance, and insurance as devices that assist in the systematic drain of income from the weaker to the more powerful. In this connection deal with slavery, wage slavery, debt slavery. Slavery required abolition (though still incomplete). The "system" ostensibly replaces personal slavery by wage slavery and debt slavery. Upton Sinclair has said: "The private control of credit is the modern form of slavery." (See Rowbotham.)

10. Into the above the full range of social costs (major costs already noted) may be inserted and elaborated as items that the system tries to escape by shifting responsibility onto individuals, communities, and generally onto society's shoulders. (See K.W. Kapp.)

A Social Costs approach to the delivery of economics will allow complementary links to other areas in Faculties of Arts, Environmental Studies, Engineering and the Sciences and implies a policy and applied economics emphases with easy links to the broader community. And as above, it also will mean a start at a relevant link between law and economics.

Reasons for Recognizing the Perils of Corporatist Governance with Democracy

But there are other reasons why one ought to stress social costs.

So long as *corporatist governance in competition with democracy* is not recognized and not put up front Economics departments intellectually, in effect, and however implicitly, will be *saying that capitalism as fascism* is a given and is not a problem. It would be difficult to be more out of touch with reality and a "scientific attitude of mind."

That capitalism is *the problem* (whether or not one can stomach the reality of fascism as capitalism) is an inconvenient truth. The fascist fact is not at all contentious for many academics. Some seem happy to be complicit in its embrace.

But the fascist label will be a problem (at least one might hope it would) for the managers of universities who have succumbed to corporate lures in some fashion or another. Some, thinking that there is nothing that can be done, will merely shrug and shirk their larger social responsibilities.

And so it goes.

The attached bibliography provides more extensive support for the line of argument presented here. It ought to be more generally useful.

W. Robert Needham
University of Waterloo

1. Some of the historical support for what follows is found in: *The Essentials of Capitalism Through Definitions: From Adam Smith to the Present Day*: http://economics.uwaterloo.ca/needhdata/CapitalismsEssentialsREV4.pdf.

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As Important as Trade Are Our Human Relations with China

The Globe and Mail (10/6, "First Person" by Yuen Paul of the Asia Pacific Foundation of Canada, reminds us what is needed is a Canada-China "human capital" pact.

We love the association of "human" and "capital" because our government is still resisting putting that adjective and that noun together. Once they learn to do that in our government accountancy most of the world's economic problems will fly away and leave the world equipped to deal with its real issues. But let us listen to Mr. Yuen Pau Woo: "China's ascendancy on the world stage has forced a reconsideration of its role in all aspects of international affairs. The least understood feature of China's impact on the global economy is human capital.

"It isn't simply that a population of 1.3 billion potential consumers constitutes an enormous market for goods and services. Nor is it that the massive ranks of reserve labour in China's rural areas will exert downward pressure on wages around the world.

"Rather, it is that human flows will be an increasingly important dimension of China's connections to the world. In the same way that the People's Republic is 'going global' as an exporter of capital and as a host country for foreign direct investment, two-way flows of people will affect foreign policy, corporate strategy and popular perceptions of the country."

"Of all the reasons for Canada to have a robust and forward-looking China policy, human capital is arguably the most important."

And surely that principle must be reflected in our government's accounting and everything else.

"The amount of travel between Canada and China is unmatched by China's ties with any other country belonging to the Organization for Economic Co-operation and Development.

"Canada-China human flows run deep, starting with the arrival of railway workers on the West Coast in the late 19th century The history of Chinese immigration to Canada has had its dark periods, most notably the imposition of a head tax between 1885 and 1923, followed by the *Chinese Exclusion Act*, which was repealed only in 1947. However, the overall picture of China-Canada people movements, especially in the past 60 years, has been overwhelmingly positive.

"The best measure of progress can be found in Canadian cities where substantial communities of ethnic Chinese residents have successfully integrated into the mainstream. While there are predictable – and, to some extent, growing – challenges related to settlement, jobs, income and integration, most of these difficulties are overcome within one generation. A new study of Canadian youth, for example, shows that 88% of young Chinese immigrants go to university, more than double the figure for young Canadians."

There is no way of exaggerating the key importance of that figure, since a sense of the importance of human capital in a nation's legacy and achievement can hardly be exaggerated. Nor disregarded Canada's politicians.

"China has been Canada's No. 1 source of immigrants for the past 11 years. Between 1998 and 2008, an estimated 360,000 Chinese nationals emigrated to Canada, accounting for 14% of new arrivals. Including immigrants from Hong Kong and Taiwan who arrived in the decade prior to 1997, new arrivals from greater China in the past 30 years account for a vast majority of the 1.3 million Chinese living in Canada today.

"It would be a mistake, however, to think that the flow of people amounts to inbound immigration only. Greater freedom of movement in and out of China and the growing influence of Chinese citizens are rapidly changing the pattern….

"Whereas Chinese students in the 1990s would have been inclined to stay in Canada after graduation, the trend is now for graduates to return to the mainland, where job opportunities are considered more attractive....

"While challenges may arise from diaspora-like populations at home and abroad, the phenomena of international labour mobility – especially of the most talented, and sometimes the most notorious – is here to stay. The challenge for policy is to take a holistic and multi-generational view of transnational citizens, rather than to treat them as a problem.

"Seen in this light, the Canada-China human capital nexus is a unique focal point for Ottawa and Beijing. While other countries are lining up to sign trade and investment agreements with China, Canada can go a step further and investigate the possibility of human capital agreements. That could encompass citizenship, visa, education and training, professional accreditation, social security, taxation and even extradition issues.

"We have an opportunity now to address these issues in a comprehensive fashion, and to turn potential problems into a fundamental strength of Canada-China relations."

W.K.

Washington Still Refuses to Examine Its Only Way Out of the Mess — Serious Accountancy and the Lessons of History

The Wall Street Journal, not known for its left-wing views, tells an already drearily familiar tale: (31/08, "FDIC shoulders big losses on loans" by Damian Paletta): "Washington – The biggest spur to deal-making among American banks isn't private equity cash or foreign investors. It's the US government.

"To encourage banks to pick through the wreckage of their collapsed competitors, the Federal Deposit Insurance Corp. has agreed to shoulder the bulk of future losses on $80 billion in loans and other assets. The initiative amounts to a subsidy for the struggling banking industry.

"Through more than 50 deals known as 'loss-cover shares,' the FDIC has agreed to absorb losses on the detritus of the financial crisis – from loans on two log cabins in the woods of Illinois to hundreds of millions of dollars in busted condominium loans in Florida. The agency's total exposure is now about six times the amount remaining in its fund that guarantees consumers' deposits, exposing tax-payers to a big, new risk.

"As financial markets heal and the economy appears to be pulling out of recession, the federal government is shifting from crisis to cleanup mode. But as the loss-share deals show, its potential financial burden isn't receding. So far, the FDIC has paid out $300 million to a handful of banks under the loss-share agreements It expects it eventually will have to cover about $14 billion in losses on the deals cut thus far.

"The practice is largely a response to the ballooning number of bank failures of the past 18 months, which has stretched the FDIC's financial resources. The FDIC had just $10.4 billion in its deposit-insurance fund at the end of June, down from more than $50 billion last year. The agency said Thursday that it had 416 banks on its 'problem' list at the end of the second quarter, which means the list of banks at a higher risk of insolvency has been growing.

"On August 14, Alabama's Colonial Bank collapsed, felled by bad commercial-real-estate lending. The FDIC, assuming its traditional role, stepped in and brokered a sale of the bank's deposits to BB&T Corp., ensuring the customers that customers wouldn't see any interruptions. It also agreed to help BB&T buy a $15 billion portfolio of Colonial's loans and other assets by agreeing to absorb more than 80% of future losses. Under the deal, the most BB&T can lose is $500 million, the banks says, and that's only in the unlikely event that the portfolio of Colonial's loans and other assets becomes worthless. The FDIC is on the hook to cover the rest.

"'After we understood how the loss-share works, we were literally overjoyed,' says Joanne Kim, chief executive of Wilshire State Bank.

"Loss-share agreements made a brief appearance in the early 1990s during the savings-and-loan crisis, but haven't been used this extensively before. The FDIC sees the deals as a way to keep the bank loans and other assets in the private sector. More importantly, it believes such deals mitigate the cost of cleaning up the industry. The FDIC contends it would cost the agency considerably more to simply liquidate the assets of failed banks, especially with the current crop of troubled institutions and their portfolios of loans on misbegotten real estate.

"The FDIC's premise is that banks that take on the troubled assets will work to improve their value over time. The agency estimates that the loss-share deals cut thus far will cost it about $11 billion less than if the agency seized the assets and sold them at fair-market value.

"'This is an issue the FDIC is grappling with because the loss rates they are estimating on these failed banks are pretty amazing,' says Frederick Cannon, chief equity strategist at Keefe, Bruyette & Woods Inc.

"By potentially mitigating losses – or stretching them out over time – the deals provide some protection for the agency's insurance fund.

"'It's a great opportunity for banks,' says James Wigand, deputy director of the FDIC's division of resolutions and receiverships."

That makes it sound like everybody is triumphing. The only item missing are the Roman candles to celebrate the occasion.

However, "The US government is now on the hook for billions of dollars in bank losses if the economy doesn't recover. It will carry that burden for a long time. Many of the loss-share deals will be in place for up to 10 years."

"Since January 1, 2008, 109 banks in 29 states have failed, ranging from one of the smallest banks in the country, Dwelling House Savings and Loan in Pittsburgh, a one-branch bank with $13.4 million of assets to Washington Mutual, which has $307 billion of assets and was the largest bank failure in US history."

Huge Dent in Reserves

"Those collapses have cost the FDIC an estimated $40 billion, putting a huge dent in its reserves. The FDIC was created during the Depression to maintain consumer confidence in banks by guaranteeing deposits. If its deposit-insurance fund runs out, the FDIC would likely have to borrow money from the Treasury Department or slap higher fees on the banks whose contributions keep the fund afloat."

The implication – not spelled out in the article – is that the largesse being poured out on the banks who step in to pick up highly questionable bargains in the banks' wreckage will eventually turn up depleting the FDIC fund guaranteeing bank depositors and thus must eventually come back to hit the banks – to say nothing of the rest of society.

"During the savings-and-loan crisis in the 1980s and early 1990s, more than 1,000 banks failed. The government set up the Resolution-Trust Corp. to take over assets from failed banks and sell them. Such a structure doesn't exist now, which means that the FDIC has to take on those assets or somehow persuade healthy banks to do so.

"Last year, the agency struck only a handful of loss-share deals with healthy banks. That left the government with lots of troubled loans from troubled banks to sell.

"'The hardest part today in the acquisition game is valuing assets or determining real equity, and with a loss-share you can do that,' says Len Williams, chief executive of Home Federal Bank in Idaho, which picked up $197 million in assets from the failed Community First Bank in Oregon as part of a loss-share agreement on August 7.

"In most cases, the FDIC agrees to cover 80% of future losses on a big portion of the assets, and 95% on the rest. The FDIC says it doesn't anticipate facing the 95% loss-coverage scenario on any deal."

Federal Deposit Insurance Absorbs Mammoth Risks

"Typical assets include loans on commercial real-estate developments, condominiums and single-family homes. Banks are required to report at least every quarter on estimated losses, and to have a team in place working full time to maximize the value of assets. Banks must get permission from the FDIC to sell any loans.

"Big banks also have used the deals to grow with minimal risk. On August 21, BBVA Compass, a unit of the giant Spanish company Banco Bilbao Vizcaya Argentaria, bought $12 billion in loans and other assets from the failed Guaranty Bank in Austin, Texas. As part of the deal, the FDIC said it would cover most losses on a $9.7 billion portion of that pool, the Office of Thrift Supervision said last week that more than half of Guaranty's loans were 'higher risk,' including commercial construction and land loans.

"BBVA Compass said the deal would have the FDIC bear 80% of the first $2.3 billion of losses and 95% of the losses above that threshold. Its chairman, Jose Maria Garcia Meyer-Dohner, described it as a 'low risk transaction.' The arrangement made BBVA Compass the 15th-largest bank in the US.

"Veteran banker Joseph Evans saw the share-loss deals as a major opportunity. He approached State Bank and Trust Co., in Pinehurst, GA, with just $35 million in assets, with a proposition: he would take charge of the bank, find investors to pump $300 million of capital into it, then buy up the assets of the failing banks in Georgia.

"Mr. Evans, who has spent years selling distressed assets, recruited investors, and on July put his plan in motion. The FIDC shut down six affiliated Georgia banks and agreed to sell $2.4 billion of deposits and $2.4 of assets to Mr. Evan's team. The FDIC agreed to absorb most of the losses on $1.7 billion of those assets. Overnight, the small bank became one of the largest in the state.

"'From a turnaround guy's perspective, I've never had this kind of downside protection,' Mr. Evans says. 'I don't think that we would have been interested or found interested investors to enter the banking industry at this moment, absent the FDIC assistance.'

"He says there's a good chance his team will make a strong profit. He estimates it will take roughly four years to work through the bad assets in the portfolio.

"The FIDC wouldn't have to resort to such deals if it could easily sell the assets of failed banks. But last year, most healthy banks refused to bite."

In short it was the old story that the banks gamble and the government in one way or another the government pays for the smashed crockery and assumes a stern attitude of responsibility by cutting services vital to society. And thus "repaired," the stage is readied for the next extravaganza of the banks in taking over the world.

Yet to provide a serious alternative all we need is a cut of our history from the time the banks were so discredited that Franklin Delano Roosevelt was able to bring in the *Glass-Steagall* law that forbade banks from acquiring interests in the other non-banking financial pillars. For what feeds unsustainable bank booms is taking over the reserves other financial pillars need for their own businesses to serve as base for the banks' own money-creation. What results is a growing skyscraper of speculation with elevators that run at accelerating speed only upward, never down. For even a slow-down of this insane phenomenon would bring down the growth forecasts already incorporated in the banks' market price.

The other is for governments to make full use of the facilities of Federal Reserve, and Canada of its nationalized Bank of Canada to finance its capital investments. In that way much of the interest paid by governments on their investments would return to them – as dividends in Canada, since the Bank of Canada was bought out for a good profit from private investors in 1938. In the United States the cost to the government of using the partly government owned Fed would be still be far less than raising it by bond issues.

Crusaders Bring Back Serious Accountancy from Holy Land

And then there is the simple principle of honest accountancy. Roughly a thousand years ago, an order of Crusaders returned from the Holy Land with an accountancy principle invented in Muslim countries to track down what interest is being charged by passive investors. For unless the financier actually shares the risk of the entrepreneur, collecting interest for simply lending him money would net him an eternity in hell. The double-entry or accrual accounting brought back to central and Western Europe by the highly prosperous Knights Templar called for two entries covering every transaction – one recording the cash or credit spent for an investment amortized "to the death" in Latin or "to the repayment of the investment cost" according to a fixed schedule. The other showed the current value of the investment which is depreciated (from the Latin for price "pretium") showing the current value of the investment. This made it possible to tell at any point how the investment was faring. Such accrual accountancy made feasible the financing of the costly voyages of exploration that led to the discovery of the Americas, and the sea route to Southern and Eastern Asia around the Cape of Good Hope. It also led to the financing of the wars that replaced the tiny feudal principalities of Europe by national governments, though in process of financing these conflicts many banks went broke.

In more recent times, governments have amortized the debt of their physical investments, but depreciated the resulting capital assets in a single year. This results in a debt on the government books that is entirely fictitious. It bears out a crucial theory of a late, great French economist with whom I was closely associated, François Perroux – his theory of the "dominant revenue." This holds that in every society the folks in the saddle present their revenue as a suitable index of the welfare of society as a whole. During and after the Napoleonic wars the DR was the high rents charged farmers because of the high tariffs on foodstuffs. With the introduction of Watt's steam engines in the British factories, the DR shifted to the industrialists who to profit from their unique efficiencies arranged the repeal of the Corn Law high tariffs to bring down the subsistence wages they paid their workers. You will find further details on the later DRs in our other publications.

What we need today is to change the "dominant revenue" from that speculative banking that must continually grow faster and faster to avoid crashing and embrace society's broader survival needs.

Moreover, there is both in the US and in Canada the example of it having been done with investments in physical capital. That happened at the height of the Savings and Loans crisis in the US where banks had lost much of their capital, and the crisis threatened to bring down the world financial system. What saved the day was

Washington recognizing the value of its investment in physical capital that had been carried on its books completely depreciated in a single year. That had produced a vast debt that was really not there. By introducing serious accounting the physical assets of government investments was depreciated over their likely usefulness. Introduced in the US in 1996 and carried back to 1959, that added some $1.5 trillion dollars by the most conservative calculation that had been completely ignored. It was not, however called "investment" but "savings," which usually refers to cash or short-term securities of the highest quality. That gave Clinton his second term and prevented the cave-in of the world financial system. Instead it produced the high-tech boom and the great bust in 1998.

And here we are confronted with the phenomenon that we opened our evening with – the spreading pattern of dodging actual relationships and resorting to fictitious ones. This leads to the complete ignoring of the lessons of our history, and economic reality.

The "dominant revenue," then, is then the exact equivalent of the growing reluctance of our generation to recognize our history and basic relationships, very much like the declining hold of formal marriages amongst older and even younger populations.

That is why, even with example before us of the solution of the major financial crisis in the early 1990s by introducing accrual accountancy for physical investments before us – though rarely if ever mentioned by those who rule the roost, our leaders – even President Obama himself have never mentioned it. Yet it has been only necessary to recognize the vast investments of governments in human capital, to reveal a prepaid source of investment that would have prevented the present crisis. Once recognized and spent in building schools for retraining our unemployed and investing in health and the environment would provide the purchasing power to get the economy moving upward again. For there is this about human capital – its expenditure is itself in many instances an investment. One of the greatest lessons of World War II was that investment in human capital is the most profitable investment a government can make.

What stands in the way of that buried lesson is the "dominant revenue" of the speculative bankers.

However, until we deal with that, society's future will continue bloody and glum.

William Krehm

Letters

Curse of Uninsurable Insurance

Our apologies to Vincent Curtis for our unintended delay in making use of his excellent letter with the reference to Aristotle, who is a most favoured source of ours. As penalty we invite Vincent Curtis to choose whatever book of our own publications as a gift with our apology. – Bill Krehm

Mr. Krehm,

In his philosophical works, Aristotle often used the expression "on pain of infinite regress" to point out the fallacy of redundancy. Infinite regress describes perfectly the process involved in credit default swaps explained in the article referenced.

Insuring against a bond is absurd, and the infinite regress such an absurdity created has led to the financial meltdown on Wall Street, predicted by you in the September 2008 issue. A bond is supposed to be backed by the assets of the corporation issuing the bond, and the risk involved is supposed to be measured by the interest rate of the bond, and by its trading value in the secondary market. To take out insurance on a bond first involves measuring the credit risk of the issuer of the bond by the issuer of the insurance – a task that should have been carried out by the buyer of the bond in the first place or least by the bond rating agency. Then the insurance purchaser has to pay for the insurance against the bond! Where is the money for the insurance supposed to come from – the interest rate on the bond? But would it not simply have been easier to sell the bond at a loss in the secondary market than pay the insurance? If the insurer correctly rated the risk, he ought to be charging at least as much and probably a little more than the loss incurred in selling the bond on the secondary market by the holder. Absurdity piled on absurdity!

The more complex these inter-related redundancies become, the more impossible becomes the forecast of the results of an actual default, even with computer models. Somehow, the appropriation of the assets of the company that issued the bond in the first place seems to disappear from the resolution because nobody can clearly claim to be the owner of the assets pledged against the bond. Absurdity.

Imagine having bought a bond from Lehman Brothers. Imagine then buying insurance from Lehman Brothers as a hedge against the default on the Lehman Brothers' bond. Lehman Brothers then goes into default. What's the result? You paid Lehman Brothers twice and have nothing to show for it. Lehman Brothers took money from you twice, and gave nothing back. But then Lehman Brothers played that game themselves with the money you gave them, and got burned! Burning you in turn!

These financial wizards were so smart, they outsmarted themselves!

If nothing else, Aristotle's warning against the infinite regress proved true once again. The KISS principle needs to be applied to financial markets as well.

Vincent J. Curtis

Carney's Desire

Mr. Krehm,

In a speech given at a Women in Capital Markets event, Governor of the Bank of Canada David Carney suggested that banks could be required to "build up their capital buffers during times of rapid credit expansion, then draw down these buffers during a downturn. In this way, capital requirements would moderate the ups and downs of the credit cycles – the reverse of what actually happens – reducing the risk of a future crisis."

It would be too much to ask of the governor to use an indiscrete expression like "reserve requirements" in place of "capital buffers" and "capital requirements." Nevertheless, we are all COMERites now!

Vincent J. Curtis

Information from Italy

Dears sirs,

We are a group of citizens living in Bergamo, near Milan, Italy, who have during the last two years developed interest in monetary issues, starting from the writings of Prof. Auriti, professor of International Law at the University of Chieti, Italy.

Prof. Auriti's main thesis is that the contemporaneous social-economic crisis is due to the fact the States have lost the property of the money and that all the money is now issued as debt towards States and citizens by the bank system. In other words, for Prof. Auriti it is absolutely essential to direct our attention to some basic question about money: what is money, who owns it at the moment of its creation and what are the social and economic consequences of it.

Prof. Auriti proposes a very simple solution: to abolish the money-debt and to give back the property of every new created money to the citizens through the State, abolishing the fractional reserve. You can find further information about Prof. Auriti's writings on www.calneva.com/money/italy.

We would like very much to have your opinion about this matter. We would also like to share with you a concern that we have: we struggle to find renowned economists who have the courage to denounce the system of money-debt. Would you be able to provide us with some names?

Yours sincerely,

Dr. Matteo Mazzariol Bergamo
Italy Secretary of "Comitato di Liberazione Monetaria" ("Money Liberation Committee") of Bergamo

Thanks from Wayne Roberts

Dear William,

Just a brief note to thank you for sending me your marvelous magazine, COMER. I always enjoy it but am moved to write today because I read two in a row at a coffee shop. I find the banking stuff tough slogging, despite your excellent writing, but am so keen on your human capital material; plan to include material on that and credit you in a forthcoming book on the food revolution.

All the best to you in your excellent work.

Cheers,

Wayne Roberts

Lessons for Obama about Proper Accountancy in Nobel Biology Awards

The New York Times (10/06, "Three Americans Share Nobel for Work in Cell Biology" by Nicholas Wade) has a crucial message on whether money spent on education should be treated as just as an expense or as investment. Indeed, as was recognized just a few years ago as the most productive investment that a government can make.

We quote: "The Nobel Prize in Physiology or Medicine was awarded Monday to three American scientists who solved a problem of cell biology with deep relevance to cancer and aging. The three will receive equal shares of a prize worth around $1.4 million.

"The three solved a long-standing puzzle involving the ends of chromosomes, the giant molecules of DNA that embody the genetic information. These ends, called telomeres, get shorter each time a cell divides and so serve as a kind of clock that counts off the cell's allotted span of life.

"The three winners are Elizabeth H. Blackburn of the University of California, San Francisco, Carol W. Greider of the Johns Hopkins University School of Medicine and Jack W. Szostak of Massachusetts General Hospital.

"The discoveries were made some 20 years ago in pursuit of a purely scientific problem that seemingly had no practical relevance. But telomeres have turned out to play a role in two medical areas of vast importance, those of aging and cancer, because of their role in limiting the number of times a cell can divide.

"'I am thrilled that basic science can be celebrated,' Dr. Greider said in an interview Monday.

"Only eight women had won the Nobel Prize in Physiology or Medicine. Asked how she felt about coming No. 9, Dr. Blackburn replied, 'Very excited, and hoping that nine will quickly become a larger number.'

"Thomas Cech, a Nobel Prize winner at the University of Colorado, said the discovery had a broad impact had had a broad impact on several fields of biology and medicine and had also provided a 'fascinating insight' into the transition between the DNA world and the RNA word that preceded it in the origin of life. RNA is a close chemical cousin of DNA.

"Though Americans have again made a clean sweep of the Nobel medicine prize, two of the three winners are immigrants. Dr. Blackburn was born in Tasmania, Australia, and has dual citizenship; Dr. Szostak was born in London. Dr. Blackburn came to the United States because it was 'notably attractive' as a place to do science. While America is still a magnet for foreign scientists, she said, 'one shouldn't take that for granted.'"

The Urgency of Recognizing the Crucial Importance of Human Capital

"Dr. Szostak also said the world was now more competitive in science. 'So maybe we have to work a little harder to attract people from around the world and make sure they stay here,' he said."

That would certainly include recognizing that investment in human capital which must certainly include education, health, and care of the environment at every level as the most productive investment a government can make. That was in fact undoubtedly the most important lesson to come out of World War II. It was arrived at like the discovery of the three most recent Nobel Prize for Physiology and Medicine almost as those by accident. At the end of World War II, Washington had sent hundreds and hundreds of economists to Japan and German to study the war-inflicted damage and predict how long it would take for those two formidable traders on world markets to resume that role again. Sixteen years later, one of these, Theodore Schultz of the University of Chicago published a book saying it was remarkable how wrong the conclusion of his colleagues and himself had been. This he attributed to their having concentrated on the physical destruction, and overlooked the far greater importance of the fact that the work force at all levels had come through the war almost intact. From there he went on to the conclusion that government investment in human capital is the most profitable a government can make. For that Schultz was feted and decorated, but within a few years completely forgotten. At the moment – would it were not so – COMER is probably the only organization that keeps his great conclusion alive.

The reason for that was a sociological law, formulated by a great French economist, François Perroux – equally forgotten – that sheds light on the oblivion that has overtaken Theodore Schultz and his great conclusion. It was his law of the "dominant revenue" the holds that in every economy, the revenue of those in the saddle is taken as the proper index of the welfare of society as a whole.

After the Napoleonic wars in Britain it was the sky-high rents made possible by high tariffs. But then with the switch of the factories to steam-powered machinery brought in by John Watt, the industrialists to profit from the lowering of the subsistence wages they paid their workers, became advocates of free trade at home and abroad, and had the protective high tariffs repealed. But the most sensational instance of the "dominant revenue," transformed the very essence of official economic theory. Up to then almost all economists, from Adam

Smith to Ricardo, had based their value theories on some version of the amount of average labour that went into the production of a given economy.

So long as the British labouring class were illiterate, they could scarcely follow the discussions and debates that went on around them. But by the mid-century, the workers were learning to read and any version of the labour theory of value, was bound to have a revolutionary effect. Barricades were being thrown up in most European capitals, and before long a stream of defeated socialist and anarchist leaders found refuge in Britain. These included Karl Marx and Friedrich Engels, whose friends and families lost no time in organizing open-air meetings denouncing capitalism almost within earshot of Buckingham Palace.

Obviously the "dominant revenue" was due for a drastic change. It came in fact from several different sources in various European capitals, quite independently, within a year or two. It shifted the basis of evaluation of commodities from the amount of labour that went into their production, to the amount of pleasure their consumers derived from their consumption. And it solved all problems in an acceptably polite way. Unemployment? That simply was declared non-existent. What had been mistaken for it was simply the fact that the worker had compared the satisfaction derived from spending the wages that he was offered with enjoying the delights of leisure in his parlor, and had concluded that the latter was the more rewarding. And the reasoning was topped off with an illiterate misuse of differential calculus.

It was forgotten that the *empirical* content that mathematics can bring to a problem is zero, what is infinite is its *analytical* power. That has been one of the roots of the present crisis that refuses to go away. It has been overlooked that you may be able to insure against something that is very risky, but not against something that is not "risky" but *wrong*. Thus the proposition 2 + 2 = 5 is not "risky" but "wrong." Write insurance against that and both the insured and the insurers will go bust. That is precisely what has happened with the bailout of AIG.

Returning to the *Times* article: "Dr. Cech, former president of the Howard Hughes Medical Institute, said the more onerous visa requirements imposed on foreign scientists in the wake of the September 11 attacks were benefitting European countries especially. 'Even so, there is an implication when foreign scientists apply for, visas, they should be distrusted, denied several times, and should have to hire lawyers and jump through a lot of hoops,' he said.

"All three of the prize winners seem to have had science in their genes, and certainly in their home environment. Dr. Greider is the daughter of two scientists with doctorates from the University of California, Berkeley, she too, has a PhD from there. Dr. Szostak's father was an engineer. Both of Dr. Blackburn's parents were physicians.

"The study of telomeres is notable as a field of research in which female scientists are particularly prominent. Dr. Greider attributed this to a 'founder effect,' the founder being Joseph Gall of Yale University. Dr. Gall trained Dr. Blackburn and other women, and they recruited others to the field 'because there is a slight tendency for women to work with other women,' Dr. Greider said. She herself trained with Dr. Blackburn.

"The field of telomere research grew out of a puzzle in the mechanics of copying DNA. The copying enzyme works in such a way that one of the two strands of the double helix is left a little shorter after each division. Work by the three winners and others led to the discovery of telomerase, a special enzyme that can prevent the shortening by adding extra pieces of DNA.

"Dr. Blackburn addressed this problem by working with a single-cell organism found in pond water known as Tetrahymena. She found in 1978 that the telomerase had a very unusual structure, in which the same sequence of six DNA units was repeated some 50 times."

Outlay on Human Capital Is an Investment Not a Debt

"She and Dr. Szostak, who with her help had detected telomerase on Christmas Day 1984. Going into the lab that morning, Dr. Greider saw from the telltale signature of the six-unit repeat that she had captured telomerase. 'That was really an exciting day,' she said.

Our Society is Being Rejigged

The Wall Street Journal (10/2, "'Jobless' and 'Recovery' May part Company – Ahead of the Tape" by Mark Gongloff) is being rejigged in ways that spell no good.

"Employers may be losing their appetite for firing, but it may be a while before they are hiring.

"The labour market is expected to look marginally less terrible when the Bureau of Labour Statistics releases September employment data on Friday. Economists think non-farm payrolls shed 175,000 jobs last month, the lowest count since August 2008, though – with this week's economic – some worry the numbers could be worse. The economists think unemployment ticked up to 9.8% from 9.7%, the highest since 1983.

"Unemployment is expected to rise to 10% at some point next year, as workers tiptoe back into the labour force to forage for jobs amid signs the economy is improving, but with companies still reluctant to hire.

"Companies have the cash for hiring, thanks partly to profits they have wrung from a weak economy by cutting staff. But given widespread anxiety about the recovery's strength, businesses might seek other ways to increase to increase production before adding workers.

"There is room, for example, to stretch the work week, which was near-record-low 33.1 hours on average, in August. Getting back to a pre-recession 33.8 hours would be tantamount to hiring three million workers, said Gluskin Sheff economist David Rosenberg.

"Companies could also hire temporary workers again. They have let temps go for 20 months in a row, driving temporary payrolls to their lowest levels since 1995.

"Firing and hiring workers is expensive, which is why even in the worst recessions most unemployment is temporary – companies furlough then call them back when the smoke clears.

"But for the first time in the nearly 30 years the BLS has kept track, a majority, nearly 54%, of unemployed workers are permanently laid off.

"Stocks often rise with unemployment. But they have already come a long way. In the past 35 years, by the time the S&P 500 has risen 58% – its recent peak – non-farm payrolls have added, on average, 2.85 million jobs. This time they have shed at least 2.4 million.

"Goldman Sachs on Thursday raised its estimate for September job losses, a move that helped drive the stock market's selloff. That suggests stocks finally losing patience with weak employment."

W.K.

"Later she found that telomerase contains a special piece of RNA that it uses as a template to elongate the chromosome with six-unit repeats. The unexpected involvement of RNA reflects a time early in the origin of life when all the important chores in the cell were performed by RNA, not DNA.

"This piece of basic biology soon turned out to have important implications for aging and cancer. Telomerase is usually active only at the beginning of life; thereafter the telomeres get shorter each time a cell divides. If they get too short, a cell is thrown into senescence, meaning that it cannot divide again.

"Short telomeres are known to have a role in certain diseases of aging like aplastic anemia. Telomeres are also important in cancer, a disease in which control of cell proliferation is lost. Cancer cells need to reactivate the telomerase gene, or their telomeres will get steadily shorter, forcing them into senescence. In some 80 to 90 percent of human cancer cells, the telomerase gene has been switched back on. The Geron Corporation has two clinical trials under way, one of a drug and one of a vaccine, to see whether cancers can be treated by inhibiting telomerase.

"Both Dr. Blackburn and Dr. Greider still work on telomerase, but Dr. Szostak left the field 20 years ago to explore a much broader question: how life could have originated from the simple chemicals present on the early earth. He has already made advances in this long intractable proto-cell could have formed and then imported the RNA building blocks. Dr. Szosrtak hopes next to show how the proto-cell and its RNA could divide naturally into two daughter cells, a feat that, if achieved, could well be a candidate for a second Nobel Prize."

Need we say that the money laid out by whatever governments on this clutch of brilliant scientists cannot be dismissed as just "spending" that we "can't afford." It is confirmation of Schultz's dead-on conclusion that investment in human capital is the most productive use of its resources that a government can make.

W.K.

New Bubble Trouble Wave Amongst US Banks

Just when the optimistic pipe-smoking prophets had ensured us that the worst was already behind *The Wall Street Journal* (20/08, "In New Phase of Crisis, Securities Sink Banks" by Robin Sidel) pours a new load of bank grief on our heads: "US banks have been dying at the fastest rate since 1992, mainly because of bad loans they made. Now the banking crisis is entering a new stage, as lenders succumb to large amounts of toxic loans and securities they bought from other banks.

"Federal officials on Thursday were poised to seize Guaranty Financial Group Inc. in what could be the 10th-largest failure in US history, and broker a sale of the Texas bank to Banco Bilbao Vizcaya Argentaria SA of Spain. Guaranty's woes were caused by its investment portfolio, stuffed with deteriorating securities created from pools of mortgages originated by some of the nation's worst lenders.

"Guaranty owns roughly $3.5 billion of securities backed by adjustable-rate mortgages, with two-thirds of the loans in foreclosure-wracked California, Florida and Arizona, according to the country's latest report. Delinquency rates on the holdings have soared as high as 40%, forcing write-downs last month that consumed all of the bank's capital.

"Guaranty is one of thousands of banks that invested in such securities, which were often highly rated but ultimately hinged on the health of the mortgage industry and financial institutions. 'Under most scenarios they were good and prudent investments – as long as we didn't have a housing or banking crisis,' says John Stein, president and chief operating officer at FSI Group LLC, a Cincinnati company that invests in financial institutions.

"The specter of a systemic collapse in the US banking system has faded, largely because the government has shored up the industry with $250 billion in taxpayer-funded capital since last fall, most of it going to big banks. But more than 20% of all banks reported a net loss in the first quarter, the latest period for which the Federal Deposit Insurance Corp. has figures, and problems are now building up in small and medium institutions. Mortgage delinquency rates and losses or credit card problems are at all-time highs. The accumulating bad assets and needs for capital means that few banks are lending aggressively, creating a drag on the economic recovery.

"Many analysts and bankers are increasingly worried that the boomerang effect that killed Guaranty will cripple many small and regional banks already weakened by losses on home mortgages, credit cards, commercial real-estate and other assets imperiled by the recession.

"'There is no question but that these securities will be for some of these banks the straw that breaks the camel's back,' says Cassandra Toroian, founder and chief investment officer of Bell Rock Capital LLC in Rehoboth Beach, Del., which manages money financial services companies and funds for wealthy individuals.

"Thousands of banks and thrifts scooped up securities tied to the housing market or other financial institutions in the past decade. Such investments were alluring because they seemed certain to outperform Treasury bonds, municipal bonds and other humdrum holdings that dominated the securities at most banks for generations."

The Difference Between a Bubble and an Investment

"As of March 31, the 8,246 financial institutions backed by the FDIC held $2.21 trillion in securities – or 16% of their total assets of $13.54 trillion.

"The problems also underscore how the boom in securitization of loans instilled a belief that risks could be controlled, an idea embraced first by financial giants like Citigroup Inc. and Merrill Lynch & Co. and then by smaller institutions reaching for higher profits.

"'We saw them as a safe investment, and now we wish we didn't have them' says Robert R. Hill Jr., chief executive of SCBT Financial Corp.'s Columbus, SC, bank with 49 branches. The bank has less exposure than some other small institutions, with the crippled securities representing about 10% of its investment portfolio.

"The overall impact on the US banking industry's second quarter results isn't clear, because disclosure of losses and even the types of securities owned vary widely from bank to bank. Some obscure their troubled holdings in a vague line item titled 'other' in financial statements.

"'The depth of the problem is very difficult for us to get our hands on,' says Jim Reber, president of the ICBA Securities, the brokerage unit of the ICBA Securities, the brokerage unit of the Independent Community Bankers of America, a trade group of 5,000 small banks and thrifts. 'These securities have declined in value, and it is not clear when they are going to come back in value, if at all.'

"Last month, dozens of small and regional banks were bruised by a deterioration in their securities in their securities portfolios. Riverview Bancorp, of Vancouver, Wash., eked out a $343,000 profit, but the 18-branch bank took a $258,000 charge on a pool of securities it holds.

"The sickened securities fall into two categories. Guaranty is among nearly 1,400 banks that own mortgage-backed securities that aren't backed by government-related entities such as Fannie Mae and Freddie Mac. Such 'private issuer' and 'private label' securities are carved out of loans originated by mortgage companies, packaged by Wall Street firms and sold to investors.

"During the buoyant housing market, many of those securities earned top-notch grades from major rating agencies, giving bank CEOs, finance chiefs and treasurers comfort. 'A lot of community banks are located in communities located in communities that weren't growing, and there wasn't a lot of [local] loan opportunity. They needed some place to invest their money,' says J. Stephen Skaggs, president of the Bank Advisory Group LLC in Austin, Texas. So, they snapped up securities.

"Small and regional financial institutions own about $37.2 billion of private-issuer and private-label securities, Red Pine estimates. But regulators are pressuring banks to write down the value of their mortgager-backed securities.

"Banks also are being battered by more than $50 billion of trust preferred securities, financial instruments that are a hybrid between debt and equity. From 2000 to 2008, more than 1,500 small and regional banks issued trust preferred securities, according to Red River data.

"In a process similar to the securitization of subprime mortgages, Wall Street brokerage firms bought the securities from individual banks and packaged them into so-called collateralized-debt obligations. The banks then sold of the CDOs to investors, marketing them as lucrative but low-risk.

"But as banks struggle with rising loan losses, some issuers of trust-preferred securities no longer can afford their obligations. In the first half of 2009, 119 US banks deferred dividend payments on their trust-preferred securities, while 26 defaulted on the securities.

"The consequences are cascading down to banks that bought the securities. One banking lawyer who asked not to be identified it as 'a wonderful chain of stupidity.'

"'A lot of these banks had no business buying this stuff,' said Ms. Toroian, a former bank analyst. 'These are banks that survived the Great Depression, and now they can't survive this financial crisis because they made some bad mistakes in their investment portfolios.'

"Guaranty's push into mortgage-backed securities underscores how easy it was for regional and small banks to double down on their real-estate bets when times were good.

"Founded in 1938 as Guaranty Building & Loan in Galveston, near the Gulf of Mexico, the institution had swelled to billion in assets and about 30 branches when the Texas real-estate bubble burst. In 1988, regulators declared Guaranty and more than 100 other savings and loans insolvent.

"Guaranty was brought back from the dead by Temple-Inland Inc., a conglomerate that owned timberland, paper mills, as railroad and a small mortgage company. With government help, that company brought the S&L and two other failed Texas thrifts into a new thrift twice as big.

"By 2005 Guaranty had $18 billion in assets and 150 branches in Texas and California. That year Guaranty bought nearly $3 billion of triple-A-rated mortgage-backed securities, according to company filings. Its holdings ballooned to $3.2 billion from $420 million as year earlier.

"A Guaranty spokesman refused to com-

Depression *from page 5*

ence when the 'political center' gets patched together by politicians and financiers.

"That leaves borrowers like Jonathan Gerhardt, 46, little choice but to pay. He is a cellist. The child of two classical musicians in Columbus, Ohio, he studied at the New England Conservatory of Music, performed with two city orchestras and finally won a spot as principal cellist of the Louisiana Philharmonic Orchestra in New Orleans. Despite climbing so high in the field, he was earning just $20,000 a year three years ago, including pay for teaching cello at Tulane University. He buckled under his $100,000 in student loans and filed for bankruptcy.

"Lawyers for the Education Department and a guarantee agency that held some of the loans could trim his expenses, such as $23.92 for Internet access and $4,851 for a gym membership. They also suggested he get rid of his cat to save $20 a month."

Politics of Compromise Leave Little Room for Social Sensitivities

"Bankruptcy Judge Jerry A. Brown, however, said Mr. Gerhardt had to work out to relieve back pain from playing the cello, and needed the Internet to look for extra work. 'Expenses related to his cat are not luxuries, considering he is single and lives alone' the judge wrote. He ruled that repaying the loans would be 'an undue hardship' and expunged it.

"The Education Department appealed. A federal appellate court sided with the government. It suggested Mr. Gerhardt find a job as a music-store clerk.

"That sure put the muses in their place.

"Mr. Gerhardt says he is already working 60 hours a week, including rehearsals with the Louisiana Philharmonic, practicing and teaching. He recently moved into an apartment with a roommate, saving $50 a month in rent. He says he stopped taking annual trips to Ohio to visit his 51-year-old mother, and doesn't believe he will ever be able to support a family or afford a house. Mr. Gerhardt is now paying $200 a month towards his loan. The government wants $900.

The great insights of Theodore Schultz have been buried not by gentle shelf-dust, but by dirt and rubble loaded as though by an earth-mover. Capital budgeting even when brought in on physical investments of government under President Clinton were sedulously hidden not to upset Wall St. But even Schultz's perceptions on the unique productivity of human capital failed to raise the importance of its cultural heritage to a society's functioning. And that, however, was very evident in the cases of Germany and Japan whose rapid recuperation as trading and cultured nations they owed to the fact that their huge investments in human capital had come out of the war relatively intact."

It was without doubt the most important lesson to have come out of the Second World War. It is the missing piece of repressed history that, more than any other, would allow this wounded planet to heal and function once more.

William Krehm

ment. 'Under pressure from shareholders such as billionaire Carl Icahn, Temple-Inland spun off Guaranty in 2007. The housing market was sliding, but Guaranty didn't waver from its self-confidence. While the deterioration in the housing and credit markets is clearly significant, and could continue, it is important to note that we did not originate or purchase subprime loans, we have very few 2000 and 2007 vintage single-vintage single-family mortgage loans. We buy straightforward structured mortgages, and lending to home builders is a long-term core competency for us,' said Guaranty President and CEO Kenneth R. Dubuque. Mr. Dubuque stepped down from Guaranty in November and couldn't be reached for comment.

"Delinquency rates in Guaranty's portfolio jumped to as much as 40% last fall from a range of 4%, to 22% in 2007. Last month, banking regulators forced the company to write down the mortgage-backed securities by $1.45 billion, or more than a third of their value in November.

"The write-downs plunged Guaranty's total risk-based capital ratio, or more than a third of their value in November."

There are other veins of fiction in banks' supposed lines of credit even when the security is abundantly in the investor's account but that at the crucial moment is not there when a buying opportunity present itself.

We will probably return to the matter in our next issue.

W.K.

Boeing's Nightmare of Building Its Dreamliner by Farming Out Assignments to Different Lands Nipped by Its Own Financial Troubles

The Wall Street Journal (10/7, "Boeing Settles In for a Bumpy Ride" by Peter Saunders) recounts a bumpy tale: "Coming on the heels of troubles in its 787 Dreamliner program, Boeing Co. said it would record a $1 billion charge on its 747-8 jet and delayed the jumbo plane's first flight until early next year.

"Tuesday's moves come as the company tries to get both the revamped 747 and the Dreamliner programs on track after lengthy delays that have damaged Boeing's credibility.

"Long at the vanguard of American engineering, Boeing hoped that its new, all-composite Dreamliner aircraft would revolutionize its manufacturing process and further cement its solid reputation. But the program's repeated delays indicate how difficult it can be to get big engineering and manufacturing efforts in line once they go awry.

"A similar situation seems to be in play with the 747-8, even though it uses traditional materials instead of composite ones and employs a more orthodox manufacturing process.

"Since much of Boeing's engineering expertise has been shuttled between the two programs in the past few years, Boeing has been stretched thin as it tries to fix two major programs simultaneously while massaging customer relationships.

"Scott Carson, chief executive of the commercial-airplanes unit since 2006, stepped down September 1 and was succeeded by James Albaugh, who had run the company's defense business. Mr. Albaugh followed a migration of defense-unit executives to the commercial-airplanes division to help fix the Dreamliner and 747-8 programs.

"Jim McNerney, Boeing's chairman and chief executive, has been under pressure from shareholders and dozens of customers to fix the problems, which have wounded Boeing's reputation for building and delivering airplanes.

"A Boeing spokesman said the company is 'disappointed in the combination of execution challenges and recession-based market pressures that have resulted in this charge to the 747-8 program. New airplane programs are immensely challenging, and we are, in fact, making progress on both the 787 and 747-8.'

"At the same time, the delays for both aircraft provide a buffer for customers hoping that economic conditions improve before they have to make hefty payments for delivery of new jets.

"Luxembourg's Cargolux Airlines International SA, the launch customer for the cargo version of the 747-8, says it still plans to take delivery of the 13 aircraft it ordered. Deutsche Lufthansa AG said it still plans to add a passenger version of the 747-8 to its fleet in 2011."

Building New Generation of Giant Airliners During an Economic Meltdown

"The new third-quarter write-down comes on top of a previously announced $2.5 billion non-cash charge for costs associated with development and production of the first six Dreamliner test aircraft.

"Chicago-based Boeing said the combined 747-8 and Dreamliner charges of about $3.5 billion will be the most it has ever recorded in a single quarter.

"Investor reaction was muted, with Boeing shares up a penny to $52.29 in 4 pm composite trading on the New York Stock Exchange.

"The 747-8 – which essentially will be a stretched version of the venerable 747 with a new wing, new engines and new cockpit technologies – has been beset by design and engineering problems since its development was announced in 2005. The plane is now scheduled to be delivered during 2010's fourth quarter, a year behind schedule.

"Boeing said about $640 million of the latest charge relates to higher production costs at the company's Everett, Wash., factory and at its global suppliers. The resulting excess costs of $360 million is related to the company's decision to keep the plane's production rate at a sparse 1.5 aircraft a month until 2013. The company then plans to build two a month on the assumption that demand will have increased by that time."

Much of the future of such planes and other large high technology items to emerge in tolerable shape depends on the economy as a whole having recovered. Failing that there could be trouble ahead that will make the companies sigh for the time when their trouble was most of an engineering and a production nature.

"Boeing is launching the cargo version of the 747-8 during a deep slump in freight traffic. Still, Boeing has found customers for the massive freighter. But sales of a passenger version haven't gotten off the ground. Only Lufthansa has purchased that version."

A second article in the same issue is entitled "Dreamliner Production Gets Closer

Continued on page 20

World to America: We Want Our Gold Back

It is not just China that is attacking the Anglo-Saxon financial system.

The world is preparing to abandon the US dollar and the UK pound. Pronouncements from Hong Kong, the United Arab Emirates, Switzerland and Germany have made clear that the Anglo-Saxon financial system's doom is only a matter of time.

A huge announcement out of Hong Kong rattled the financial world on September 3. Although big media relegated the story to the back pages, it should have been front and center! What's the news? China is demanding its gold back.

"Hong Kong is pulling *all its physical gold holdings* from depositories in London," reported MarketWatch (www.marketwatch.com/story/hong-kong-recalls-gold-reserves-from-london-2009-09-03) (emphasis mine throughout).

The announcement, coming in the midst of the global economic crisis, is sending a clear signal: Britain is in far worse economic shape than generally realized, and China thinks it needs to get its gold out while it can – before something happens to it. Gold closed at a new record high (www.latimes.com/business/la-fi-gold12-2009sep12,0,2529261.story) of $1,006 per ounce on Friday.

Governments have a notorious history of confiscating precious metal reserves during times of crisis – even in America. In 1933, in order to stabilize the monetary system, President Franklin D. Roosevelt issued an executive order confiscating all privately owned gold (www.blanchardonline.com/beru/confiscation_again.php) in the United States. Later, in 1968, President Johnson issued a proclamation that all Federal Reserve Silver Certificates were merely fiat legal tender and could not be redeemed in silver. Then in 1971, the US government closed the gold window completely and declared that foreign nations would no longer be allowed to exchange US dollars for the gold that was supposedly backing them.

But China's decision to demand its gold back is more than just a vote of no-confidence against the pound. It is a direct challenge to the whole global Anglo-Saxon-dominated financial system. China wants its own gold bullion money center. Toward this end, it also announced that it has created bullion storage facilities in Hong Kong to compete with London and New York. Chinese officials said they will soon launch a marketing drive to convince Asian central banks to transfer their gold reserves from overseas money centers to a storage complex closer to home in Hong Kong.

In today's world of fiat paper currencies, many have forgotten the golden rule: *He who has the gold rules.* Beijing hasn't forgotten – it has just been playing along.

China Knows that US Too Can Print Money

The Chinese administration is not against fiat currencies in principle. It too relishes the ability to print fiat money. It loves the power it gives it to essentially confiscate the wealth of the country's tax base. However, China also knows that the United States and Britain can print money too.

America and Britain owe China and other countries trillions of dollars. As long as Washington and London did not overtly abuse the ability to create money, Beijing was happy to keep lending. But with the global financial situation still teetering on the precipice, both Britain and the US have publicly admitted to "quantitative easing" (the technical term for creating new money out of thin air) to intervene in the bond market and pay back borrowed money. The dollar is at risk of a major devaluation – and China knows it.

Once countries start down the funny-money road, confidence deteriorates rapidly. How valuable is that $100 bill when the government is creating hundreds of billions to give to big banks? It is often a short trip to the paper currency recycle bin. At that point, you have a free-for-all. Once it gets ugly, nations will go to extremes to avert economic collapse.

Thus, China wants its gold. As much as possible, as soon as possible, before the world's monetary system falls apart. On September 6, Ambrose Evans-Pritchard reported in the *Telegraph* his conversations with Cheng Siwei, former vice chairman of the Chinese Communist Party Standing Committee. According to Evans-Pritchard, Cheng, who now acts as sort of an unofficial economic ambassador to the world, says that China is alarmed by US money printing (www.telegraph.co.uk/finance/economics/6146957/China-alarmed-by-US-money-printing.html).

Cheng stated on the record that *China has lost confidence in the US dollar* and is moving toward *a partial gold standard* through reserve accumulation. "The US spends tomorrow's money today," he said. "We Chinese spend today's money tomorrow. That's why we have this financial crisis."

"If they keep printing money to buy bonds it will lead to inflation, and *after a year or two the dollar will fall hard.* Most of our foreign reserves are in US bonds, and this is very difficult to change, so we will diversify," he said. "Gold is definitely an alternative, but when we buy, the price goes up. We have to do it carefully so as not to stimulate the markets."

But China doesn't seem too overly concerned about the price – it just wants the gold. The Chinese government has even unleashed an advertising campaign (www.mineweb.co.za/mineweb/view/mineweb/en/page33?oid=88452&sn=Detail) through its state-run media to encourage people to purchase gold and silver as a way to invest and protect their wealth. The theme seems to be: Get as much gold into the country as possible before the crash comes. Other nations are grabbing their gold and heading for the exits too (www.commodityonline.com/news/Dubai-to-get-back-gold-reserves-from-London-banks-18124-3-1.html).

A few months ago, the United Arab Emirates announced that it had begun constructing a major gold storage facility that would be marketed to members of the Gulf Cooperation Council. The UAE said it had requested its gold currently stored by the London Bullion Market Association to be sent home.

Bob Chapman's (www.globalresearch.ca/index.php?context=va&aid=15126) *International Forecaster* reports that Germany stores significant portions of its gold with the US government. He says that Germany has asked that its gold stored in the US be transferred back home. Economic analyst Jim Willie (www.321gold.com/editorials/willie/willie091109.html) also mentions unconfirmed reports that Germany has requested that its gold be sent back.

Even Switzerland has threatened to remove its gold (www.reuters.com/article/rbssFinancialServicesAndRealEstateNews/idUSTHO15017420090221) from custodial accounts in the US Reuters reported in February that the populist Swiss National Party (Switzerland's largest political party) said that if Washington decided to go ahead and force Swiss Banking Giant UBS to divulge names of its banking clients that Switzerland should, among other things, *pull all of its national gold reserves* from America. America has since pressed ahead with its case. In August, UBS said it would release approximately 10,000 client names.

Everywhere you look, big events are occurring in the global economy. Last week, the United Nations said that the *dollar's unique role as a global currency was at an end*. Although China, Brazil, Russia and India have all called for a new economic system not based on the dollar, this is the first time that a multinational institution (www.telegraph.co.uk/finance/currency/6152204/UN-wants-new-global-currency-to-replace-dollar.html) has suggested scrapping the greenback. Also last week, the US administration was forced to ask Congress to raise the debt ceiling again (www.reuters.com/article/newsOne/idUSTRE52H2CY20090318) – this time to over $12 trillion – a level that will be breached by October. On Friday, three more banks failed in the US, bringing the total to 92 this year. The Federal Deposit Insurance Corp. recently increased the number of problem banks on its watch list to 400 – up from around 300 during the first quarter of the year. In Britain, last week, the World Economic Forum listed Britain's economy as less stable than Peru's (www.telegraph.co.uk/finance/economics/6157759/Britains-economy-less-stable-than-Peru.html).

The world is awaking to the possibility that America and Britain face real collapse. The part that stings the worst is that one can't blame them for getting their gold while they can. They are right – the facts indicate America's and Britain's economies are going down. It is just a question of time.

To find out the most fundamental reason for Anglo-America's decline read: The United States and Britain in Prophecy (www.thetrumpet.com/index.php?page=book&q598.6.0.0).

Robert Morley

Fed's Bernanke Tip-toes Around What Worked in Past to Keep Those Responsible for the Current Crisis in the Saddle

The New York Times (2/10, "After Criticism of Fed's Role, Bernanke Supports Creation of a Group of Regulators" by Edmund L. Andrews) reports: "Washington – The chairman of the Federal Reserve Ben S. Bernanke, told skeptical lawmakers on Thursday that the Fed should be put in charge of regulating the nation's biggest financial institutions.

"But in a nod to critics who have expressed alarm about the Fed's immense power during the financial crisis, Mr. Bernanke said responsibility for monitoring broader risks in the financial system should go to a council of regulators.

"'We have never supported, and the administration has never supported, a situation in which the Fed would be some kind of untrammeled super-regulator,' he told members of the House Financial Services Committee.

"Mr. Bernanke said the Fed would be merely one of several players on the new council, and he endorsed the Obama administration's proposal to have the Treasury lead that council.

"But while most lawmakers have praised the Fed's aggressive efforts to tame the crisis, others have attacked it for failing to prevent the problems in the first place and then amassing too much unchecked power in bailing out the financial industry.

"As a result, some of the Fed's supporters in Congress predict that the agency's role will be more modest than they originally thought.

"Representative Spencer Bachus of Alabama, the senior Republican on the committee said Republicans would prefer to strip the Fed of all its regulatory powers and leave it just with its core role of setting monetary policy.

"'The Federal Reserve offered few warnings of the forces undermining the foundations of our markets,' Mr. Bachus said on Thursday. 'What has changed that should make us believe the Fed will be up to the task in the future that it so manifestly could not handle in the past?'

"President Obama's proposal would put the Fed squarely in charge of complex financial institutions – probably about 20 major bank holding companies and a few other giant institutions – that could jeopardize the financial system if they failed.

"Mr. Bernanke called for imposing higher capital requirements, not just to provide more cushion against possible losses but also to penalize companies for becoming too big to fail.

"'Enhanced requirements are needed not only to protect the stability of individual institutions and the financial system as a whole, but also to reduce the incentives for financial firms to become very large in order to be perceived as too big to fail,' he told lawmakers.

"Mr. Bernanke said that giant financial players might be forced to adopt 'contingent' capital – selling bonds that would automatically convert into common stock if a company had trouble.

"The idea of contingent capital has been gaining popularity within the Fed; officials content that it would expose bondholders to more risk and therefore make them more reluctant to let giant banks finance their growth with debt.

"As a practical matter, most government bailouts have wiped out ordinary shareholders while partly or entirely rescuing bondholders and other creditors.

"Mr. Bernanke carefully stayed out of the battle to create a new consumer financial protection agency. That proposal would strip the Fed of its authority to regulate deceptive practices in consumer lending, an idea that Fed officials bristle at privately but do not oppose publicly.

"Mr. Bernanke conceded that the central bank had failed to prevent the explosion of no-document mortgages and other exotic practices at the heart of the mortgage bust, though he said the Fed was 'competent' at protecting consumers and had adopted tougher rules in recent years.

"Mr. Bernanke also said the Fed would gladly support another part of the regulatory overhaul that would reduce its power to bail out financial institutions in the event of 'unusual and exigent circumstances.'

"If Congress gave the government new power to shut down troubled giants, Mr. Bernanke said, he would be happy to give up the power to bail them out. 'No one is more sick of bailouts than I am,' he said."

But not sick enough of that sport to go back to the very recent history of the 1996 for a case where it worked wondrously fast for the Clinton regime to avoid the international collapse of the banking system, by introducing accrual or double-entry accountancy with respect to the US government's physical capital investments that had been written off up to then as current expenses. That meant that while the government debt incurred for such investments was carefully "amortized" in accordance with a set schedule, value of the actual investment was "depreciated" in a single year and then carried at a token dollar. Obviously that presented as lot of government debt – in addition with the money supply that is only federal debt – that is not really there. That averted the collapse of the economic system.

A crusading order had brought back such "accrual accountancy" to central and Western Europe a thousand years ago. But it still has not been brought in for the human investment of the US and Canadian governments. Working on the figures created by the introduction of accrual accountancy for physical investments of the US government, which was completed by 1996, a highly conservative calculation of the ignored capital assets of the US federal government would amount to some $3.6 trillion US dollars in the US and taking the usual rough proportion of one to ten in calculating the relative value of similar rebootings of such global statistics between the two countries, that would give us in Canada some $360 billion dollars. That would be enough to build schools and public housing, and look to protecting the environment by putting to use the still unacknowledged prepaid human capital that is still ignored.

The question then is: why is that great secret never mentioned today – neither in Parliament or Congress or in economic courses in our universities.

It is *verboten.*

William Krehm

Boeing *from page 17*

Monitoring" by Daniel Michaels Michaels and Peter Sanders: "Everett, Washington – To get the troubled 787 Dreamliner back on track after more than two years of delays, officials at Boeing Co. are counting on interpreters who can handle 28 languages, earthquake detectors and high resolution video cameras.

"The features are core to a major overhaul of production methods that Boeing hopes will tighten control, provide more information and speed work in its belated effort to get the Dreamliner off the ground. The US aerospace giant is playing catch-up because it overreached six years ago, when it set out to make the world's most high-tech passenger jet but didn't prepare sufficiently for the project's complexity.

"At the time, Boeing took the unprecedented step of outsourcing most of the Dreamliner's manufacturing. Boeing had previously designed and built its own planes in-house, bearing the whole expense. But early this decade, when air traffic plunged after September 11 terrorist attacks, top Boeing executives balked at investing more than $10 billion to develop a new plane.

"Instead, suppliers would independently bankroll their parts of the project, sharing costs and risk. Investors like the idea, lifting Boeing's stock price from a low around $31 per share in August 2003 to a high above $107 in July 2007."

There was, it seemed a stroke of market luck, inspired by involving suppliers in the financing and other risks.

"But when factory workers here started assembling the first Dreamliner around the time the stock hit its high, the system's flaws became clear as quality suffered and major components weren't completed. Many suppliers were accustomed only to manufacturing from blueprints supplied by Boeing – they weren't ready to manage sub-contractors or get designs approved by safety authorities. Others couldn't increase production fast enough. Boeing which had earlier culled its own engineers to cut costs, was stretched too thin to monitor and fix blunders.

"In recent months Boeing has been trying to draw a line under the Dreamliner's problems by improving communication, taking major production lines back in-house and adding engineers to oversee work.

"The Dreamliner's first test flight, which Boeing abruptly canceled in June because of a technical problem, is now scheduled for year's end. The first delivery, to Japan's All-Nippon Airways Co. is promised in the fourth quarter of next year.

"Vital to Boeing's plan for keeping the 787 on track as it starts building the 850 planes on order is a space center-style control room – officially called the Production Integration Center.

"One of the hub's wide glass walls overlooks the Dreamliner final assembly line, where the plane's body and wings come together. On the opposite wall, 24 big screens display information including overseas shipments of parts, urgent technical questions and even earthquakes around the globe, which could misalign factory equipment and cause delays.

"Suppliers as far afield as Australia, Italy, Japan and Russia can call through translators and show Boeing engineers in the components using high-definition handheld video cameras.

"Robert Noble, Boeing's vice president of supplier management who runs the 24-hour center, says immediate, multimedia communications have eliminated the problem of often unclear email exchanges between distant engineers who work on opposite ends of the clock. 'That takes days out of problem resolution,' he says.

"Still Boeing's problems with the Dreamliner have had widespread repercussions.

"Suppliers are suffering financially because of the delays and many are hesitant to invest heavily again. This could cause problems for Boeing in the coming months as it attempts to negotiate with suppliers to increase production output.

"Meantime, both Boeing and rival Airbus, which has faced similar development problems on its A380 superjumbo, are slowing jetliner development work significantly, to avoid additional hasty mistakes. That means new models are likely to hit the market more slowly than the industry had predicted.

"As Boeing grapples with its extended supply chain, it is also taking part of the program back in-house. In March 2008, Boeing bought Vought Aircraft Industries Inc.'s 50% stake in Global Aeronautica, a joint venture with Italy's Alenia Aeronautica SpA to assemble fuselage sections in Charleston, SC. Terms weren't disclosed. Then, this July, Boeing bought Vought's own Charleston factory, which makes the 787's rear fuselage sections.

"Boeing says it recently added additional project engineers, who were brought from other divisions of the company and will be responsible for specific parts being produced by Airbus, a unit of European Aeronautic Defence & Space Co.

"Francois Bertrand, chief executive of French aerospace supplier Groupe Latecoere SA, says his company invested €200 million ($294.9 million US) to develop components for both planes and secure long-term positions on the marquee projects. But with returns on the two investments lagging, Latecoere late last year had to renegotiate bank debts to gain financial breathing room."

W.K.