THE JOURNAL OF THE COMMITTEE ON MONETARY AND ECONOMIC REFORM

COMER

$3.95 Vol. 21, No. 10 • OCTOBER 2009

CONTENTS

2 Bailed-out Banks Settling Accounts with the Nation?
3 Canadian Land is Starting to Shine as an Investment
4 Meltdown for Dummies, or How to Make a Hit at Your Next Cocktail Party
6 Three Potent Steps to a Sane Economy
7 Report of a COMER Study Class in Colorado
10 Could Capitalism have Survived Without the Chinese Revolution?
11 Obama Hip-deep in Potholes
13 New Bubble Trouble Wave Amongst US Banks
14 Cash for Clunkers
15 Have You Wondered?
16 Some Highly Relevant Points about Elementary Education
17 Vive the "Dominant Revenue"
18 Number-crunching as Opposed to Analysis
18 Letter to the Editor
19 Cross-currents in Deep Offshore Oil Finds
20 BRIC — Hitting the Head or the Wall?

Are New Social Patterns Taking Over from Marriage to the Distribution of Seats in Congress?

The National Post (3/08, "More older couples preferring to live common-law than marry" informs us: "Census figures show large increases in the number of people over 50 in common-law unions, with the most significant growth in the early-sixties crowd. At the same time, the practice of marriage has nearly flatlined or even declined among the twenty- and thirty-somethings. Experts say that as a result of more liberal social attitudes, a 'been there, done that' mentality among those who have been divorced and the lack of financial incentive to marry, many older Canadians simply do not feel the need to walk down the aisle. Between 2001 and 2006, the most recent year for which census data are available, the number of Canadians in common-law relationships shot up 77% among those aged 60 to 64, and between 44% and 64% for all other age groups over 50" (Canadian News Service).

But to stop there would be simplifying a change in society's basic structures that manifests itself for a variety of reasons. Higher education standards for women, with the resulting increase in their earning powers, and strengthening their critical powers and independence. It has more to do with the changing structures of our societies than the romantic or unromantic attachment between individuals.

That shake-up in our personal relationship and ways in which we relate to other individuals is affecting their groupings in congresses and parliaments as well as in marriage. *The Wall Street Journal* (25/08) shovels up the evidence of that in parallel trends in the US congress and in society at large.

"The federal government has hired tens of thousands of temporary workers to prepare for the 2010 census – a population count that could remake the political map even as the foreclosure crisis makes it more difficult to account for millions of dislocated Americans.

"Early analysis indicates that Texas will likely be the biggest winner since the prior count a decade ago, picking up three or four seats in the US House of Representatives, according to the National Conference of State Legislatures and Election Data Services Inc., a political consulting firm. Other states poised to gain at least one seat include Arizona, Nevada, Georgia, Florida and Utah.

"Growth in these states is driven by factors including migration from other states, immigration and birth rates. The economic crisis has put the brakes on some of this expansion – Florida has just reported its first year of population decline since 1948 – but in general, Sun Belt states have grown faster than other states over the past decades.

"Since the number of seats in the House is capped at 435, the gains in the South and the West have to be offset by losses elsewhere. And that, of course, ensures a certain mobility evident as well as that in the less-permanent relationships of mature Canadian couples.

"New York, New Jersey and Massachusetts and the recession-battered states of Michigan, Ohio and Pennsylvania each stand to lose a House seat. So does Louisiana, where population still hasn't rebounded from Hurricane Katrina in 2005, which replaced so many residents that census takers face a difficult task in tallying them all.

"A state's votes in Congress is less clear, said Karl Eschbach, the Texas state demog-

Continued on page 16

COMER

FOUNDING EDITOR
John Hotson 1930–1996

PUBLISHER–EDITOR
William Krehm
(comerpub@rogers.com)

CARTOONIST
Allen Good

INFORMATION SECRETARY
Herb Wiseman (herbwise@cogeco.ca)

WEBMASTER
John Riddell

Economic Reform (ER)
(ISSN 1187–080X) is published monthly by COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, Ontario M4M 2S6 Canada
Tel: 416-466-2642, Fax: 416-466-5827
Email: comerpub@rogers.com
Website: www.comer.org

COMER Membership: Annual dues (includes *ER* on request plus 1 book or video of your choice): CDN$50

***Economic Reform* Subscription only:**
One year, 12 monthly issues, in Canada CDN$30, Foreign CDN$40

Send request and payment to:
COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, ON M4M 2S6

***ER* Back Issues:** CDN/US$4, includes postage; additional copies same issue, $2; additional issue same order, $3. Send requests for back issues to Herb Wiseman, 56 Robinson Street, Peterborough ON K9H 1E8.

Copyright © 2009
COMER Publications
All rights reserved

Permission to reproduce is granted if accompanied by:
"Copyright © 2009 COMER Publications. Reproduced by permission of COMER Publications"

Publications Mail Agreement 41796016.

Postmaster, please send address corrections to:
COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, Ontario M4M 2S6

LAYOUT
Tony Koch (comer@pagecraft.org)
Pagecraft Computer Services

PRINTING AND DISTRIBUTION
Watt Solutions Inc., London

Printed in Canada on recycled paper.

Bailed-out Banks Settling Accounts with the Nation?

The way the question is posed in *The Financial Post* (September 1, taken from *The New York Times*) short-changes the question and hence the answer as well. More than just the dollars and cents lent out to save banks or their depositors from bankruptcy, are the lives that have been ruined, families broken up, schooling interrupted – damage that will not be made good even when the dollars and cents that went missing are repaid. Moreover, nothing is repaired in a lasting way so long as the lessons of the financial crash are not brought into the light of day and the lessons that must be drawn from them are not incorporated into the statecraft of the nation.

With that brief reminder of what we are or should be talking about, let us proceed to update of the official record as reported in the *Post:* "Bailed-out US banks paying off for taxpayers US $4 billion profit" by Zachary Kouwe.

"Nearly a year after the United States began rescuing that nation's biggest banks, the US taxpayers have begun seeing profits from the hundreds of billions of dollars in aid that many critics thought might never be seen again.

"The profits, collected from eight of the biggest banks that have fully repaid their obligations to the government, come to about US $4 billion, or the equivalent of about 15% annually, according to calculations compiled for *The New York Times.*

"That does not include the roughly US $35 million the government has earned from 14 smaller banks that have paid back their loans. These early returns are by no means a full accounting for the huge financial rescue undertaken by the US government last year to stabilize teetering banks and other companies.

"The US government still faces potentially huge long-term losses from its bailouts of insurance American International Group, mortgage companies Fannie Mae and Freddie Mac, and automakers General Motors Co., and Chrysler LLC. The Treasury Company could also take a hit from its guarantees of billions of dollars of toxic mortgages.

"But the mere hint of bailout profits for the nearly year-old Troubled Asset Relief Program has been received as a welcome surprise. It has also spurred hopes that the US government could soon get out of the banking business.

"'The taxpayers want their money back, and they want the government out of their banking system,' Rep. Mac Thornberry (R-Texas), a member of the Congressional over-sight-panel examining TARP, said in an interview.

"Profits were hardly high on the list of US government priorities last October, when a financial panic was in full swing and the Treasury Department started spending roughly US$240 billion to buy preferred shares from hundreds of banks that were facing huge potential losses from troubled mortgages. Bank stocks began teetering after Lehman Brothers Holdings Inc. collapsed and the government rescued AIG, and fear gripped the financial industry around the world.

"US taxpayers were told they would eventually make a modest return from these investments, including a 5% quarterly dividend on the banks' preferred shares and warrants to buy stock in the banks at a set price over 10 years.

"But critics at the time warned that taxpayers ought not to see any profits until then and in fact could lose much of their investment if the assets they were buying turned out worthless over time.

"As Congress debated the bailout bill last September that would authorize the Treasury Department to spend up to $700 billion to stem the financial crisis, Rep. Mac Thornberry (R-Texas) said: 'Seven hundred billion of taxpayer money should not be used as a hopeless experiment.'

"So far that experiment is paying off. The government has taken profits of about $1.4 billion on its investment in Goldman Sachs, US $1.3 billion on Morgan Stanley and US $414 million on American Express. The other five banks that repaid the government – Northern Trust, Bank of New York Mellon, State Street, US Bancorp and BB&T – each brought in between US$100,000 million and US $334 million in profit.

"The US Government bought shares in these and many other financial companies last fall, when sinking confidence among investors pushed down many bank stocks to just a few dollars a share. As the banks strengthened and became profitable, the

government authorized them to pay back the preferred stock, which had been paying quarterly dividends since October."

The Bonanza of the Banks Buy-back of the Warrants Issued

"But the real profit came as banks were permitted to buy back the so-called warrants, whose low fixed price provided a windfall for the government as the firms' shares soared.

"The government is owed about US $6.2 billion in interest payments from banks that have not yet repaid their loans.

"But all the profits taxpayers won could still be wiped out by two deeply troubled institutions. Both Citigroup and Bank of America are still holding mortgages and other loans that were once worth billions of dollars but whose revised values are uncertain. If they prove 'toxic' because they cannot attract buyers, they could leave large holes in the banks' balance sheets.

"Neither bank is ready to repay its bailout money anytime soon, even though their stock prices have surged in the past month, leaving the government sitting on paper profits of about US $18 billion between them."

W.K.

Canadian Land is Starting to Shine as an Investment When Financial Instruments are Getting Ever More Iffy

The Globe and Mail (19/08, "Cheap Canadian farmland lures foreign buyers" by Steve Ladurantaye) informs us of a trend that invites some pondering: "The renowned cranberry harvest in southern Quebec has long attracted tourists to the picturesque region. But the cranberry bogs sprinkled throughout the countryside near Victoriaville attracted a different type of sightseer earlier this summer – a billion-dollar, US-based agriculture fund hungry for cheap Canadian farmland.

"Attracted by Canada's low political risk and fertile fields, Hancock Agricultural Investment Group, a Boston-based unit of Toronto's Manulife Financial Corp, decided its first Canadian purchase would be a 1,100-acre patch of land that it called 'one of the most highly productive properties in the industry.'

"The company will not disclose how much it paid, or even the exact location of the farm. But president Jeff Conrad said the company is in Canada to stay, and the fund plans to seek more land.

"'A lot of people get uncomfortable because they don't know us and they don't know how we operate,' he said. 'We aren't in this to flip properties, and we're not fast money. Our clients are long-term, institutional firms – pension-funds – and they have a place in their asset allocation for farmland.'

"According to a report by London-based Knight Franks LLP, Canadian farmers can expect a flurry of international interest in the coming months as investors bet that low commodity prices will rebound as the world struggles to meet its need for food. Canadian farmland is still cheap by global standards, but unlikely to stay that way for long.

"Large global funds are increasingly drawn to Canada and Australia as they seek agricultural investments, with a hectare of arable land worth about $1,725 (US) according to data collected at the beginning of the year, said Knight Frank's head of rural property research, Andrew Shirley. Comparable land in England goes for $17,000; in Australia, it's $3,450.

"While land can be purchased for less in developing countries, there are often complications that make ownership difficult.

"'Large investors want to buy in Canada because the government isn't going to come take your land away on a whim,' he said. 'There's also infrastructure, so once you've harvested your crops, there are good roads to get to market. If your combine breaks, someone can fix it. This is an attractive proposition."

"There is a gigantic asterisk beside the $4,725 figure for Canadian land. Foreign ownership is restricted in the Prairies and, up until 2002, only residents of Saskatchewan could actually own land in the province. This has kept prices depressed and opened the door for Canadian-only funds to snap up assets at low prices.

"Agcapita Partners LP and Assiniboia Capital Corp. each operate funds that purchase large swaths of prairie land, with an initial investment averaging $10,000. Only Canadians may invest.

"Both point to the same data when pitching their products – farmland around the world has appreciated at a rate 2% higher than inflation since the 1950s. At a time when investors are looking at 50% losses on their stocks, it can be an attractive proposition.

"'When we started out five years ago, people thought we were nuts,' said Stephen Johnston, president of Agcapita, which has about $4,100 million under management. 'Canada has the lowest prices for land of any G8 country. This is real property that kicks off cash and isn't going anywhere.'

"The market could open up – Saskatchewan Agriculture Minister Bob Bjornerud has suggested he's open to changing the ownership rules to attract fresh capital to the Prairies. It's a conversation still in its infancy, but likely to get louder as aging farmers look to cash out and move on.

"In the meantime, large funds will continue to look to provinces like Ontario and Quebec for investments. There are no specific rules in those provinces, although the *Investment Canada Act* does contain a passage that allows the federal government to overrule a transaction it sees as a threat to the national interest.

"'As the agricultural industry continues to globalize and trade barriers continue to fall, we believe the US, Australia and Canada, and other large and efficient producers, stand to benefit,' said Hancock's Mr. Conrad. 'It's a big country, and most of the deals will still be between farmers. But that doesn't mean that there aren't opportunities for other players.'"

The argument could be somewhat reformulated to better emphasize the interest of the cultivators of the lands. In return for an inherited life style protected from the bustle of mega-urbanization, lower production costs for both city-dwellers and those who actually work the land could ensue.

W.K.

Thank you for your support!

Meltdown for Dummies, or How to Make a Hit at Your Next Cocktail Party

"The study of money, above all other fields of economics, is one in which complexity is used to disguise truth or to evade truth, not to reveal it." John Kenneth Galbraith.

The economy, it's the topic of the day – in barbershops, at cocktail parties and ad nauseam in the media. Politicians around the world are making excited noises about it. Ever wonder if any of these people really know what they're talking about? Take the cocktail party. Everybody seems to be listening to the CFP who is saying (like the Prime Minister) that there are some good buys to be made in the market turn-down. Attention swings to the plastic surgeon lamenting that he has "already lost a quarter of a million." Wouldn't it be great if you, yes, modest you, could drop a little crystal of clarification into this murk!

You might say, "Well to make sense of what's happening, you really need to know one or two simple things about the monetary system. Yes, I did say 'simple' things. For instance, let me tell you where money comes from." That should get their attention.

"You have seen TV commercials picturing an office in a bank with a bank official on one side of the desk and a customer, or a couple of customers on the other side. Keep that picture in mind, because that picture is the elemental scenario in the creation of 95% of our money supply. It has two essential elements – a bank willing to lend and a borrower (government, corporation or simple citizen) willing to borrow.

"When the bank official taps her computer, smiles and says, 'There, I have just put $25,000 in your account. You can pick up your new car today,' at that moment, $25,000 in new Canadian money has just popped into existence. They don't have some depositor's money in their vaults to give you, nor reserves of cash at the Bank of Canada – not since the Mulroney government phased out reserves in 1993. No, at that moment $25,000 (or if you're General Motors, $25 billion) in new money comes into existence. It's not cash. There is no cash involved. It's just credit, but so long as somebody trusts the bank to honour your cheques, it acts like cash. The borrower can sign it over to the car dealer, who can use it to pay his salesman's commission; the salesman can use it to buy his wife a bouquet or to bet on a horse, and so it continues on its unremarked and useful way through the economy. It is withdrawn from the economy only when the borrower pays back the principal to the bank.

"So remember that elemental scenario – a bank willing to lend and a borrower willing to borrow. Millions of repetitions of that event provide us with the money supply for the whole economy. A money shortage – in the current lingo, a 'credit crunch' – develops when that scenario breaks down. It breaks down either because banks are not willing to lend or because borrowers are not willing to borrow. At the present time we seem to have both conditions, banks edgy about lending and a scarcity of new borrowers. So what has to be done to remedy this constipation in the money supply?"

This would be a good time to take a sabbatical. Just slip over to the bar and refill your glass. By the time you return, the whole subject may have slid irrecoverably beneath the surface, or metamorphosed into a partisan political wrangle. If it is still alive, however, ask, "Would you like another simple idea?" Assuming that they consider anything from you better than the current trend of the conversation, go on to explain the "growth imperative." Don't mention it by name until you have got them to picture a fish tank.

A Fish Tank Economy

"Label the fish tank The Economy. Okay, now picture two pipes connected to it: an inlet pipe and an outlet pipe. The inlet pipe brings in new credit money every time the elemental scenario is enacted in a chartered bank somewhere. The outlet pipe takes money out of the economy every time one of the borrowers makes a loan repayment. Incidentally, the bank does not put the principal part of this pay-back into its vault for the next willing customer. It just writes the asset off its books. That money disappears.

"So long as there is enough water in the tank (money in the economy) and the inlet and the outlet are roughly in balance, the fish are happy. Right? Now, here's the simple point. When the bank creates a credit loan, it creates only the principal. It does not create the interest. It just creates the principal. The interest, however, also has to be paid to the bank. So, if it is not created into the money supply, where does the interest come from?"

You might pause here to wait to be asked for the answer. If the conversation turns combative and absurd, edge back in by repeating, "Remember that elemental scenario – a bank willing to lend and a borrower willing to borrow, Add to that the idea that the borrower must also be willing, and able, to pay rent (interest) for the money he, she, or it, has borrowed. Where is that interest money going to come from? Take the individual borrower. She is counting on next month's or next year's income. Now that assumes she has a job, or an investment maturing, or a rich auntie dying, or a winning lottery ticket. What about government borrowers? They have to pay the bank interest, too, at commercial rates (unless they borrow from the Bank of Canada). Where does their rent-of-money expense come from? Only one guess allowed, and it begins with 'T.' But taxes draw money out of the economy, too, just like repaying your bank loan. So we cannot expect sustainable solutions from either individual or government borrowers. What about corporations or small businesses?"

In the barber shop you might not get a burst of useful information on this question, but try it at a cocktail party, preferably earlier in the evening, of course. When you get the word "grow" or "growth" or something related, jump in with, "Growth, yes. That's the way the interest on our money supply is paid. Somebody – it has to be business – must create new wealth. So businesses are compelled to "grow the company" that is do more business this year than last year. It's called the "growth imperative."

"We hear a great deal about growth in the economic reports. You have reports of 'December's growth rate' and predictions of next year's growth rate. Did you ever ask why 'growth' is such an obsession? The answer is, as you see, simple: we have a debt money system, with over 95% of our money supply created as debt, and no money created to pay the interest on the debt. New wealth has to be continually created: another row of houses built, another ton of iron mined and smelted, a new product or service provided. Hence, the growth imperative."

When Growth Stops

"So what happens when growth stops, or reverses? Well, one thing is that the banks get uncomfortable and consider tightening up on their loans – just the wrong thing for a shrinking economy."

As the meltdown/"credit crunch"/recession/deflation/depression sequence spirals on, we could use a few backward-looking seers who know some of our history. For example, bank bailouts didn't work in 1932. Who expects them to work now? We could also use a lot more dummies who ask simple questions and won't settle for flim-flam doublespeak from "experts" who either don't know what they are talking about or, perhaps, prefer to keep the dummies ignorant. For example, how about some plain-spoken truth on these canards?

Overheard at Parliamentary committee: "Government borrowing from the Bank of Canada is inflationary." Overheard at Chamber of Commerce dinner: "The main problem is the national debt is too high." Overheard at the Albany Club: "The real cause of this recession goes back to excessive demands by the unions." Overheard at the barber shop: "The banks caused the stock market meltdown."

Wouldn't it be refreshing to hear some wise voice refute these magisterial pronouncements (all false) with simple explanations in simple language? Wouldn't it be great if you, yes, modest you, could drop a little soupçon of sense into this stew? Once you know that our money supply is created only as debt, you have a pretty good handle on how to think about the credit shortage. That's right, remember that the bulk of the credit-money we use (over 95% of the money supply) is rented from the chartered banks, and the rent has to be paid by growth in the business sector.

You might slip into a conversation on the latest decline in "GDP growth" by saying, "That means we won't be able to pay the rent." Half of the company will assume that you're short a full deck, and politely pretend they didn't hear you. But if somebody challenges you with, "Whaddayamean, with GDP growth off, you can't pay your rent?" Then you laugh. (Be sure to laugh. You set it up, so it's your joke.) You laugh and reply, "I didn't say I couldn't pay my rent. I said we won't be able to pay the rent on the national money supply. You probably call it interest, but in the economics schools they often call it 'rent.'"

You are now one up with the laugh, and one up with the put-down on rent/interest. So Mr. Whaddayamean will probably fold his tents and hump away.

But there may be some curious dummies in the company who want to converse on topics of national economic interest with some wizard who is familiar with "economics schools" (plural, no less!). The conversation might go like this.

Dummy I: (Chamber of Commerce). Yes, the government debt is too high. We pay too much interest on it.

Wizard You (confidently): You're certainly right about paying too much interest. If the politicians were only as smart, and as persistent, as the bankers, the government would still be borrowing from the Bank of Canada instead of paying rent to private finance.

Dummy II: (one who reads the minutes of Parliamentary committees): But wouldn't that be inflationary?

Wizard You: No. If the government merely transferred some of its existing $500+ billion debt from private lenders to the Bank of Canada (over a period of time, of course), there would be no increase in the money supply. So no inflation. There would be no "printing of money," as the spokesfolk for financial institutions always put it. The Bank would simply create the loan as a credit in the government's account, just as the chartered bank does to your account when you get a mortgage. There's no inflationary result if the total borrowed money in the economy stays the same. Where it is borrowed from is irrelevant, except to those who would profit from lending to government.

If the Government Financed Its Investments Through the Bank of Canada

Dummy 1: But we'd still have to the pay interest, except we'd be paying it to the Bank of Canada, wouldn't we?

Wizard You: Actually we would avoid almost all the interest expense for loans from the Bank of Canada If you own all the shares in a company, you get all of the profit as dividends, and Canada is one of only two or three developed countries whose government owns its own central bank. It gives our national government enormous power, which successive governments over the last forty years have been persuaded not to use. So if half of the current $550 billion national debt were loaned by the Bank of Canada, we would save half the interest we now pay to private lenders. Except for a small service charge, most of the rent would be returned to the government as dividends.

Dummy II: Well, if it's not inflationary, and we'd save all that interest, why hasn't the government done it?

Wizard: Because bankers are smarter, and more persistent, than politicians.

Dummy III: Well, the banks caused the stock market crash. So what should we be doing to shorten the depression?

Wizard: You know that taking on debt increases the money supply, and paying off debt decreases the money supply. If we have "credit crunch," that means too many borrowers are paying off debt and not enough borrowers are borrowing.

Dummy III: So what is the best way to cure the credit crunch and get more money into the economy? I sure heard lots of opinions when people were talking about the Budget.

Wizard: For starters, always ask the question, Who gains? You need that perspective before you can judge a proposal. For instance, the bankers say, "Give us lots of money and we'll lend it, and at lower interest rates." Some borrowers, like the common consumers) say, "Give us secure jobs at good pay, and we'll pay down our debts and start to borrow again." The entrepreneur says "Give me more money (I prefer handouts to loans) and I'll grow my business and create jobs." Governments say 'We'll borrow more money, and we'll put people to work repairing roads and teaching pre-schoolers, digging urban subways and erecting rural wind generators. And we'll hire more nurses.

If you were a member of the Canadian dream team consisting of the PM, the Minister of Finance and the Governor of the Bank of Canada, what would you choose from this menu of options? Think about it. Then lock in your vote by writing the members of the "dream team" with your solution. You should explain why your option would work best. They certainly need some new advice on that.

Dummies I, II, and III (in chorus): A lot of attention they'd pay to us. What do you think?

Now here's your opportunity, an appreciative audience with their mouths and ears open. You might say: "Well, let's take them one at a time. Proposal one – feed money to the banks. Who benefits? Well it won't cause bank shareholders to weep. But remember, the banks are the prime creators of our money supply. And they don't create cash; they create credit. They just have to get people to trust them. So leave that to the banks; they are good at it. Government could help by imposing some regulations to

guard them from unwise impulses, which brought us to the current problem.

"Proposal two – feed the entrepreneurs. Who benefits? Well, new jobs are created by new and expanding industries. But they need credit. Usually they get it from the banks. I would recommend by-passing the banks for a while at least and providing credit directly to promising businesses. The process of the bureaucracy managing direct subsidies to businesses has a lot of potential for problems, but, if it could be done for a short term, it does go directly to the heart of the matter.

"Proposal three – give consumers secure jobs. I would add give them direct subsidies, such as tax reductions for the spending half of the citizenry. (Forget the investing half; they're smart enough to look out for themselves.) Extend E.I. Devise mortgage support measures, so that homeowners can keep their homes and pay down their debts. Getting consumers spending is a two-stage process: first they have to shed some of their excessive debt before they will have the confidence to borrow again. Only at the second stage, the spending stage, can the commercial banks take over.

"Finally, proposal four – government spending to expand public sector functions and new work projects. The big objection you hear is to the horrors of government annual deficits and an increase in total government debt over the long term. Ask who benefits from government debt, because that depends on where the governments borrow. If they follow the practice of the last thirty years and borrow from the private banks, you know whose shareholders are again the winners. If (this applies to the governments of the UK and Canada, who own their own banks), if they borrow from their publicly-owned central banks (the Bank of Canada and the Bank of England), then government debt becomes the money supply, and it does not have to be paid back until it becomes inflationary. And that's not going to happen until the economy is booming again and ripe for plucking by the tax-collector. Isn't that just what we want – a booming economy and high taxes to pay down the debt? That keeps all the fish happy!"

Some astute listener may note, "You seem to be by-passing the commercial banks. You want the government to by-pass them on the bailout front, and to by-pass them on government borrowing."

Don't fudge. Say "Yep. The commercial banks are indispensable in financing a boom economy, but in a shrinking economy they are counterproductive. In a depression, helping banks helps banks, but it takes a long while for the banks to do much to help the economy. The borrowers have to be resurrected before the lenders can lend. A strong, direct government policy is the most effective medicine to cure a serious meltdown.

"Have another drink. Save a job in the distilling industry."

Gordon Coggins

Gordon Coggins is a retired Brock University professor and an occasional contributor to ER.

Three Potent Steps to a Sane Economy

Amidst today's uncertainties, is an historic opportunity to secure our lives and the lives of those we love. First we have to recognize the common cause of the financial and ecological crises – that human activity is touching planetary limits.

In order to achieve a balanced relationship with the Earth, we need to picture a new order in our hearts and in our minds. Then, each time we buy food, pump gas or have a conversation with a friend, we can advance long-term well-being.

Two different types of economic activity are identified below, followed by three potent steps we can take toward a sane economy. Together they provide a foundation for imagining what can be. As enough minds ripen the images, change happens.

Please pass these details around.

Two types of economic activity:

"Economics" is a somewhat mysterious word for "mutual provision." While, individually, we have limited ability to provide for our needs, we produce abundance in societies. Each person gets good at certain tasks and we trade with each other.

There are two types of economic activity. One type requires continual inputs of non-renewable resources and produces problematic waste. Transportation systems and disposable consumer goods are examples. The other type consists largely of human creativity and good-will, like education and most health care at the preventative level. While there are almost no physical limits to the amount of education and preventative care that we can have, there are serious limits associated with resource intensive industries.

For the things that we do need from the resource intensive line, the first two of the following steps can reduce our impacts on the Earth dramatically. All together, these three steps can usher in a long period of ecological stability.

Three potent steps:

1. Shift the imagination and creativity that presently goes into designing for obsolescence and use it, instead, to design goods that are durable and easily repaired.

2. Instead of using our persuasive communication abilities to encourage people to throw things away and to buy new stuff, we could use those same talents to reclaim an appreciation for durable and familiar products.

3. Finally, if we search for personal fulfillment in what we can do with our lives, such as learning, love, laughter, friendship, art, music, dance, sport, service, and the like, rather than by accumulating and consuming material goods, we could have more real satisfaction while minimizing resource exploitation and waste.

While such steps would do wonders for securing the future, they would be disastrous for a growth-based economy. We either have to increase the size of the Earth, or reorganize mutual provision so that we can all share in the necessary work and revel in the new security.

There are many ways to reorganize mutual provision to serve a mature (post growth) civilization, but it is getting harder and harder to stretch the Earth. Do we want to grow until we drop, or develop the economics of sustainability? It is a Question of Direction.

More about the Question of Direction and how we can cooperate to have the answer heard can be found at www.SustainWellBeing.net. Note the introduction at "The Challenge and the Goal."

Civilizations don't change direction easily. They must either suffer catastrophe, or exercise an extraordinary redirection of will. By launching a public discussion about which direction offers the better future, millions will come to imagine the options. Together we can then make a major contribution toward redirecting society's will.

Mike Nickerson

Report of a COMER Study Class in Colorado

You might find interesting this summary I prepared for a year long study group I host at our Senior Center. We have been examining the creation of money and our financial system now in such extremes. We meet for two hours every Friday. I believe the concept – so incredible – is getting through.

I attach my explanation of how the Fed creates money in an rtf file which all Microsoft windows software can read with Word Pad. I believe I have made my point.

Regards,

R.W. Zimmerer

To our Friday Study Group:

In July I wrote up what is more or less our consensus view of the role of money in an economy which I "enclose" below. My next commentary is on how the Federal Reserve, our US central bank, creates our "really, really" new legal tender much as the banker in the great board game Monopoly passes out $200 to the players as they pass Go to keep that game going. The present financial structure cobbled together on Jekyll Island 100 years ago is broken beyond repair. A new financial structure must be constructed out of today's wreckage!

Bob Zimmerer

An economy is:

The word comes from Greek referring to the management of a household. The simplest Economy would be a family household of parents, children, close relatives living together in a stable long-term relationship. A group of families in some cooperative arrangement of mutual support which has a long-term existence might be called a society. A society would have some distribution of tasks and duties agreed upon by its members to provide food, shelter, clothing, and organization management.

Within a family we are aware of this: father and mother provide the family's necessities of life for themselves and their children. The parents also provide organization and management. In a rural society most families live on a farm and can grow most of the food they need, probably build their own shelter (sod shanty or log cabin in the early US) and some clothing from empty flour sacks. In a sustainable society families support each other through diversification of activities. Farmers do not all grow exactly the same crops and livestock, grain would be ground into flour by a family which does not grow grain, a tailor would craft clothing for others to wear. Teachers in schools educate other peoples children as well as their own.

As a society prospered it would grow, expanding in both population, variety of occupations, and complexity. At this point its organization would likely develop a more versatile method of trading services and products than face to face exchange. Seeds planted in spring produce grain in the autumn. Surplus grain and flour would be stored. Cause and effect become separated in time if not space. Verbal promises, handshake deals, would lead to confusion and disputes when exchanges are completed over time among many people. Archeological evidence shows that records were made and kept of what today we call business deals – this now for that later. Writing may have originated in the need for keeping books of business deals. At a later stage, physical tokens were invented representing not the physical items exchanged but some numerical value associated with the items. Thus tradable items came to have a numerical value, a price, within the society which produced the items and invented the tokens. The token must be an invention as important as the wheel! One concerned time the other space.

Within a family, exchanges are not considered business deals (for the most part). The "cost" of raising a child is not recorded with a parent's expectation of being repaid some day. But my immigrant Norwegian great aunt did just that in Brooklyn, NY, 100 years ago. Parenting carries the implicit acknowledgement of child-raising obligations, a social contract, an investment. Among families and trades people it becomes practical to write down obligations (a contract) and use tokens to facilitate exchanges. To keep record books requires paper but to use tokens requires a source of tokens. Who creates tokens and how they become used is the story of money. In today's world, bookkeeping and tokens merge within computers. Rather than use a token one swipes a credit card to tell a computer somewhere to change token ownership in a record book. The credit card has proved more useful than its predecessor, the written bank check, which had reduced the use of tokens by 90% in its day.

Some History. The use of money/tokens has always been a tool of great power. Used by kings to build castles and fight wars it is a tool for peaceful commerce among his subjects. A monarch held tight control over the money created and used within his nation. History reveals that a nation's economy prospers when there is sufficient money in circulation and stagnates or declines when there is a shortage of money. A major cause of the Great Depression was banks creating too much money (making loans) for unproductive activity. The US government failed to save the banks from their folly or to replace the money destroyed by defaulting debt.

The Roosevelt New Deal was a decade long experiment with radical financial ideas of spending money and business involvement. John. M. Keynes advocated that government borrow and spend money to revive failing economies. WW II forced the USA to spend incredible amounts of money, deficit spending, to restart US industry which had languished for 10 years. War production brought instant full employment and produced astonishing amounts of war materiel of little peaceful use.

After WW II there was much surplus war materiel some of which had peaceful uses like machine tools and busses. Most of it was destroyed at government order to encourage peacetime industrial production to replace it and sustain full employment. The automobile industry rapidly converted back to private car production to meet the demand. In five years the new car market was reaching saturation as was the nationwide housing boom. Employment was falling and the US economy was heading toward recession when the UN Korean "police action" began and new jobs were created.

What Organization? Social organization exists in a remarkable range of sustainable forms. A society can persist with both a fabulously wealthy elite and greatly impoverished masses. It can have slavery. It can be a police state, an authoritarian theocracy or an open democracy. But its economy must supply basic materials for life: food, shelter, clothing. A common cause of societies to fail is their consuming the natural resource base supporting them as revealed in written history and unearthed by archaeologists. As humans migrated to new lands or invented new techniques for exploiting their environment, they always carried it to exhaustion much as unthinking parasites consume their hosts. The latest such natural resource being

consumed to exhaustion is fossil fuel. But while the party lasts, humans have gained extraordinary physical power over their environment. They have invented machines which replace human labor and enable us to change the course of rivers; remove mountains; land on Mars! Computers can organize vast amounts of information for us to analyze. Unlike past societies – Romans, Polynesians, Aztecs, Incas, Egyptians, Ephesians – we have the means to overwhelm our resource base and predict the consequences of our behavior.

The speed of communication and transportation has brought the peoples of Earth into close contact. It is more and more difficult to maintain independent national and regional economies. There is but one inhabitable planet and human societies have acquired total control over Earth's accumulated and renewable resources. The present use, abuse, and management of these resources threatens the existence of higher life forms on Earth and the sustainability of human societies.

The Vital Role of Money in Today's World Economy

A Brief History. The introduction of tokens to facilitate trade across time and space expanded business activity. It required agreement on a uniform numerical value for the token and control of their creation and circulation. From earliest human history it was the government of a king or emperor which administered the creation and distribution of tokens. They entered circulation by government purchases in the market place – when the king spent them. Tokens then circulated as a convenient alternative to direct barter and bookkeeping. Gold and silver were the common material used being durable, scarce, and easily fabricated into tokens. Tokens of gold and silver had inherent value of the metal from which they were made. They were imprinted with a number indicating their official value as legal tender. "Primitive" societies also invented trade tokens and made use of scarce easily controlled materials like rare sea shells and stones. The history of money is fascinating to read.

Gold smithing was a craft dealing with gold and silver. Gold smiths worked with gold given to them to fabricate decorative or functional objects for the owner. Gold smiths gave customers paper receipts for accepting their gold. These receipts had the market value of the gold they represented. Gold held by a gold smith could be traded among its owners by exchanging receipts for the gold. The value of gold tokens was proportional to their weight an easily measured number by even a street vendor.

Banking evolved from using gold receipts as paper money. Gold smiths became bankers as they began loaning gold coins deposited with them. They issued paper notes representing gold coins they held. The gold tokens, coins of the realm, legal tender, originated under tight control by the reigning monarch who alone could manufacture them. Banks were allowed to print bank notes, receipts, exchangeable for the king's tokens they supposedly held in their vault. The monarch did not regard this as counterfeiting his money. Bankers discovered how easy it was to issue more bank notes than the gold coins in the bank vault. As long as more bank notes were not exchanged for coins than a bank possessed, business flourished and the economy prospered. The history of banking records the sad frequency of economic depressions resulting from too many people demanding nonexistent gold coins for their bank notes. Business booms routinely end in busts. As a result banks became more and more regulated by state and federal government trying to avoid recurring financial panics. Bank notes printed by different banks were often not accepted by other banks nor by business people suspicious of a bank's ability to "cash" a bank note for the real thing. The practice of loaning money a bank doesn't have is called "fractional reserve banking" and is the principle method of increasing the amount of money in circulation.

After the 1907 US bank panic a federal reserve (bank) system, the Fed, was established by an Act of Congress in December 1913. Its 12 regional banks are privately owned but the seven members of its Board of Governors, are nominated by the US President and confirmed by the Senate. It is the US Central Bank, the Bank of Last Resort and banker to the US Treasury Department. Congress thus delegated its constitutional authority over the monetary system of the US to the Fed "…to provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes," as stated in its founding act. The Fed has had an indifferent record achieving these goals.

New Money Created by Computer. Today's commercial banks, accepting deposits and deciding who gets loans, guide the US economy if not control it outright. Loans are made by writing a number into the borrower's bank account. It is a bookkeeping action which creates new money with a computer key stroke. It is a powerful activity akin to banks of old printing bank notes but this time the bank creates new money which the Fed must support with legal tender, Federal Reserve (bank) notes. Private banks are supposed to be regulated and supervised by various agencies of federal and state governments. New money enters circulation when a borrower writes a check to pay for something. When the loan has been spent into circulation there remains an interest paying loan on the bank's books, an asset to the bank as long as it earns money. It is a debt liability to the borrower who is expected to pay interest and someday pay back the loan.

Banks are limited by the Fed to how much new money they can create making loans. Financial inventions like credit default swaps and securitized investment vehicles evade limiting rules and create tension with government bank regulators trying to enforce rules. One of the most successful financial inventions is the personal credit card which allows its owner to print new money. As long as the credit card owner pays the minimum monthly charge, bankers "make" money and business booms with new money entering circulation. Personal savings is no longer a virtue nor needed. Citizens, now called consumers, buy on credit, new money which they can create with a swipe of their credit card. Personal spending is over 70% of commercial activity.

Banks creating money by fractional reserve banking is not considered counterfeiting nor called a Ponzi scheme. Borrowing is accepted to such an extent that the federal government itself borrows money to pay its expenses. Income taxes paid to government come from a loan somewhere. Interest on outstanding private loans as well as on national debt, can only be paid by more loans. If bank loans (debts) were all paid off with checks on bank deposit accounts, a bookkeeping action which involved no actual legal tender, there would be no outstanding loans (debts), bank deposit accounts would be empty, and very little money would remain in circulation. If, however, depositors one day closed their accounts demanding cash, the Federal Reserve would have to provide the cash which would far exceed any cash the banks possessed. Banks would be left with loans

but no deposits on their books.

New money can be created as long as new loans can be made. An economy sustained on debt-created money needing ever more debt just to pay the interest on it is not possible. It is simple mathematics to show that activities depending on endless increase are exponential and unsustainable. There comes a time when exponential increase stops and dire consequences result. This is a basic cause of financial panics. In the classic board game of Monopoly the bank has an unlimited supply of money from which to give players $200 each time they circle the board. In the real world the US central bank, the Fed, essentially does this to keep our US economy going. It does so by adding to an ever increasing US national debt supporting the myth that money is not created just borrowed. Attempting to continue the present failed financial system guarantees continuing cycles of boom and bust. It will soon be 100 years since the Federal Reserve system was created. Doing the same thing over and over expecting different results is called madness. It is however a gift which keeps on giving to some private bankers.

Does the US Central Bank, the Fed, Really Work This Way?

Figure 1 represents the hierarchy of banks in the US. The central bank like the US Supreme Court is at the top of its hierarchy. The Fed manages its own deposit account, the US Treasury deposit account, and a family of privately owned commercial banks diagramed here as one composite "BANK." BANK in turn manages the deposit accounts of a myriad of private and public deposit accounts which write checks to each other as their owners carry on business transactions.

The legal tender of the USA is the $US, the dollar. It has a physical existence, the Federal Reserve note and miscellaneous metal coins. Almost all business transactions are conducted with surrogates of legal tender, bank checks being most commonly used to move the contents of deposit accounts among their many owners. Of course a deposit account is not literally a container of legal tender which can be touched and physically moved. It is a number in a bank record book of accounts. The book today is a computer and banks manage bank account records at the touch of a computer key to move their contents, money, at the speed of light, among bank accounts. Only a small portion of banking today is with actual physical money, cash.

This describes how money is manipulated. Where does the money come from to manipulate? Commercial banking's principle activity is making loans by creating debt. It is called "fractional reserve banking" whereby a bank loans money into existence. The bank adds numbers to the record of a deposit account which increases the quantity of money it holds. There is no new legal tender, cash, involved. The holder of that bank account can now write checks to pay money for business transactions. The amount of money circulating in the economy has increased. There has been no increase in the amount of legal tender. Banks are regulated in how much new money they can thus create. The power of money creation is placed with the Congress by the US Constitution. Congress created the Federal Reserve system in 1913 and delegated this power to the Fed making it the central bank of the USA. The Fed is charged by Congress to manage the creation of US money and the function of the US banking system.

The US Treasury obtains money through taxes, tariffs, fees, and borrowing to pay for the US military: Coast Guard, National Institute of Health, NASA space program, constitutional obligations of the federal government. New Treasury bonds, like private securities, are auctioned to underwriters who purchase them for resale. Entities that have cash or money in their deposit account, purchase them. This money from the final purchaser then flows back through the banking system into the deposit account of the original bond seller. In the diagram above Treasury sells bonds to BANK. BANK writes a check on its own bank account at the Fed payable to US Treasury. Treasury deposits BANK's check into its Fed account.

Treasury now has more money to pay defense contractors and pay interest on existing Treasury bonds. The Fed decreases BANK's Fed account the amount of the check. BANK has exchanged money in its Fed deposit account for an interest earning asset. The result is that money in circulation has been moved from BANK's ownership to Treasury. BANK then sells off its Treasury bond in pieces to its many customers who pay for it with checks on their account at BANK. BANK no longer owns the US Treasury bond but many others now do and collect interest on it.

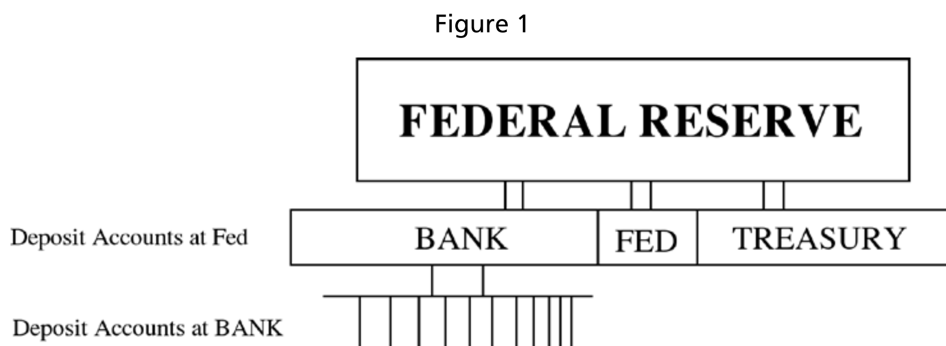
BANK now has increased (restored) its Fed deposit account with money moved from its customers account to BANK's account as they purchase pieces of the Treasury bond. The net result is that money in circulation has been moved from private depositors accounts to Treasury's deposit account. Private money has been exchanged for a financial asset – a Treasury bond.

The Manipulation of Deposit Accounts. All this bank activity is done by bookkeeping (computer) entries as deposit accounts are manipulated. There has been no increase in the total money in circulation (the US money supply) just a change in its ownership. The money supply can increase however if the Fed buys the pieces of that new Treasury bond from the people who purchased it from BANK. The Fed then becomes bond owner and increases the deposit account of the seller. The Treasury has in a round about way sold its new bond to the Fed and apart from the fees paid through the many transactions, Treasury will now spend entirely new money.

Fed owns the new Treasury bond and all interest paid on it is paid to Fed's own account. By law the Federal Reserve is allowed to earn a small fee for its management of US money and must deposit the remainder of any money it earns from banking operations into Treasury's Fed account. Thus most of the bond money and subsequent interest paid by Treasury is returned to Treasury's Fed account from whence it came. This is not a very efficient way for Treasury to sell bonds.

The Fed in this scenario created new

Figure 1



money by buying a new Treasury bond something like a private bank creates new money by creating a new debt. But the Fed is the central bank of the USA. It pays with legal tender it gets as it needs from the US Treasury Department Bureau of Engraving and Printing and Bureau of the Mint. It does not "balance" its account books like a private bank. *It does not decrease its own account when it buys a Treasury bond or any other security.*[1] New money is created from the new national debt which was created by selling a Treasury bond. Likewise new money is created when the Fed buys any securities toxic or not. Thus legal tender is debt money as much as the money a commercial bank creates by fractional reserve banking.

Over time there will be quantities of Treasury debt held by the public and by the Fed. The Fed can buy Treasury bonds held by the public and can sell its Treasury bonds to the public. When the Fed buys publicly held Treasury debt it can write a check or credit an account thereby increasing money in circulation without decreasing (debiting) any account. When the Fed sells its Treasury debt to the public it reduces the amount of money in circulation. This is the principle method used by the Fed to control the amount of money in circulation. In either situation the US Treasury continues to pay interest on its bonds.

This commentary shows that there is no need for using physical, tangible, legal tender – cash. Money movement can be accomplished by bookkeeping entries. Private banks create money by debt as does the Fed create money with a national debt. The checks used by individuals to buy a Treasury bond spend money which was created somewhere by a bank loan. Treasury spends money created by the national debt to pay government expenses. The taxes and fees individuals pay to government originated in a bank loan. The money in circulation, the US money supply, is almost entirely created by interest earning (paying) debt: it is all debt-money! The interest being paid (earned) by debt-money requires that ever new debt-money must be created!

To meet the small need for actual cash-in-hand, banks can "cash" checks with Federal Reserve notes or coins. Banks maintain a small amount of legal tender for that purpose. The Fed maintains a vast store of legal tender which can be physically delivered by armored truck to banks in need of cash. In many ways the US economy is financed much like the players in the popular depression-era game of Monopoly. Monopoly money is continuously injected by the Monopoly banker who passes out $200 to players each time they pass Go from his inexhaustible Monopoly money supply. The game also shows how financial wealth tends toward concentration into one account.

R. W. Zimmerer

1. Page 33, Purposes & Function of the Federal Reserve System, www.federalreserveg.gov/pf/pdf/pf_complete.pdf.

Could Capitalism have Survived Without the Chinese Revolution?

The Wall Street Journal (19/08, "China's Appetite for Nickel Drives a Symbiotic Alliance" by Devon Maylie) presents that puzzle. Translated into Canadian terms, it reads: "Chinese nickel companies are quietly collecting stakes in junior miners, in a move that guarantees future supplies for China and could help the small companies meet output targets.

"With its huge construction projects and export market, China is the world's biggest consumer of stainless steel, of which nickel is an important ingredient. But with the country's consumption of nickel ore outstripping its own mines' output – China needs to import about 23% of its consumption – the country has traditionally imported large amounts of the refined metal.

"So, eager to ensure its future, China is buying stakes in resource-rich junior nickel miners, many of them based in Canada. And as a further guarantee of supply, it is parlaying some of its holdings into takeovers.

"'China isn't self-sufficient in nickel,' said Vanessa Davidson, an analyst at consultancy CRU. 'If it wants to be self-sufficient, it needs to negotiate new contracts for [raw material] because it doesn't have that much in the ground.'

"That is where the stakes in small miners come in. Many small miners have been struggling since finance dried up and credit tightened last year. But Chinese nickel companies are offering small miners an alternative, in the form of stake acquisitions and off-take agreements, where Chinese companies agree to buy part of the miners' output at a fixed price.

"In short: the juniors have the material and China has the smelters and the financial firepower. The juniors are able to reduce debt, restart closed projects and resume mine development. And China secures nickel supplies for its expanding smelters.

"'My sense is that the Chinese prefer to be an investor with significant stakes that secures stuff for the future,' said BMO Capital Markets analyst David Cotterell.

"Mr. Cotterell said Western-owned companies tend to be good at producing, and the Chinese companies appear to be happy to let them run the mine and then get the output results.

"Taking stakes in several small miners spreads out risks – at least one of the projects is likely to be fruitful, Mr. Cotterell said. And the lower profile of the junior miners compared with that of big companies such as Rio Tinto Ltd. minimizes the risk of political problems, analysts say.

"In May Jilin Jien Nickel Industry Co. completed a $30 million deal to buy a stake in Canadian nickel miner Liberty Mines Inc. It is now the company's largest shareholder, with 51% of common shares; Liberty restarted mining operations this month as a result of the funding.

"'With bleak nickel conditions it's a good opportunity for Chinese companies to be involved in overseas nickel operations,' a Jilin Jien spokesman said. 'We are the second largest nickel producer in China and we need more nickel from overseas,' the Jilin Jien spokesman said.

"The company likes small-to-medium mining operations producing ore with a nickel content of at least 1%.

"Liberty chief executive Gary Nash said the company normally sends half of its output to Jilin and the rest to Xstrata PLC, with price determining whether it is ore feasible to ship to Xstrata's smelter in Ontario, Canada, or farther afield in China.

"Jilin also has investments in Canada's Victory Nickel Inc. and Goldbrook Ventures Inc. Victory Chief Executive Rene Galipeau said that with its smelter and refining technology, Jilin is a good destination for Victory's nickel concentrate output. 'They're a strong shareholder, a plus for financing and a potential customer,' he said."

That would appear to cover all bases.

W.K.

Obama Hip-deep in Potholes

The Wall Street Journal (07/30, "Risks and Rewards in Push to Boost Community Colleges" by David Wessel) President Obama seems hopelessly lost in the ambiguities of speech whenever he opens his eloquent mouth to let forth some new aspect of his sweeping reforms. These never quite clarify what it is he is proposing and where the money is to come from. We cite: "Like his predecessors, President Barack Obama has discovered community colleges, the too-often denigrated community institutions that offer a first chance to those who never mastered English or arithmetic and a second chance to those whose skills no longer command a decent wage.

"Much more than his predecessors, Mr. Obama is offering money – $12 billion over 10 years, pushing private companies out of the student-loan business to raise the money.

"Student-loan providers are shrieking. Community colleges are celebrating, though wary of a provision that requires quantitative benchmarks on their progress. But the headline writers have moved on to health care and housing prices; the president has gone from speaking at Michigan's Macomb Community College to sharing a beer at the White House with the Harvard professor and the Cambridge, Mass., cop.

"Yet details of his American Graduation initiative offer a window into the Obama approach to government, both its potential to produce the 'change' for which he so loudly campaigned and the risks he is running by spending so much with so many promises.

"Mr. Obama offers lofty man-on-the-moon goals: The US will once again have the highest proportion of college graduates in the world by 2020. But even he doesn't have enough money to finance that. So he proposes a competition as he has for K-12 money. A bill likely to pass the House soon lays out a long list of criteria that the Education and Labor departments are to use in design software, to design process piping for refineries and power plants in a six-week intensive course.

"The notion, a hallmark of Mr. Obama's spending is to use money to spur innovation and to devote taxpayer dollars to the most promising avenues, rather than financing old ways of doing things.

"It sounds good. And no doubt community colleges could use the money. Their enrollments are rising; their budgets aren't. They remain among the most important escalators of social mobility. But a lot depends on how the colleges use the money. Taking federal money to do more of the same won't do it."

And here we must interrupt Mr. Wessel to interject a word on the importance of alternate life styles even for climbing the corporate ladder. Moreover, on a variety of over-lapping grounds. A knowledge of arithmetic will better equip the more lowly against the lures of advertising that could take unfair advantage of those with inadequate or faulty schooling. During the Great Depression not only the Social Credit folks but writers of the stature of George Orwell prepared for careers of great distinction by using the literacy acquired where they could to develop their gifts. During the Great Depression of which I have intimate personal memories, public libraries were a blessed refuge. They were the means for educating yourself when your family's money and seemingly the government resources were taken to have run out. One of the important things to be learned was how to be a competent citizen eager to make best use of your vote, so that our democracy might function better.

So there is much to be said for even Mr. Obama spending more time in libraries to broaden his grasp of how to set this world aright. He could learn about the costly confusion of mistaking all "debt" of the government to be a negative thing – a sign of extravagance and improvidence. That debt includes the entire money supply of the land including what is hoarded by China and other foreign powers. It also in large part includes unspeakably faulty accountancy of the federal and state governments that treats the governments' (all three levels) investment in human capital as just another current expense, even though it was proven by the greatest lesson to have come out of WWII as the best investment a government can make. Because that experiment has been erased from governments' memories, we of COMER are condemned to repeating it so that it may not be lost. So here we go, once more.

After the end of World War II, Washington sent hundreds of economists to Japan and Germany to study the war damage to predict how long it would be before those two defeated mighty trading countries could reappear as such again. One of these economists, Theodore Shultz, sixteen years later revealed his final conclusion – that he and his colleagues could not have been wider off the mark. And the reason was, he concluded, that they had concentrated on the physical destruction and overlooked the importance of the detail that their highly educated, disciplined, and talented work forces had come through the war almost intact. Nor did he stop there. From that he reached the further conclusion that investment in human capital – which would include preservation of the environment, of course, is the most productive investment a government can make.

That, of course, like the arms of an octopus extended significantly into every field of human endeavor. For a few years, Schultz was feted and even decorated, and then completely forgotten by a very active negative act of public memory that transformed the accountancy of governments throughout practically the entire world into fraud.

About one thousand years ago an order of Crusaders, the Knights Templar, had brought back from Saracen countries a system of double-entry bookkeeping known as "accrual accountancy.' Each capital transaction of the government was entered twice – once the cash or debt incurred to make the investment was written off in accordance with a preset schedule and *"amortized"* over the foreseeable useful life of the investment. On the asset side it was *depreciated* to its current market value. Thanks to it, a glance could tell all interested parties – and notably creditors – how the investment was doing. To the Muslims this had been a vital means for observing the restrictions on charging interest of their faith – it could be charged without risking eternal hell fires only if the lender put himself at risk in sharing the hazards of the enterprise he had helped finance.

That made possible the flowering of the Republic of Venice since it gave it the means – alone amongst Christian nations for a long period – of trading with the Muslim world. But, especially in central and Western Europe it made possible the financing of the great maritime voyages that led to the discovery of the Americas and of the maritime route around the Cape of Good Hope to Southern and Eastern Asia.

In one degree or another accrual or "double entry" accountancy became the basis of accountancy that private firms and individuals had to abide by. But not the governments themselves. They fell into the habit

of carefully "amortizing" the financial outlay for the financing of the government physical investment, but the value of the capital assets involved were "depreciated" in a single year. The end result: at the end of Year 1, the asset value of the investment was written off to a single dollar, while the debt incurred to have made it was almost at its original level. That reported, in consequence, a fictitious deficit. And with physical assets of government carried on the books at a token single dollar from year two on, it made possible highly fictitious "privatizations" for well-connected parties. The government books were thus cooked. The purpose?

For the answer we must turn to one of the main achievements of a French economist with whom I had a special relationship – François Perroux – and his theory of the "dominant revenue." This holds that in every society the growth of the revenue of the class in the saddle is taken as the reliable index of the well-being of the society as a whole. In sequence the "dominant revenue" over the 19th and 20th centuries in Britain have been – the large feudal landowners and due to it land rent were kept high behind the Corn Law tariffs. Then the "dominant revenue" passed on to the industrialists as John Watt's engines transferred supremacy from the landowners when they still had a virtual monopoly on steam-power equipment in their factories, and made of them evangelists of free trade throughout the world.

So long as the British workers were illiterate, economists could adhere to some version of the theory of labour as the source and yard-stick of value. But as the 19th century moved on philanthropic "mechanics institutes" and then even public schools had begun teaching them to read. At the same time, by 1848 barricades were being thrown up in almost every capital in central and Western Europe, and soon, defeated socialist and anarchist leaders were arriving in Britain as refugees including Karl Marx and his family and Friedrich Engels. They lost no time in starting open-air meetings in Hyde Park almost within earshot of Buckingham Palace. Clearly labour theories of value had become perilous sources of sedition crying for replacement. The need was answered in at least three European capitals independently within a few years of one another. By it the miracle of value creation of commodities was shifted from the dismal factories to the elegant sales galleries, and traced its measurement to the degree of pleasure derived from their consumption.

To guarantee the success of so violent a switch, the shift was spiced with a touch of misplaced infinitesimal calculus, mistaken by the mathematically naive for a guarantee of scientific soundness. In fact mathematics can bring no empirical content to a scientific problem. Its capacity for analysis, on the other hand, is unbounded. There is a distinction that has escaped what passes for official economics today.

FDR's Daring Improvization

By the early 1990s the restrictions imposed on banks under Roosevelt during Depression were practically disregarded though they were still in the law books. Even those like the *Glass-Steagall* law that barred banks from acquiring interests in "non-banking financial pillars" – at the time essentially stock brokerages, insurance and mortgage companies. The reason was clear – without such a ban the bank acquiring such pillars will make a bee-line for their cash and near-cash reserves needed for their own business and use them as money base for their own bank-credit creation. What results is a skyscraper each floor of which is acquired in turn by acquisition. What emerges is a skyscraper of conquest with elevators restricted to going only upward, never ever downward, and at ever-increasing speed. Since the current acceleration of the elevator has already entered into the deregulated bank's self-evaluation, slackening its speed, let alone descending, would cause a thundering market crash of the sort that we are currently experiencing.

This sort of crash took over in the latter 1980s and led to the Bank for International Settlements – which had become a sort of war room for the plans and plots of central banks to bring back the bank deregulation of the 1920s. It resulted in the BIS bringing in an arrangement under which banks of developed countries if they meet their capital requirements – note well, judged by their capital, not their liquidity – can acquire an unlimited amount of government bonds of advanced country governments without any down payment. And some three or so years later came a declaration of the BIS manager declaring that interest rates had to be pushed up until what it chose to call "zero inflation" were attained. In its zeal to get back to the happy 1920s BIS overlooked that if interest rates are pushed up to achieve "zero inflation" the market value of the immense amount of government acquired by banks without down payment three odd years earlier would crumble. And when that happened, the IMF, the US and Canada put up the largest standby fund ever to that date $51 billion US to prevent the resulting crash of the world monetary system.

It proved unnecessary to draw on that fund, but the experience left the Clinton administration shattered. It decided there and then that the days of ever higher interest rates were over. As a result it brought in accrual accountancy for physical investments of the government, carrying back the reworked accountancy to 1959 and in doing so revealed some $1.5 trillion dollars of government in physical capital that could be considered prepaid because for the first time it appeared as such on the government books. Canada followed lamely in 1998, when the Auditor General encouraged by the US adoption of accrual accountancy refused to approve two years of government accounts without reservation unless this had been done in Canada as well. The government resisted strongly, and a bad compromise was reached for a far lesser amount, and misrepresented under the heading "savings." Since "savings" usually relates to cash or short-term securities of near legal-tender quality. the title could only have been deliberately misleading.

But the precedent had been set for the same sort of recognition of government investment in *human capital* being applied both in the US and in Canada. When the 1.5 trillion dollar recognition of prepaid physical capital was reached reaching back to 1959, even allowing for the exchange rate changes alone would account for some $2,500 billion. Add another trillion for the grossly understated increase in the stock of human capital and we come up with a $3,500 billion of human capital investment, and – taking one tenth of that as a plausible figure for Canada – $350 billion in Canada of up to now unrecognized human capital investment.

There is this about human capital, it frequently represents a further investment even by being spent. The children of well-educated parents tend to be more easily educated, healthier, and better adjusted. Moreover it cuts what is currently classed as an expenditure and reveals it a prepaid further investment in many, possibly the most cases. It is one of the few things that would really turn around the economy. Why then does it not rate a mention although COMER tried alerting President-Elect Obama to its vast possibility well before his inauguration.

The reason: the "dominant revenue," my little and big ones, the "dominant revenue" stood in the way of even a mention of it, let alone its application.

Let our readers take it up from there.

William Krehm

New Bubble Trouble Wave Amongst US Banks

Just when the optimistic pipe-smoking prophets had assured us that the worst was already behind, *The Wall Street Journal* (20/08, "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 COO 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 cards are at all-time highs. The accumulating bad assets and needs for capital means 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 a question 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 for companies and 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.

"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."

The Menace of Crippled Securities

"'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 very 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 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 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 that weren't growing, and there wasn't a lot of 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 mortgage-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 200 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 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

Book*Store*

Available from COMER Publications
245 Carlaw Avenue, Suite 107
Toronto, Ontario M4M 2S6

Price EXcludes postage and handling.

Hazel Henderson

- *Building a Win–Win World — Life Beyond Global Warfare*, $15
- *The United Nations: Policy and Financing Alternatives: Innovative Proposals by Visionary Leaders,* Editors Harlan Cleveland, Hazel Henderson, Inge Kaul, $10

W.F. Hixson

- *It's Your Money,* $10

William Krehm

- *Towards a Non-Autistic Economy – A Place at the Table for Society,* $10
- *Babel's Tower: The Dynamics of Economic Breakdown,* $10
- *The Bank of Canada: A Power Unto Itself,* $5
- *Democracies and Tyrannies of the Caribbean,* second English and third Spanish editions available, $15
- *Meltdown: Money, Debt and the Wealth of Nations – Volume 1, ER* from 1988–1998, $25
- *Meltdown: Money, Debt and the Wealth of Nations – Volume 2 ER* from 1999–2001, $30
- *Meltdown: Money, Debt and the Wealth of Nations – Volume 3 ER* from 2002–2003, $30
- *Price in a Mixed Economy – Our Record of Disaster,* $15

COMBO OFFERS:

- One volume of *Meltdown* plus either *The Bank of Canada* or *It's Your Money,* $35
- One volume of *Meltdown* plus *Democracies* (English or Spanish), *Price in a Mixed Economy, Babel's Tower, The Bank of Canada* and *Towards a Non-Autistic Economy – A Place at the Table for Society,* $90

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 described it as 'a wonderful chain of stupidity.'"

Lights for Banks that Survived the Great Depression

"'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 a 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, a railroad and a small mortgage company. With government help, the Austin company put the S&L and two other failed Texas thrifts into a new thrift that was 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 a year earlier.

"A Guaranty spokesman refused to comment. '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 by 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 presents itself.

W.K.

Cash for Clunkers

Dear Bill:
I want to thank you for your writing in the journal COMER. It is a voice of reason in a sea of myth. I also attach a little poem of mine.
Regards,
Dr. A. Allan Schmid, University Distinguished Professor, Dept. of Agricultural Economics, East Lansing MI

A man loses his job.
Nobody has money
To buy what *he* makes.
And, he has no money
to buy what *they* make.

Who has the money?
Has it blown away,
leaving many destitute?
Have our factories rusted,
leaving labor no machines?

If it takes more money
to make things,
then let's make
more of it.

Can't do that, old sages say.
We must suffer for past excesses.
But, those suffering
are not those who
made silly paper.

Can do it, new voices say.
If banks only want to play at casino,
let the government write numbers
after the names of the homeless,
Joe the plumber and Sarah the unemployed.

Only blind superstition stops it.
We won't be the first civilization
to worship old gods while
they perished from the earth.

Have You Wondered?

The answer was not long in coming. *The Wall Street Journal* (20/08, "SEC Plays Keep-up in High-Tech Race" by Tom McGinty and Kara Scannell) has made the connection.

The Securities and Exchange Commission says it is taking a close look at flash quotes, high-frequency trading and other dark corners of the stock markets. We described the techniques in question, and wondered how the brokerage fraternity would have the gall to bring in a heightened amount of distracting technology at a critical moment like this. It was the *WSJ* piece that grasped the deeper connection: it was to create enough confusion with all the new high-tech to soar over the head of the enforcement agencies, and repeat its stunts at a level of technology that leaves the bureaucrats, and President Obama himself out of the race.

But harken to the *WSJ:* "The Securities and Exchange Commission says it is taking a close look at flash quotes, high-frequency trading and other dark corners of the stock markets. By many accounts, the agency is outmatched by the traders and market venues with technology that is remaking the trading world.

"The agency lacks its own traders with knowledge about cutting-edge strategies and how the markets operate. It long ago ceded the daily surveillance of trading to self-regulatory organizations like NYSE Regulation and the Financial Industry Regulatory Authority. And it takes a lawyerly approach to regulation and rule-making that rarely employs deep analyses of real trading data.

"Jonathan Katz, who left the SEC in 2006 after 20 years as secretary, says the complexity of modern markets poses a stern test for the agency.

"'You need the quantitative, analytical capacity that the agency has never had,' Mr. Katz says. 'You need to start looking at these issues, but you need to look at them also as questions of national economic policy: how do the markets truly function?'

"The SEC's examination of the trading tactics comes as the agency is under pressure to prove to Congress and investors that it is up to the job many say it failed to do in the lead-up to the financial crisis.

"Fighting to preserve the SEC's pre-eminent place in the regulatory order, Chairman Mary Schapiro has ramped up enforcement efforts and quickly responded to complaints of market inequities. In response to criticism after the agency's oversight of investment banks that collapsed and its failure to detect the multibillion-dollar investment fraud pulled off by money manager Bernard Madoff, she created new positions geared toward recruiting on Wall Street to help the agency better understand what is going on in the markets on a real-time basis.

"In recent statements, commission officials have admitted they lack the tools to do the same kind of data-intensive surveillance as the self-regulators. In prepared remarks to Congress last month, Ms. Schapiro said the SEC was 'seeking to develop systems to mine data from multiple sources.'

"'We are enhancing training for our staff and also recruiting additional professionals with expertise in securities trading, portfolio management, valuation, forensic accounting, information security, derivatives and synthetic products and risk management,' she told Congress.

"The SEC is expected as soon as next month to issue a rule-making proposal on flash orders, which give equities and options traders on some exchanges an early look at orders before they are routed to other markets. Critics say flash trading can hurt market transparency and give a leg up to certain traders.

"The staff is also considering rules to root out unfair advantages to traders in dark pools, automated trading venues in which orders are matched without displaying all quotes publicly.

"In proposing the rules the SEC is expected to solicit comments and meet with proponents and opponents of flash orders and dark pools. But the agency hasn't collected market data that would allow it to follow a trail of flash quotes and analyze their true impact on share prices and trade executions, according to people familiar with the agency's progress."

Shortcomings of the SEC

"'Although the SEC receives many filings of different sorts, it does very little to collect significant data, analyze it, and then disseminate it to other government agencies and the market-place,' said Harvey Pitt, a former SEC chairman, in an email to *The Wall Street Journal.* He said he expected to make a similar push when he was appointed in 2001, but those plans were derailed by the September 11, 2001, terrorist attacks and the Enron and WorldCom scandals.

"The agency toyed with its own surveillance in 1980 when it deployed the Market Oversight Surveillance System, a Computer program that plugged the SEC into mounds of trading data being generated by newly electronic markets.

"The exchanges, which had policed themselves, complained bitterly that MOSS usurped their authority, according to media accounts. The SEC ultimately extracted promises that the exchanges would beef up their ability to police trades across markets and discontinued its own surveillance system in fiscal year 1985, according to SEC documents.

"Today the SEC still requires the exchanges to conduct their own market surveillance, and it closely monitors the adequacy of the programs through inspections. NYSE Euronext's regulatory arm conducts a review of its New York Stock Exchange, while Finra polices the trade on NASDAQ and the over-the-counter markets.

"A large portion of the trades is generated by high-frequency traders, whose computers scan the markets for profit-making opportunities and make rapid-fire trades to lock in gains. Finra has its own constantly evolving computer code that sifts the data for suspect patterns. When anomalies are found, alerts are sent to analysts in Rockville, MD, says Tom Gira, who heads Finra's market regulation department.

"'The alerts – that's our bread and butter,' Mr. Gira says. 'It's all technology. So much of the market is technology now.'

"At any time, Mr. Gira says, Finra's analysts are conducting 3,000 investigations spurred by the alerts. Each year, 250 to 300 investigations result in formal charges of securities law violations he says.

"The SEC's enforcement division also is developing its own screening system, Earlier this month, the new chief of enforcement, Robert Khuzami, told New York City lawyers, 'We expect to build some of our own technological tolls and screening programs to ferret out suspicious trading activity.'

"Still, those changes don't do much to assuage critics who think the SEC leads first with enforcement and then with analysis. Industry representatives and former SEC officials say the conflict has at times chilled frank conversations between firms and the regulator, inhibiting the SEC's ability to obtain real-time information."

W.K.

Some Highly Relevant Points about Elementary Education that Could Help President Obama Find a Way Out of the Jungle

The opening of school term has occasioned a gush of discussion in the press on whether much of the stuff still taught in schools is really relevant in this computer-run world. Much of the material carried in *The National Post* (5/09, "Children have very distinct thinking skills: Five kinds of smart" by Megan O'Toole). Amazingly, the official economists who shape the economic disasters that pass for economic policy, score close to zero or worse on every one of these.

We quote: "Howard Gardner, the Harvard psychologist and education guru who revolutionized thinking about how we learn with his multiple intelligences theory, has insights even more challenging for teachers heading back to the classroom.

"While multiple intelligences dictated different teaching methods for the different style of learners in each classroom, his latest 'five minds' theory suggests that every lesson needs to develop the distinct mental abilities he says humans need to succeed.

"These are distinct thinking skills – the disciplined mind, the synthesizing mind, the creating mind, the respectful and ethical minds – that, he says are often not stressed enough in traditional learning environments.

"To measure performance, we need to expose students to new examples – news articles, scientific findings – where they have not already been taught a prescribed response or analysis, and see whether they can make sense of them,' he said in an interview.

"'Unfortunately,' he said, 'too many schools today are stuck on more traditional methods of teaching and assessment, with an unhealthy emphasis on standardized testing that allows only one correct answer.'

"Mr. Gardiner explained his theories, for which he has become widely renowned and named one of the world's 100 most influential public intellectuals, in an interview before delivering an address at a Toronto education symposium this week.

"Under the multiple intelligences theory, a child who struggles to comprehend basic math problems may be just as brilliant, or even more so, than a youngster who breezes effortlessly through pages of calculations. The importance is in the type of intelligence each child possesses. The struggling child, for example, may become alive with understanding when the same mathematical material is presented in a different way: through language or song.

"In the simplest terms, the multiple in-

Patterns *from page 1*

rapher. Texas, for instance, is solidly red when it comes to presidential elections, but Democrats have begun to make inroads in the state Legislature, buoyed by a flow of newcomers from more-liberal states such as California. So political analysts believe one or more of Texas's new seats in Congress may well translate into a Democratic pickup."

Changing Population Structures Affect Distribution of Federal Grants

"But population counts do more than determine congressional seats. They also govern the distribution of nearly $400 billion a year in federal funds for health care, transportation, housing and dozens of other programs.

"Before all these calculations can begin in earnest, heads must be counted. And the 2010 census looks to pose a greater challenge than those of decades past.

"The wave of foreclosures has pushed hundreds of thousands of families out of stable homes with known addresses, making them more difficult to track down. Some people are living with friends, crowding into motel rooms, moving from one rental to the next or camping out in cars." Are they going to catch those people?, asked Kimball Brace, president of Election Data Services.

"Census employees recently spent months scouring every corner of the US – on horseback and by boat when necessary – in quest to identify all the places 'where people live or could live,' said Gabriel Sanchez, who directs the bureau's efforts in Texas, Louisiana and Mississippi.

"Mr. Sanchez's job includes counting residents of the most remote shanty towns along the Texas-Mexico border – places with no streets, let alone addresses – and communities populated mostly by illegal immigrants 'who do not want to be found by the government,' he said.

"The 2010 census will cost a record $14 billion, which includes some unprecedented steps to reach immigrants, both legal and not. For the first time, the bureau will mail census forms in Spanish to 13 million households. It is buying television, radio, print or online ads in 28 languages (up from 17 in 2000), among them Dinka spoken in south Sudan; Khmer, spoken in Cambodia; Teochaw, spoken in parts of China and other Asian nations, and Wolof, spoken in Senegal.

"This year's form will be among the shortest in history, with just 10 questions, to make it less intimidating."

"No questioning will address respondents' legal standing to live in the US In decades past, citizenship status was asked on the long-form census, which went to a sampling of households, but that form was discontinued this year because the Census Bureau already gathers much of the information in separate community surveys.

"Some critics of the census are angry about the lack of any attempt – this year or in years past – to classify undocumented immigrants separately. They carry the same weight as anyone else when congressional districts are redrawn even though they can't vote.

"US citizens in one state should not be losing representation in Congress to illegal aliens in another state,' said Ira Mehlman, a spokesman for the Federation for American Immigration Reform, which advocates tougher measures to stem illegal immigration.

"His group calculates that if the undocumented were left out in 2010 in California, Texas, Arizona, and Florida would all lose seats while Midwestern states such as Indiana, Iowa, Michigan and Missouri would gain."

The over-capping fact is that the world and its population are being re-scrambled according to new structures of which we are still but dimly conscious.

W. Krehm

telligences theory says the mind is better thought of as 'a number of relatively independent computers rather than one general purpose computer.' It posits that human beings possess many different types of intelligence, from linguistic, to mathematical, to musical and many more. He even finds place for existential intelligence, which he deems 'the intelligence of big questions.'

"In an educational setting, that natural fallout of his multiple intelligences theory is increasingly individualized instruction.

"That practice dictates educators should learn as much as they can about each student, teach in the specific ways so they can learn, and assess in what ways that students can show their knowledge. It also leads to finding a variety of ways of teaching a single topic.

"Gail Baker is a longtime follower of the Harvard professor's research. She is also director of the Lola Stein Institute, the research and development arm of Toronto's Hesche Jewish day school, which hosted the recent symposium at which Mr. Gardiner spoke."

A Plethora of Teaching Approaches

"The school's curriculum, modeled after Mr. Gardiner's theories, moves beyond rote learning to focus on big questions, such as how students fit into Canadian society, Ms. Baker said – and teachers deliver material in a plethora of fashions.

"'We can stand up at the front and talk. We can start with a piece of art. We can start with kinesthetic activity. There are so many ways as entry points and the more ways you do it, the more opportunities you're providing for children to access that information,' she said. It's no longer acceptable to take a history text-book and just rhyme off the causes of World War Two and what led up to them. That's just not acceptable in good schools any more.

"Stanley Katz, an expert on cultural policy at Princeton University who taught Mr. Gardiner in his Harvard days, says his former student has been a great advocate for art education by showing how children learn aesthetically as well as logically. This is a natural result of a theory that promotes teaching to the individual student, not the classroom as a whole.

"'This is of course diametrically opposed to what's done all over the world,' Mr. Gardiner noted. 'Everybody's forced to go through the same lens, the same eye of a needle, and if they can't learn that way, tough noogies.'"

Our readers will have grasped that what has gone on in most of our universities over the past few decades is far more destructive. What had already been learned about the need for keeping track of the government's investment in physical capital as had been learned the hard way during World War II and applied in the case of governments' investment in physical investments by the government in the US in 1996 and in Canada to a partial extent in 2002 to prevent the breakdown of the international financial system. However, after the World War II Washington had sent hundreds of economists to Japan and Germany to study the destruction of the war to foretell how long it would take these former great trading nations to resume such roles. Some sixteen years later one of these American economists, Theodore Schultz, published his conclusion that their forecasts had been so wrong because they had concentrated on the physical destruction during the war, but neglected the importance of the highly educated, trained and disciplined work forces

Continued on page 18

Vive the "Dominant Revenue"

"All of the chamber's Democrats and independents voted in Judge Sotomayor's favor except for ailing Sen. Edward Kennedy of Massachusetts, who was absent. Among Republicans, the vote was nine in favor and 31 against.

""I'm filled with pride in this achievement and great confidence that Judge Sotomayor will make an outstanding Supreme Court Justice,' Mr. Obama said after the vote. Judge Sotomayor's confirmation amounted to 'breaking yet another barrier and moving us yet another step further to a more perfect union,' he said.

"The Senate acted in line with the White House's timetable for confirmation, an achievement for Mr. Obama as Congress takes a slower approach to his health-care and climate-change initiatives.

"Chief Justice John Roberts is scheduled to administer the two oaths of office on Saturday morning to Judge Sotomayor at the Supreme Court building. She will then become the 111th person and third woman to serve on the high court. Her formal investiture was scheduled for September 8, one day before her first public appearance on the bench, when the court sits for a special summer argument to consider striking down limits on corporate political expenditures.

"Republicans joined Democrats in citing Judge Sotomayor's life story as an example of the social mobility America offers.

"Her curriculum vitae in some ways mirrors that of the last justice confirmed to the Supreme Court, Samuel Alito, who was approved in a 58-42 vote that was also largely along partisan lines. During his 2005 confirmation hearings, Democrats criticized his membership in a conservative Princeton alumni group that was critical of affirmative action efforts. This time it was Republicans who criticized Judge Sotomayor for her former membership in a Latino advocacy group, the Puerto Rican Legal Defense and Education Fund, and for lectures in which her aspirations for Latinos crossed into 'racism,' as Sen. James Inhofe, R., Okla.) charged Wednesday.

"Democrats said her 17 years of experience on the federal bench, where she compiled a conventional, if liberal leaning, judicial record, coupled with her working-class background, would equip her to understand the real world impact of judicial decisions. Republicans, however, seized on the word Mr. Obama used to describe a quality he had sought in selecting her – 'empathy' – as evidence that he expected his nominee to skew legal cases to favor minorities.

"Asked at her hearings whether she would employ empathy to reach decisions, Judge Sotomayor flatly said no. On Thursday Mr. Obama himself avoided the word, saying that Judge Sotomayor would ensure that 'whether you're a mighty corporation or an ordinary American, you will receive a full and fair hearing,' and that 'the outcome of your case will be determined by nothing more or less than the strength of your argument and the dictates of the law.'

"Republicans claimed a consolation prize in discrediting the president's appeal to judicial empathy. Should Mr. Obama have the chance to fill another high-court vacancy, 'I don't think we're likely to hear that term,' said Alabama Sen. Jeff Sessions, the Judiciary Committee's ranking Republican."

Long live the "dominant revenue" – unmentioned, unrecognized but controlling the movement of the wooden figures on the public stage.

W. Krehm

Number-crunching as Opposed to Analysis

The following is from a communication sent to Connie Fogal, at the time in the early years of the 2000s when she was leader of CAP. It deals with the function of the central bank.

To begin with nothing personal is implied in the use of the term "number-crunching." It happens to be one of the afflictions of our age. A high-tech culture based on a compulsion ever to expand has become the format of our lives. Most folk, accustomed to numbers as the prods keeping them on the course prescribed for their existence, are innocent victims rather than villains in this vast disinformation ploy.

Such "number-crunching "slams and bolts the door against the very possibility of serious information." It starts out by identifying the "economy" with the "market" on which everything to really count must be traded. Trading is envisaged as taking place not on the markets of this real world that are more and more run by huge international corporations, but in an idealized "pure and perfect" market where all actors are of such minute size, that nothing that they can do or leave undone can possibly influence prices. From this model the existence of equilibrium points – such as a flat price level is deduced, though it is clearly incompatible with the real world around us.

The very term "inflation" is misleading because it covers upward movements of price indexes due to completely different causes. Prices moving up may indeed be doing so because of an excess of demand over supply. That is the proper use of the term "inflation." However, prices can go up because both physical and human investment by governments essential to the welfare and of our exploding population and paid for by taxation. That inevitably results in a deepening layer of taxation in price. To deprive society of such essential services to keep prices flat is a barbaric, inhuman thing. That however, has been the main agenda of official economic doctrine of the past three decades.

But if the government consents to its central bank raising interest rates to keep prices flat or to balance a budget that makes no distinction between government spending for current purposes and public investment, then it either doesn't know what it is doing. Or worse, still, it doesn't want the public to know what it is doing. Our universities, press and parliament have been increasingly denied information on such vital matters, and reduced to number-crunching. Number-crunching can be defined as an absorption in a statistic to the complete disregard of the very different factors that may be contributing to its movements. The main damage inflicted by number crunching is that it diverts public attention from the destruction of institutions in which the democratic achievements of the past have been lodged. That was notably the case of the monopoly of the monarch in coining and recoining the money of the land. That was defended under monarchs such as Charles II of England, but as Karl Polanyi has shown, even feudal governments could in running their realms defend the social interest against the rapacious up and coming capitalist class.

The prerogative of the feudal monarch in coining gold and silver money in the fullness of time was transmuted into the prerogative of democratic government to

Education *from page 17*

coming through the struggle almost intact. From this he deduced what was probably the most important lesson of the war – that investment in human capital is the most productive a government can make. Its mere expenditure tends to be a further investment. The children of educated parents tend to be more readily educated, healthier. Britain is still getting a return on what it spent to teach Isaac Newton algebra.

Yet today what was done in recognizing the investment of governments in physical capital was recognized as such and resulted in restating what had been treated as a government debt as capital investments already largely prepaid. Today that remains to be done with the investment of governments in *human* capital. Elsewhere we have carried an understated figure for our governments' still ignored investment in human capital to amount to at least 3.5 trillion dollars in the US and approximately one tenth of that in Canada. That is enough prepaid investment to start the world economy functioning once more – but of course must not be squandered.

W. Krehm

Letter to the Editor: Budget Bust

I loved most of Alice Klein's Budget Bust article but I wish to take issue with one statement that she made which is an essential premise in part of her argument.

She said that "the Tories" will "fritter away our future spending power (which is what deficit spending is all about)." This is true *only if the money for the deficit comes from the moneylenders in our society*. And it is only true if the Liberal or NDP or Green parties, should they achieve power singly or in coalition stay inside the same box as the Tories, Liberals and Ms. Klein.

But it doesn't have to be that way. Unfortunately, in this instance, we are a species that relies on our beliefs (often false) for decisions and planning. When we step outside of the box of our usual beliefs, then new solutions become apparent. It is ironical that I am accusing Ms. Klein from *NOW* magazine of staying inside the box but that is exactly the case for this part of her economic argument.

In our economic system, money is largely debt. But the economic main stream media (including *NOW*) doesn't get it and usually won't try.

If the government of Canada owes money to the Bank of Canada, the debt is interest-free and repayment in the future is a non-issue. But if the government of Canada owes money to the private moneylenders (such as the banks), there is also interest charged and, indeed, that interest is what created over 90% of Canada's debt in the past and is what will steal from our future as predicted by Ms. Klein.

I recognize that these may be difficult concepts to grasp for many people at first glance. If it is hard for people to wrap their heads around these ideas, it is probably not because they are hard ideas to understand but because they challenge existing beliefs.

I urge Ms. Klein and others to step outside the box and look at this issue with fresh eyes and to suspend their initial disbelief. To aid in that, visit the website for *Economic Reform* www.comer.org, and watch the video *Money as Debt*.

Herb Wiseman

share in the profit of the private banking system. That was known historically as the government's right of "seigniorage." It took the form of the private banks redepositing with the central bank a portion of the deposits they took in from the public with the central bank. And on these "statutory deposits" the central banks paid no interest. And the government in Canada received the profits of the Bank of Canada in the form of dividends – for the government was its sole shareholder since its nationalization in 1938. That nationalization and those cost-free statutory deposits of the banks was a recognition of the assignment of the money creating powers of the government to the banks.

I have often wondered out aloud what form the next bank bailout from their heightened speculations. The answer has already come from the German and other European central banks paying the private banks interest on the statutory reserve under the name of the "banks' seigniorage." By that society is already in the process of being deprived of the memory of another key institution embodied in the language. The immediate efforts of those who insist on a "policy" on the debt expressed as a percentage of interest to be paid by the central bank to the banks for shifting from government debt to it, are not likely to lead to immediate results. Better immediate results could be had by insisting on the provisions still in the *Bank of Canada Act* (subsections of section 18), that allows the Bank to hold both unfunded and funded debt of the central government and the provinces. Even talking in terms of the Bank of Canada paying the banks interest on its transfer of federal debt redeposited with the BoC, surrenders the vital notion of government seigniorage. At the very time that the European central banks have brought in their notion of "bank seigniorage," it doesn't make sense for monetary reformers in Canada to be surrendering key institutional assets for monetary reform for the indulgence in a bit of number-crunching.

On the subject of valuable institutional assets, you may remember I promised our

Cross-currents in Deep Offshore Oil Finds

Like other oil-rich countries, because of the decline of onshore oil production, Brazil is torn between a dependence upon foreign technology and capital to exploit the deep new oil fields being discovered offshore and the trend towards reserving a larger share of the eventual product for the Brazilian state on nationalist grounds. *The Wall Street Journal* (01/08, "Brazil Claims Stake in Oil Find" by John Lyons) describes the resulting dilemma: "Sao Paulo – Brazilian President Luiz Lula da Silva announced government plans to play a far bigger role in exploiting newly discovered oil reserves, a bid to grab a bigger share of the profits and fund an ambitious development agenda.

"Calling it an 'independence day' for Brazil, Mr. da Silva said in a radio address Monday that his goal was to make Brazil richer, more developed, from the scientific point of view, from the educational point of view, from the point of view of social policies, all of this because of oil.

"To make good on his promise, Mr. da Silva will need to succeed where generations of Latin governments from Mexico to Bolivia have failed: Turning vast natural resource wealth into an engine of development. Brazil, with some of the world's biggest stores of iron ore and silver, has among the world's widest rich-poor divides. With the new oil discoveries, 'God has given us another chance,' Mr. da Silva said recently.

"In addition because the new fields lie miles beneath water, rock and shifting salt, they pose a new technological challenge that will require collaboration to overcome. Brazil may not attract the help it needs unless it offers partners more lucrative terms.

"Under the proposal, which must be approved by Congress, Brazil's state-run oil firm Petroleo Brasileiro SA, or Petrobas, will be guaranteed a dominant role exploring and producing crude in plentiful offshore fields believed to stretch along 500 miles of Atlantic coastline. Brazil says the find holds up to 50 billion barrels of hydrocarbons, enough to lift Brazil into the major leagues of oil-producing nations.

"That would make Brazil the latest in a string of oil-producing nations from Ecuador to Russia to relegate the world's major oil firms to supporting roles in oil production. Under the proposed rules, such firms will participate as business partners of Petrobas, rather than as owners of concessions to exploit individual fields as is the case today.

"To guarantee a bigger draw for public coffers, the federal government will become an automatic shareholder in new wells, receiving a share of the profits and direct ownership of a portion of the oil. Profits are to be funneled to a special investment fund bound by law to invest in development projects. Brazil will create a new company, to be called Petrosal, to oversee production in the region.

"Brazilian officials say the government's bigger role reflects Brazil's rising technical and relatively low risk in finding high-quality crude in the fields. Some Brazilian oil officials have taken to calling the drilling risk as 'near zero' – a strong claim even in an era of relatively reliable geological imaging and other exploration technologies.

"The realities of Brazil's energy reserves have changed profoundly as have the risk-reward ratios,' Minister of Mines and Energy Edison Lobao said.

"Shares of Petrobas fell Monday, in part on concern that the government will take a bigger ownership stake in the company.

"The first field discovered in 2007, called Tupi, has between five billion and eight billion barrels, making it the biggest single Western hemisphere find in at least three decades.

"Some observers question Brazil's basic assumption that recovering the oil is a sure thing. B.G. Group PLC of the UK, one of the oil firms with a pre-existing concession to develop offshore Brazilian fields, said last month that it failed to find hydrocarbons at its Corcovado-2 well. That followed Exxon Mobil Corp's July dry well. Brazil has said most of the test wells drilled by Petrobras have hit oil.

"Congressional debate over the plan will be heated. Some opposition congressmen said a bigger state role will create opportunities for corruption. Mr. da Silva, however, commands major support in Congress."

And thus the tug goes on.

W.K.

VISIT THE COMER WEBSITE
www.comer.org
Pass word of it to
your friends.

Saskatoon friends to track down precedents for the Bank of Canada lending money to the provinces and municipalities. In my preliminary reading of the back issues of *Economic Reform* for the second volume of Meltdown that our visit in Saskatoon encouraged me to undertake, I have come across this forgotten gem. This is a footnote in the *ER* of October 2000, page 6, of an article entitled "O O Canada – The Central Bank Stands on Guard for Thee": "In our last issue we reported the attempt of the Saskatchewan Finance Minister, Mr. Eric Cline, at the suggestion of the local COMER chapter, to persuade Mr. Thiessen (governor of the Bank of Canada) to refinance maturing debt at low rates against federal guarantee. A letter signed by Mr. Thiessen was received saying the BoC does not make such loans because of their inflationary effect. At that point your editor was enlisted as assistant researcher and came up with loans made by the BoC reported under the heading of 'Less Liquid Assets – Provincial Municipal Securities amounting to $14.9 billion in January 1999, up from $2.6 billion in October 1989.' Mr. Cline and COMER have written the BoC for an explanation of the discrepancy with the signed statement of the Governor along with a breakdown of the figures so that we might judge why they presumably were not inflationary. To date no reply has been received." "In this connection we were intrigued by a column in the *G&M* (16/9) of Madeleine Drohan, 'Canadians Reveal Shocking Ignorance of Central Bank.' It tells of a survey commissioned by the BoC on public attitudes toward the bank. '43% of those surveyed cannot even hazard a guess at what the BoC does.' Until a convincing rectification of Mr. Thiessen's erroneous reply to Minister Cline and COMER comes in, we must add the Governor himself to that 43% of Canadians who were clueless about what the Bank does and doesn't do."

Your faithful sub-searcher,

Bill Krehm

BRIC — Hitting the Head or the Wall?

The Financial Post (08/7, "BRICS Hold Up the Wall" by Alix McMullen) reported: "The world has been anxiously awaiting signs that China, along with other emerging market economics will emerge as the new drivers of global export demand to replace the once spendthrift US consumer.

"In a new report, Goldman Sachs Group Inc. economists say the BRIC nations – Brazil, Russia, India and China – can do just that and predict the four will account for half the globe's consumption growth in 2010.

"The investment bank said China would shine particularly brightly, likely accounting for 30% of that growth next year. That exceeds the combined growth of the G3 – US, Japan and Germany – as they crawl out of recession.

"Goldman, which coined the term BRIC in 2001, said the emergence of the BRIC consumer is an important development that will create demand and hence support the export markets of developed economies.

"'As the G3 countries face a slow and difficult recovery, final demand will need to rise in the rest of the world to sustain global growth in the future,' the Goldman economists said. 'The world can look to the BRICs to increase their contribution to global domestic demand through higher consumption.'

"The report said consumption in the BRIC economies would be supported by a shift in spending powers from the richest countries toward a growing middle-income bloc in the emerging markets. Consumption would likely receive a further boost when the rapid economic growth in China and India feeds through to the rural population.

"As these economies develop, the type of goods they consume is also predicted to gradually transform away from low-value-added products, like agricultural goods, to those at the higher end, such as cars, office and telephone equipment.

"The Goldman economists estimate that Chinese retail sales, a key indicator of consumption, rose 17.6% in the year ended June, with food and beverages products posting the biggest gains. It said retail sales in Brazil, while lower than in 2008, remained well supported and would likely increase in the third quarter.

"In Brazil, retail sales have recovered substantially, thanks to government tax breaks, monetary and fiscal policy stimulus, and the resumption of credit lending to households,' the economists said.

"India does not measure retail sales, but individual components, such as vehicle sales are used to gauge the appetite for consumption. Goldman said car sales had picked up markedly and were now selling faster than before the crisis.

"Of the BRICs, India is the clear laggard in penetration of goods,' the report said. 'However, as the middle class continues to grow and consumer expenditure rises, there is plenty of room for increased consumption."

"Russia, after years of strong growth, was the only BRIC country where retail sales growth had suffered. Sales in the year to June fell 6.72 % on the back of a sharp fall in non-food products.

"But while most agree the BRIC countries will have an increasingly important role to play in the global economy, not all are convinced they can drive demand on their own, particularly China where much of the world's hopes are pinned.

"Paul Biszko, a senior emerging market analyst at RBC Capital markets, said China needed demand to pick up externally before domestic demand could prosper.

"'It is still an export-driven economy, not an internally-driven economy where exports account for the dominant share of their growth outlook, so for the world to be relying on them as a consuming nation, that view's a little bit misplaced,' he said."

China, too, might make up the shortfall by spending-investing the vast earned human capital that it of all nations, has stored up but is not recognized as capital assets. When spent, a great portion of the expenditure is actually further social investment since the children of educated parents tend to be more readily educated, healthier, and better adjusted than those brought into the world by uneducated folk.

BRIC, no less than the developed countries have crucial need of accrual accountancy that will recognize human investment as much of the world did under great duress with physical investment in the 1990s.

At this point we can refer you to the abundant literature we have produced supporting the great research done by Theodore Schultz in reaching the conclusion from a gigantic US government project at the end of the Second World War. The most comprehensive details are to be found in the three volumes of our *Meltdown* book series that have already appeared.

William Krehm