THE JOURNAL OF THE COMMITTEE ON MONETARY AND ECONOMIC REFORM

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$3.95 Vol. 21, No. 9 • SEPTEMBER 2009

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Romanow Speaks — As Always, It Is Worth Listening

Roy Romanow hardly needs an introduction. As former premier of Saskatchewan and commissioner on the future of Health Care in Canada, he has always espoused the cause of those getting a bum wrap in this country's distribution of rewards and neglect. Currently Mr. Romanow is chair of the Institute of the Wellbeing advisory board.

The following contribution appeared in *The Globe and Mail* (03/08) under the heading "How to make recovery quicker and less painful for those hurting most."

"The Bank of Canada recently declared an end to the recession. There's a world of difference, however, between and end to economic decline as measured by GDP and a real recovery as felt by Canadians. And when we look behind the numbers, we can't avoid the fact that the costs are profoundly unequally shared, as those who suffer most will be those who can bear it least – unemployed and poor Canadians.

"History has a lot to tell us about the difference between the technical end of a recession and real economic recovery, and the consequences for lower and middle-income Canadians.

"A recently released report, The Economic Crisis through the Lens of Economic Well-being, points out that in each of the past two recessions, lower and middle-income families experienced much larger losses of income proportionately than higher-income households. In the 1982-3 recession, the market income of the bottom 20% per cent of households dropped by 38 per cent and that of the middle 20 percent dropped by 13%, while the top 20% of households lost just about 3%. In the 1990-93 recession, the bottom 20% lost 74% of income and the middle 20% lost 19% compared to 5.1% for the top 20%. This means that whether the depression ends now or later, recovery will be longer and slower for low and middle-income households.

"Connecting the dots between unemployment and poverty, the report also reveals that during the recession of the 1980s, the unemployment ratio grew by 4.4 percentage points while the poverty rate went up by a smaller 2.4 percentage points thanks to the impact of Canada's relatively strong social safety net. During the recession of the 1990s, however, unemployment rose by 3.9 percentage points but poverty increased much more – by 4.1 points. That change shouldn't surprise anyone as it coincided with significant cuts in EI coverage and benefits – the safety net designed to cushion Canadians from the worst effects of economic downturn. Even though the unemployment rate started falling in 1994, poverty kept rising until 1997 – three years later.

"Poverty is expected to grow in step with unemployment in this recession as well. EI is even weaker now that it was in the 1991 recession, and the impact of those cuts has been magnified by a weakening of welfare in most parts of Canada. To put it bluntly, it is much more difficult to avoid becoming poor in a weakening economy in Canada today than it used to be and it is much more difficult to climb out of poverty than it used to be. The report suggests that unemployment will continue to climb to 10% in 2010, with the poverty rate rising to more than 13% – a level our country hasn't seen since 1998.

"From the public there are two priorities for government action. First, governments must continue to offset the shortfall in private-sector spending that prevents our econ-

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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

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

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***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.

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.

Romanow *from page 1*

omy from operating at full capacity. This is no time to become complacent and assume that just because GDP may be picking up a little, the market economy will take care of everything. It was that kind of thinking that got us into trouble in the first place.

"Second, since recessions primarily hit the unemployed hardest and longest, it is vital that governments support individual Canadians who lose their jobs through income-supplement and retraining programs to meet their needs. The system we now have simply isn't up to the task and fixing it is going to require more than tinkering.

"In short, ongoing government stimulus and support for both individuals and the economy is still very much needed if we are to avoid the extended periods of high employment and even higher poverty rates that have followed previous recessions.

"Canada has already by lowering interest rates and injecting massive stimulus into the economy to ensure an even higher poverty than most had predicted. It now must demonstrate that it has learned how to make the recovery quicker and less painful for those who are hurt the most."

Since Mr. Romanow penned these eloquent, and highly humane, lines, the New York Stock Exchange has provided evidence that it, too, the spirit of Obama notwithstanding, has no intention of standing still. Elsewhere in this issue we publish the report of what certainly must be one of the greatest construction efforts still under way on this continent – a huge Rapid-Trading Hub in the New Jersey suburb of Mahwah equipped to house the equipment for it in an old abandoned quarry.

There is another similar Rapid-Trading center of NYSE going up near London in England.

This will allow the continued dizzy expansion of trading that must continue increasing because it dare not, cannot, stand not increasing at an ever accelerating pace, to support its forward lean, while hopefully avoiding collapse. That this should happen at the very time when our banks and their brokerage departments have been so utterly dependent on the largesse of the government should strip us of any possible illusion of those who run this show.

I resume my direct quote from the *WSJ* article: "A rogue firm engaging in aggressive trading could destabilize parts or even all of the market, Mr. David Shillman, associate director of the Securities and Exchange Commission's division of trading and markets, said. 'Unfettered access by unregulated entities into a market where trades can ripple through multiple markets can raise the level of systemic risk. The very high frequency traders could be doing more of these activities that could go awry.'

"SEC officials are particularly wary about 'sponsored access,' in which registered brokers lend out their identification numbers to high-speed trading firms. That effectively allows the firms to trade using a broker-dealers' code, helping them remain anonymous. A rogue firm engaging in aggressive trading could destabilize parts or even all of the market,' Mr. Shillman said.

"'Most high-frequency traders provide liquidity to the market, and that is a good thing,' said Larry Harris, a finance professor at the University of Southern California and former chief economist at the SEC.

"Just as traditional stock investors used to race to the phones to place an order based on a hot tip, today's new breed of high tech wizards are deploying ever-faster equipment to make money on fleeting moves in the marketplace.

"Most worries about high-frequency trading aren't focused on established players such as Goldman Sachs Group Inc., hedge fund firm Citadel Investment Group or high-frequency trading specialist Getco LLC. Rather, critics are more concerned about smaller and newer firms operating in the shadows, with little regulatory oversight.

"The NYSE has largely kept its facility under wraps, even keeping the exact location a closely guarded secret. Executives recently made oblique references to the company's plans, describing them as 'critical' to the NYSE's future.

"The NYSE is seeking to stem a slide in market share from more than 80% in 2004 to about 40% this year, according to data from Equity Research Desk, a research company in Greenwich, Conn. Second-quarter earnings are expected to slide 40% a share, according to a survey of analysts by Thomson Reuters.

"The NYSE started taking orders for space in the nearly 400,000 share-foot Mahwah facility, internally dubbed Project Alpha, this month. The exchange expects to attract everyone from large Wall Street banks to traditional brokerages and hedge funds.

"The idea behind the site is to get firms' computers as close as possible to the trading site – trades here are calculated not in milliseconds but in microseconds, or millions of a second."

And now who is saying that Wall Street is being given a hair-cut and brought into civilized society?

Back to Romanow

In the light of this our proved champions of social justice – and among these Mr. Romanow ranks high – must bring to the struggle still more powerful weapons for the popular cause. We will mention just a few. They all are essential parts of our history, which has been sanitized to suit the interests of those who determine what is to be remembered and what buried as though it never existed.

1. The Bank of Canada which was nationalized in 1938 by buying out some 12,000 private shareholders at a good profit, must be used to finance capital projects of the federal government. When this was done during WWII and for some two decades thereafter, the interest paid by the government to its central bank (less a small handling charge) came back to it as dividends. There is still an unused provision in the *Bank of Canada Act* for the provinces to use the BoC to finance its capital projects through the central bank as well, but since the provinces are not shareholders of the central bank the bulk of their interest charges on such loans will not come back to them, but go to the central government. That however, clears ground for friendly arrangements between the two levels of government for sharing the interest savings thus ensuing between the two levels of government.

2. The municipalities are not singled out for similar treatment. But they can come in under the heading of "corporations" which they are. They do require as sponsor for the purpose either the federal or a provincial government, and hence the door is opened for similar arrangements. Up to now our municipalities have been left alone to meet the bulk of the economic costs of coping with the economic crisis on their own.

3. The *Glass-Steagall* law brought in under F.D. Roosevelt in the first year of his office after a bank moratorium of one month had been declared because the banks simply could not go on functioning. That barred the banks from taking over interests in the non-banking financial pillars – at the time, stock brokerages, insurance companies and mortgage companies. The reason was clear, Allow the banks access to these and they will make a bee-line for the cash reserves such companies need for their own businesses. And once they lay hands on these they use them as the legal tender base on which they raise castles in Spain of subprime and other questionable bank credit.

4. Almost one thousand years ago the Knights Templar returning from the Crusades brought to Europe accrual accountancy that they had learned from the Arabs. This entered every business transaction once through its outlay of money or credit "amortized" according to a fixed schedule and stretching roughly over the expected useful period of the investment, and then the current market value ("depreciated" to the current value of the investment). This not only helped enforce the Muslim religious principle that charging interest is not a sin, only if the lender shares in the risk of a venture. Accrual accountancy adopted in western and central Europe made possible the great voyages of discovery the Spaniards and Portuguese. and other Europeans. However, our governments in recent times have not only ignored, but violated it in keeping their own accounts.

Our Government's Bogus Accountancy

It was only in 1996 in the US when the US banking system having violated the restrictions of the *Glass-Steagall* law that prevented banks from taking over any of the non-banking financial pillars – stock brokerages, insurance and mortgage companies – and obtaining access to the financial reserves these non-banking companies needed for their own businesses, and brought on a major financial crisis, that President Clinton brought in accrual accountancy in the US federal government's accounts of its physical investments. That did away with Washington "amortizing" – i.e., writing off its financial outlay on a fixed schedule of the government investment, but depreciating the physical assets in a single year. This resulted in the presentation of a huge bookkeeping deficit that simply was not there, but served to drive up interest rates. Since buildings, bridges, and other physical assets were carried on Washington's books at a token dollar that made for some brilliant privatization coups for well-connected candidates, but also prolonged and deepened economic crises and left the government treasury seemingly empty of resources to assist the resulting bankrupt and unemployed.

In 1992, however, this world-wide situation threatened to bring down the world financial system, and after putting together the greatest standby fund to date to forestall a world financial collapse, the Clinton Government introduced accrual accountancy for its *physical* investments, Where there had appeared a grievous government deficit, there suddenly turned up ignored government assets when accrual accountancy was taken back to 1959 of some one trillion and a half dollars. In Canada, where the step was brought in under fierce resistance from the federal finance minister but on the insistence of the then Auditor General, a very imperfect version of accrual accountancy was brought in. In the two countries that, as though by magic, ended a financial crisis and replaced it with a boom that gave President Clinton his second term and the world its high-tech rally that ended in the high-tech bust in 1998.

What bearing has all this to the present seemingly endless gropings of the Obama administration under the guidance of leading bureaucrats of the Bush years? A most intimate one.

Possibly the most important lesson to have come out of World War II was that investment in human capital is the most profitable investment that a government can make. It resulted from Washington having sent hundreds of economists at the end of WWII to study the damage and predict how long it would be before Japan and Germany could resume being the formidable competitors on world markets they had been. Some sixteen years later one of these, Theodore Schultz of the University of Chicago concluded that he and his colleagues had been remarkably off the mark. This he attributed to their having concentrated on the physical destruction and ignored the importance of the highly educated, disciplined, and gifted work-forces having come through the struggle almost intact. But his genius did not stop there. He went on to conclude that the most productive investment a government can make is in its human capital. For a few years Schultz was feted and decorated, and then as though somebody pressed a button, he and his great conclusion were utterly forgotten. COMER seems to be the only ones who refer to him or his great law. Although what the world seems to be clamoring for is precisely a vast reinvestment in human capital, that will send the unemployed back to schools and universities to retrain for urgently needed employment to offer no less needed services.

Why then is there no connection between what was learned at a cost of many millions of lives and our present crying needs? For that the late French economist, François Perroux, developed a theory that explains why authorities are so ready to bury the most crucial lessons of our history. He called it the "dominant revenue" and runs as follows: in every epoch the class in the saddle imposes its own income as the "dominant revenue" that by its volume can be taken as a safe measure of the well-being of society as a whole. After the Napoleonic Wars, behind the high Corn Law tariffs, British landowners screwed their rents to the skies.

By the mid 1830s, the industrialists thriving on their introduction of John Watt's steam energy replacing human muscle in their factories took over and saw in free trade not only a chance of reducing sustenance wages still lower, but meanwhile setting a good example of free trade to their oversea competitors who had still not applied the high art of John Watt. So the "dominant revenue" of the day shifted to the industrialist. Adam Smith and David Ricardo had based their value theories one way or another on the average labour that went into the production of a commodity. That may have been fine when the workers of the land were illiterate, but became a social peril when they finally learned to read, and the country was swarming with socialist and anarchist refugees after their defeats at the barricades they had thrown up in just about every European capital. A basically different "dominant revenue" became a crying need. It came in at least three European capitals, quite independently and saw the amount of enjoyment the ultimate buyer derived from the consumption of a product, rather than the sweat of the producer in the factory as the source and measure of value. The magic of the formula leads inevitably to the "tinkering" that you refer to in your letter to the *G&M*.

You may remember that our paths have crossed before. COMER has one important initiative underway, and another planned in which you and your organization would be welcome to play as important a part as you may wish. One is an appeal to the federal court system to make full use of the *Bank of Canada Act* that is still quite intact on our law books. This is in the hands of our solicitor. Rocco Galati.

The other, still in the planning stage, is to endow a scholarship with at least one university that will not simply involve what COMER believes to be valid, but give voice to its critics, a comparison of the merits and demerits, but above all raise to the public attention whatever historical reference may be relevant to the present crisis. For, indeed, it is not one to be tinkered with.

William Krehm

Why "Waste" the Money on Training and Education?

Programs that cannot stand up under the light of day burrow under misused language and bogus accountancy. The latest instance of that may be what is happening at Kitimat until very recently being equipped for importing liquid natural gas (LNG) since wasn't it an almost universally accepted fact that we were running out of our natural gas and would soon be dependent on importing it from the outside? And before the shovels were even brought in new sources of gas at far greater depths were discovered so that the import ports planned are being transformed to export NLG based on natural gas discovered at far greater depths. This requires new technologies and huge additional investments not only in physical capital but investments in human capital involved in training and educating humans.

But let *The Wall* Street *Journal* tell the tale (10/08, "Apache to Fuel Asia's Gas Demand" by Ben Casselman): "Houston-based Apache Corp. has agreed to provide natural gas for export to Asia through a project in Canada, the latest sign that that huge gas discoveries in North America are reshaping global energy markets.

"Kitimat LNG Inc., the Canadian company planning to build the liquefied-natural-gas export terminal in Kitimat, British Columbia, will announce today that Apache has become the second major North American gas producer to sign on to the project. Last month, another Houston-based gas producer, BOG Resources Inc. signed a similar deal.

"If the Kitimat project is completed in 2013 or early 2014 as planned, it would be the only North American LNG export terminal south of Alaska. The terminal would be in the ideal location for serving Asia, where gas prices are higher than in the US because demand is stronger and sales contracts are usually linked to the price of oil, which is higher than the price of gas.

"'We're pretty excited about the potential to open up some other markets,' said John Crum, president of Apache's North American operations.

"Apache and other British Columbia gas producers are looking for buyers for the trillions of cubic feet of natural gas they expect to pump in coming years. Apache recently said it could drill as many as 3,000 wells in BC with the potential to produce 10 billion cubic feet each. Other companies active in BC include En Canada Corp., Devon Energy Corp., and industry giant Exxon Mobil Corp.

"The Kitimat project is still in the planning stages, and the deals with Apache and EOG are memorandums of understanding – essentially agreements to negotiate. Nonetheless, the agreements underscore the rapid shift in the North American natural-gas market.

"Just three years ago, most experts thought North American natural-gas production was in permanent decline and predicted the US and Canada would become major importers of gas from overseas.

"Instead, new technology led to the discovery of vast new gas fields from New York to Louisiana, sending gas production soaring and pushing down prices in the US to below $4 per British thermal units from more than $13 per million BTUs last summer.

"Most gas producers have said they believe low prices are temporary, the result of weak demand due to the recession. The Kitimat project, however, is one of the first signs that some in the industry believe there is a long-term over-supply of gas in North America.

"'We're confident that there's going to be plenty of gas available for export for a long time,' said Greg Weeres, vice president of Pacific Northern Gas Ltd., which is planning to build as pipe-line to supply gas to the Kitimat facility.

"The Canadian project originally was conceived as an import terminal that would receive liquefied gas from the Middle East and Australia, convert it back into a gas and transport it via pipelines to Canada and the Western US.

"But Kitimat LNG President Rosemary Boulton said the company, based in Calgary, realized about a year ago that new North American supplies made such a facility unnecessary. 'Suddenly North America is awash in natural gas,' Ms. Boulton said.

"So in September, Kitimat announced it would build an export terminal instead.

"Kitimat, which is backed by private-equity firm Denham Capital Management LP and others, isn't the first company to discuss exporting gas from North America. Last year, Chesapeake Energy Corp. said it had hired investment bankers to study exporting liquefied gas from the Gulf of Mexico.

"Chesapeake Chief Executive Aubrey McClendon said in an interview that he ultimately decided to focus instead on trying to boost demand for natural gas in the US. But he expects operators of existing facilities to look into converting themselves to hybrid import-export terminals.

"'I don't see how anybody can arrive at the conclusion that there is not a decade's long supply of natural gas,' Mr. McClendon said.

"The Kitimat facility will take about 700 million cubic feet a day of natural gas produced in Canada and supercool it to minus 256 degrees Fahrenheit, which converts gas to a liquid. The liquefied gas can then be shipped to overseas markets. Kitimat has the necessary permits for the project, but still has to raise the $2.5 billion to $3 billion to build it."

And it will need some highly educated and trained workers to handle the technology and economics of so complicated but promising an undertaking. These don't drop from heaven. They have to be educated and trained long in advance.

W.K.

SCORE BOARD

Cuba — Still Awaiting Obama Miracle

The Globe and Mail (1/08, "Cuba suffers through austerity measures" by Will Weissert, Havana) reports: "It's hard to find a spare tire in Cuba these days, or a cup of yoghurt.

"Air conditioners are shut off in the dead heat. Factories close at peak hours, and workers go without their government subsidized lunches.

"Cuba has ordered austere energy saving to cope with rising budget deficits and plummeting export profits. The Communist Party Central Committee yesterday lowered 2009 economic growth projections by nearly a full percentage point. The committee also announced that it was suspending plans for the first Communist Party congress in 12 years to deal with the financial crisis.

"A report in the official Cuban newspapers cited President Raul Castro as saying the island is struggling through a 'very serious' crisis and hinted that further belt-tightening is on the way. The government already has imposed conservation measures even as it continues to get free oil for services from Venezuela, fuelling rumors that Cuba is selling President Hugo Chavez's crude on the side to raise cash.

"More likely, the shortages result from a global recession that hit an already struggling economy still reeling from last year's hurricanes. President Castro scolded Cubans in a recent national address to work harder because they have no one to blame but themselves.

"Every bit of belt-tightening stings in a country where almost everyone works for the state and average wages are less than $20 (US) a month. The price of nickel, Cuba's chief export, is down more than 50% from last year, according to Toronto-based Sherritt International Co-operation, Cuba's energy partner.

"The company's oil production on the island was down 19% last quarter compared with the second quarter of 2008, mainly because Sherritt suspended drilling earlier this year when Cuba fell behind on its payments.

"The government and Sherritt have worked out a plan to pay down the debt, and the company says Cuba has been sticking to it. The situation could have spurred the mandatory energy savings. Neither the government nor Sherritt would provide further details.

"Beginning June 1, the government ordered energy conservation measures as part of a broader plan to cut the national budget by 6%. Central planners also announced yesterday they were revising their economic growth projections downward, to 1.7% from 2.5%. The island's economic woes began in earnest with three hurricanes last summer that caused more than $10 billion in damage and wiped out some of the food and grains the government had stockpiled to insulate itself from rising commodity prices. *Associated Press*

Switzerland — US Scores in Cracking the Swiss Bank Tax-shelters of Wealthy Americans

The same issue of *The Globe and Mail* carries a report of some progress in "opening a crack" in the fortress-like protections the Swiss government grants clients of this government's banks.

"Secretary of State Hillary Clinton and her Swiss counterpart, Foreign Minister Micheline Calmy-Rey, told reporters ahead of a meeting in Washington yesterday that the two countries had reached an 'understanding' in their dispute over the US Justice Department 's attempt to force Zurich-based UBS AG to turn over the names of 52,000 American account holders.

"The agreement was also revealed in a conference call involving lawyers and the federal judge in Miami who was to set to preside over the jurisdictional showdown between the two governments. Justice Department lawyer Stuart Gibson provided no details of the accord, saying they may come on August 7.

"The US government sued UBS for the names in February after winning a separate, but similar, legal skirmish with the bank. In that instance, UBS agreed to pay $780 million (US) and turn over data on more than 250 US clients in order to avoid criminal charges that the banks helped wealthy Americans avoid taxes.

"UBS's agreements to turn over that data represented an unprecedented breech of the financial secrecy laws that form the foundation of Switzerland's position as an international banking power. The second suit became too much to take. The Swiss government injected itself into the case, saying the US demands were illegal under Swiss law and a threat to its sovereignty.

"Ms. Calmy-Rey said she was 'very pleased' with the agreement. Still, the risk for Switzerland and other countries that offer low tax rates and legal cover is that the international investors on which they base so much of their national incomes begin to question whether these tax havens are truly safe.

"Washington is not alone in taking a more aggressive stand on tax havens. The group of 20 members, including Canada, has pledged to keep up clamping down on tax-dodgers around the globe.

"'If the Swiss can be broken, anyone can be broken,' said Reuven Avi-Yonah, a University of Michigan professor who has advised the US Treasury on international tax law. 'Other tax havens don't have the clout of Switzerland.'" ■

The NYSE's Gigantic Misreading of the Future

The Wall Street Journal (30/07, "NYSE's Fast-Trade Hub Rises Up in New Jersey" by Scott Patterson and Serena Ng) would seem to have put in an all-time bid for understatement. And before we have our little say on the matter, we will pay our tribute to both the mistiming and the proportions of their misreading of what lies ahead. In its dimensions it might suggest that it is a single-building effort to wrap up the depression in the building industry. We quote: "Mahwah, New Jersey: The future of the New York Stock Exchange is inside the red-brick building that is rising from the ground here about 35 miles from Wall St."

"Right now, the mammoth activity being constructed on the site of an old quarry is a largely empty shell with a jumble of high-tech gear. In about a year, the building is expected to house several football fields of cutting-edge computing equipment for hedge funds and other firms that engage in high-frequency trading, or use the computers and complex algorithms to trade at lightning speed.

"'When people talk about the New York Stock Exchange, this is it,' said NYSE EURONEXT Co-Chief Information Officer Staley Young. 'This our future.'"

And therefore beyond a doubt *your* future, dear reader. For, Obama notwithstanding, the matter seems to have been financed and hence passed muster with those who count.

"As trading goes increasingly electronic, the last bastion of floor trading is embracing high-frequency trading as part of its race to keep up with competitors such as NASDAQ OMX Group Inc. High-frequency trading now accounts for more than half of all stock-trading volume in the US as banks, hedge funds and institutional investors seek to gain an edge by trading before rivals.

"But even as the Big Board and other exchanges scramble to win more business, some regulators are getting concerned about the risks that high-speed potentially poses to the broader financial system. As trade flows at an ever quicker pace, a computer glitch at even just one firm could trigger a wave of selling that sets off huge losses across markets, some people worry.

"'Unfettered access by unregulated entities into a market where trades can ripple through multiple markets can rise to the level of systemic risk,' said David Shillman, associate director of the Securities and Exchange Commission's division of trading and markets. 'The very high frequency traders could be doing more of these activities that could go awry.'

"SEC officials are particularly wary about 'sponsored access,' in which registered brokers lend out their identity numbers to high-speed trading firms. That effectively allows these firms to trade using a broker-dealer's code, helping them remain anonymous. A rogue firm engaging in aggressive trading could destabilize parts or even all the market, Mr. Shillman said.

"These troubling scenarios haven't happened yet, although several high-frequency funds have been put out of business by erroneous trades, according to people familiar with the matter. The worry is that as speeds increase and more traders wield a rising hoard of cash, the risks will increase.

"The NYSE says it offers risk-management software to firms that trade on its exchange, but use of the software is not mandatory."

High Technology that Enslaves Rather than Frees

"Some practitioners say that rather than adding to risks, high frequency trading helps markets operate more smoothly by providing an ample, ever ready pool of shares or other securities when investors need them. 'Most high-frequency trading provides liquidity to the market, and that's a good thing,' said Larry Harris, a finance professor at the University of Southern California and former chief economist at the SEC.

"Just as traditional stock investors used to race to the phones to place an order based on a hot tip, today's new breed of high-tech wizards are deploying ever-faster equipment to make money on fleeting moves in the marketplace.

"Typically, high-frequency traders use computers to search through markets for signals that can give them an indication about which direction parts of the market will go. If gold is rising, oil is falling and the dollar is losing ground against the Japanese yen, for instance, that could mean automotive stocks are likely to rise for the next hour, based on historical patterns. The high-frequency will start putting in orders for shares of auto-makers at superfast speeds, turning around and selling them an hour later.

"Some firms trade only with their own money, while others trade on behalf of clients and investors. Others make money by facilitating trading activities, collecting tiny spreads between bid and offer prices and collecting fees exchanges provide market participation.

"Most worries about high-frequency trading aren't focused on established players such as Goldman Sachs Group Inc., hedge-fund Citadel Investment Group or high-frequency trading specialist Citadel Investment Group or high-frequency specialist Getco LLC. Rather critics are more concerned about smaller and newer firms operating in the shadows with very little regulatory oversight.

"Controversy also is growing over a practice known as "flash" orders, in which exchanges allow traders to briefly see and react to certain orders ahead of the rest of the market. The SEC is looking into the practice and is widely expected to ban it, according to people familiar with the matter. Exchanges such as NYSE, NASDAQ and Intercontinental Exchange Inc., or ICE, oppose the use of flash orders.

"The NYSE has largely kept its facility under wraps, even keeping the exact location a closely guarded secret. Executives recently made oblique references to the company's plans, describing them as 'critical' to the NYSE's future. When they discuss second-quarter earnings, set before the opening bell Thursday, those plans are likely to b addressed in more detail.

"The NYSE is seeking to stem a slide in market share from more than 80% in 2004 to about 40% this year, according to data from Equity Research Desk, a research company in Greenwich, Conn. Second-quarter earnings are expected to slide 40% from a year ago to 45 cents a share, according to a survey of analysts by Thomson Reuters.

"The NYSE's decision to build its own data center surprised some industry observers. In the past, most exchanges have rented out space to data-center providers. The NYSE is rolling the dice that it will become a go-to venue for high-speed space to other exchanges.

"The exchange is building a similar facility outside London, which will cater to clients who want access to oversea markets. The combined price-tag for the two data centers will be about $500 million, according to people familiar with the matter.

"The NYSE started taking orders for space in the nearly 400,000-square-foot Mahwah facility, internally dubbed Project Alpha this month. The exchange expects to attract everyone from large Wall St. banks to traditional brokerages and hedge funds. The NYSE won't say how many customers have signed up.

"The aim behind the site is to get firms' computers as close as possible to the trading site, helping to shave off tiny amounts of time – trades here are calculated not in milliseconds, but in microseconds, or millionths of a second."

We are left with only two questions.

1. How has this fitted in with Obama's plans for solving not only the still unsolved economic crisis?

2. Should Obama have given up on his plan to solve that problem by leaning on Bush's experts, and should it be a miracle arranged in heaven to solve this crisis in ways apparently unknown to President Obama?

Or has some expert in the Fed bureaucracy decided on a two-for one strategy, by which the NYSE mega-building projects revive both the building industry and Wall Street at the same time?

William Krehm

Deregulation and Globalization Leaves Yet Another Calling Card — Woes of Chinese Drywall

The Wall Street Journal (6/08, "The Prisoners of Drywall" by M.P. Mcqueen) is here to remind us that woes tend to come not single but in superimposed layers like the layered cakes of economic delight promised us.

If you have the strange belief that a possibly near-bankrupt builder is not there to make good what was promised and paid for, when he is in the same country and at arm's reach by the same courts, hearken to this later report of what house owners are up against when much of their house may have come from places at the other side of the globe.

"Shortly after buying their home in Cape Coral, Fla., in 2006, Keith and Denise Cramer noticed a peculiar acid smell they thought was wet paint. The odor never left.

"There were other strange occurrences. Chrome-plated faucets and showerheads became pitted or turned black. The central air conditioning unit faltered and failed. Their son, Gavin, suffered frequent ear and upper respiratory infections, and Gavin and Denise got rashes.

"The Cramers and thousands of other homeowners in Florida and elsewhere – now believe that imported Chinese drywall is making them sick and destroying their property. The drywall, which is used in walls and ceilings, is emitting sulfur compound gases that homeowners have described as giving off a sour or 'rotten egg' odor. Many blame the fumes for eye, skin and breathing irritation and nosebleeds, as well as the corrosion of copper pipes, electrical wiring and air conditioners.

"The Cramers say if the government tests conclude the Chinese drywall is a health hazard, they will be left with a difficult choice: 'We will have to either ruin our son's life by staying, or ruin our credit by walking away from the home,' says the 34-year-old Mr. Cramer.

"An estimated 100,000 houses across the country, most built in 2006 and 2007, may be affected, based on the 500 million pounds of Chinese drywall – also known as plasterboard or gypsum board – believed to have entered the US during that period. The drywall is being investigated by numerous agencies, including the US Consumers Products Safety Commission, the Environmental Protection Agency, and the Centers for Disease Control and Prevention, along with the health departments. Several are due to report their findings later this month or in September.

"If the agencies conclude a 'substantial' electrical, fire or health hazard exists, they could issue a recall or other action. More than 800 complaints from 23 states have been filed at the Consumer Product Safety Commission's Drywall Information Center.

"Experts estimate that it costs about $100,000 to pull out bad drywall and replace corroded electrical wiring and appliances and appliances in an average-sized home, and the problem is shaping up as a costly disaster for homeowners and the battered housing industry. Many homeowners are hoping the federal government will step in with some sort of aid similar to that provided for victims of hurricanes and tornados, as well as a moratorium on mortgage payments.

"Others are staking their hopes on lawsuits against builders and the drywall manufacturers and distributors. Many of the suits are being consolidated in federal court in New Orleans. But suing foreign-based manufacturers for liability is difficult and complicated, legal experts say.

"A few builders are already taking action. Lennar Corp. has set aside almost $40 million to fix 400 houses in Florida and is ripping out the drywall in many homes throughout the state, the Miami-based home builder said in a securities filing last month. Some other builders are making similar repairs.

"While Chinese drywall was initially thought to have been used mainly in Florida and Louisiana, complains have been pouring in from many other states. Colleen Nguyen, 41, of Virginia Beach, VA, says she, her husband and three girls moved out of their waterfront home built in 2006 and into a trailer last April for three months on the recommendation of their pediatrician, Their computers, phones and microwaves kept breaking down, and the circuit-breaker kept tripping, they say. They are suing their home-builder and drywall subcontractor. The cities of Virginia Beach and Norfolk, Va., recently banned builders from using Chinese drywall in construction."

"Certainly no home-run for the Chinese trade offensive.

"Ms. Nguyen says the family left their belongings behind in the house because the odor had permeated the bedding and upholstery. 'I won't expose my children to it until they can explain what it is,' she says. 'We have not had a bloody nose since the date we moved out.'

"One major manufacturer of the Chinese drywall, Knauf Plasterboard Tianjin Co., says its tests indicate that its drywall isn't harmful. Testing found that carbon disulfide and carbonyl sulfide are being emitted by some of its drywall, but not at levels that would damage health, says Phillip T. Goad, principal toxicologist and partner at the Center for Toxicology and Environmental Health in North Little Rock, Ark. The center is a private company hired by Knauf Tianjin that consults for corporations and government agencies."

W.K.

A Frosty Examination of Obama's Half-Year Score

In *The Globe and Mail* (4/08, "Obama's gambit leaves him much to lose" by John Ibbitson) comes to a goose-egg in his rating.

"Six months into his presidency, Barack Obama is all in.

"The 44th President of the United States has gambled his administration on getting health-care reform legislation through Congress. If the various bills before the House and Senate synthesize into one coherent and substantial set of successfully passed reforms, then Mr. Obama will have achieved something that has eluded presidents since Harry Truman.

"But inter- and intro-party wrangling have wreaked havoc with the time-line. The bill could fail. Health care isn't just health care. Health care is environment, health care is energy, health care is immigration, health care is education."

Excellently put!

"Failure could wreck everything.

"'It is absolutely crucial that the bill passes,' believes Darrell West, vice-president of the Brookings Institution, a Washington think tank. 'If health care fails to pass, Barack Obama goes from Superman to Clark Kent.' The name is unknown to me and probably to my readers.

"The President invited every Democratic senator to lunch today to celebrate his 48th birthday and stiffen their spines on getting a health bill passed. That meeting followed a weekend cabinet retreat, where the administration assessed its own performance after half a year. The report card, it must be said is mostly blank.

"Mr. Obama's claim that his $800 billion economic stimulus package prevented a severe recession from collapsing into depression is nonsense.

"By the administration's own reckoning, stimulus funds are only now beginning to flow into the economy. If anything saved us from the abyss, it was the previous administration's $700 billion (US) rescue of the banking sector, accompanied by trillions in loan guarantees.

"Outside health care, this administration's most important accomplishment thus far has been the taxpayer-financed rescue and restructuring of General Motors and Chrysler. But only time and the market will tell us whether that investment was inspired or foolhardy.

"The President would have to admit that he has thus far failed one important goal he set for himself: fostering bi-partisan – or post-partisan – amity on Capitol Hill and in the broader discourse.

"Instead, the Republican rump is waging a total culture war against the President and his administration, egged on by a conservative 'commentarial' that has gone beyond all previously known bounds.

"Last week, responding to Mr. Obama's misspeak on the racially charged controversy surrounding Harvard professor Henry Gates and the Cambridge Police Department, the uber-conservative pundit Glenn Beck accused Mr. Obama on Fox News of being 'a racist' with 'deep-seated hatred for white people or the white culture.' Fox declined to censure Mr. Beck or even disown the comment, saying he was entitled to his opinion.

"And over on CNN, Lou Dobbs has joined the ranks of the so-called 'birthers,' demanding that Mr. Obama prove he was born in the United States, though he has repeatedly stated that he was."

Treating the President Like a Border-crosser

"It would be funny, except 11 Republican members have sponsored legislation in the House demanding that future presidential candidates produce a birth certificate.

"But it is not the Republicans and their fellow travelers whom Mr. Obama needs to worry about most. His biggest challenge in government is reconciling the deeply divided Democratic Party.

"In Congress, senators and members from the liberal coasts are more or less offset from those from the conservative South. Power rests in the hands of moderates, many of them from the heartland.

"Changes between parties in the congressional balance of power are less significant than they appear, since these seats tend to rotate between moderate Republicans and conservative Democrats, who currently hold the balance of power.

"It is these so-called Blue Dog Democrats who are giving the President grief. They are nervous about the costs of the proposed health-care reforms and wary of the public insurance option that would compete with private insurers. For more than a week, the Blue Dogs stalled progress on the bill in the House Financial Services Committee and one of the most powerful figures in Congress, predicted to Politico.com: 'I don't think it would pass the House – I wouldn't vote for it.'

"The Congressional Democratic leadership's inability to resolve the tensions between conservatives and liberals within in its own caucus, while also persuading at least a few reluctant Republicans in the Senate to back the plan, has left the legislation in limbo as lawmakers prepare for their August recess.

"Senators and Representatives will now spend this month listening to unhappy constituents who are fed up with the current state of health care, but who fear that the proposed changes will only make things worse.

"Still, only terminal pessimists would predict failure at this point. There are powerful forces aligned in support of the legislation. Doctors and nurses are onside, as is big business, which is desperate for relief from skyrocketing insurance costs. Policymakers know that, unless the system is reformed now, it will collapse soon.

"We are further along than we ever have thought possible, believes Mandy Krauthammer, executive director of Doctors of America, which supports the president's health-care reform.

"Mr. West [of the Brookings Institute] is confident some kind of health-care legislation will pass, because the Blue Dogs know the political cost of failure. Even if the final product is badly watered down, he believes Mr. Obama will profit politically. 'People will give him the benefit of the doubt.'

"And the rest of the President's audacious agenda will be ready to roll.

"The Obama administration looks shakier at six months than it did at 100 days. But while momentum has slowed. it has not slowed, it has not stalled."

But what is woefully missing from this journalistic report, as from President Obama's view of the nation's and the world's problems and destinies is a knowledge of their histories, not just forgotten but suppressed. For a solution to the problems currently engulfing the planet were devised and partly applied successfully at critical junctures of fairly recent history.

Fortunately, *The Wall Street Journal* (08/07, "Deficit a Growing Concern for Public – and White House" by Gerald F.

Seib) arriving this morning has relieved us of the need of repeating ourselves once again, for it illustrates how even professionals have been deprived as though by surgery of their memories of crucial turning points of their own histories.

We quote: "More broadly, one in three ranked the deficit as one of the top issues facing government, placing it behind only jobs and economic growth.

"Of perhaps more immediate concern to Democrats, a poll out this week from the Quinnipiac University Polling Institute shows that the deficit is fomenting unease about the health overhaul the president is pushing. Voters said by 57% to 37% that they would be willing to drop a health overhaul if it adds 'significantly' to the deficit (which is, to be sure, something Mr. Obama insists he won't allow).

"These public sentiments are a bit surprising. Peter Brown, assistant director of the Quinnipiac poll, notes that voters haven't exactly showered rewards on politicians who have made an issue of deficits in the past. In 1984. Democratic presidential nominee Walter Mondale tried to demonstrate how serious he was about addressing the deficits that prevailed then by declaring he would raise taxes to deal with them. He was rewarded with an electoral loss of historic proportions, falling to President Reagan by 50% to 41%.

"Business maverick and third-party presidential candidate Ross Perot made a splash in the 1990s by talking about deficit-spending and promising he would 'get under the hood' of the federal government to erase it. That message made him a force for a while both in 1992 and 1996, but ultimately he couldn't use his fiscal responsibility gospel to challenge the power of the two major parties.

"Fast forward to 2009, and there was ample reason to believe the conventional wisdom at the start of this year. It held that that Americans would be prepared to simply forget about the deficit for a year or two while the government spent money to pull the economy out of the ditch.

"But maybe the conventional wisdom wasn't quite right. Perhaps the sheer size of the budget deficit has altered the normal public tendency to feign concern about deficits but quickly forget about them The deficit this year will be $1.8 trillion and next year will be $1.4 trillion, under the current estimates. The $290 billion deficit that prevailed when Mr. Perot went on his crusade seems a pittance by comparison."

What is most revealing in this research of a university organization, is that they roll over in total unawareness of a crucial happening between 1992 and 1996 years that they do mention, but not for the crucial accountancy change in the government's handling of its physical investments that allowed it to overcome a crisis that threatened to flatten the world economy. The vast US deficit that threatened to flatten the economy of the entire globe, had been brought on by the absence of any serious accountancy in its ledgers. The vast apparent deficit seemingly run up by Washington. had dealt with a huge apparent deficit that turned out to be due, not to overspending, but simply to the deplorable way in which the government kept its books. About a thousand years earlier the Knights Templar, a crusading had brought back to Europe from Saracen lands a crack double-entry system of accountancy – "accrual accountancy" – that had allowed the Muslims to keep track of their religious prohibition of charging interest for financing an enterprise unless the lender had shared with the borrower the risk of the enterprise.

Accrual Memory Loss

This "accrual accountancy" had made possible not only the success of Venetian Republic in trading with the Muslim world, but also the great voyages that led to the discovery of the New World and the sea voyage around the Cape of Good Hope to Asia, and much, much else. Its essence was to enter the particular deal in the ledger of the investor twice – once the money or credit put up to finance the enterprise – and that was "amortized" according to a preset schedule extending more or less to the likely life-span of the physical assets. The current value of the investment was noted according to its current market, and that was depreciated (from the Latin for price "pretium"), i.e., as the market would determine. That not only allowed the Muslim authorities to check what the local financiers were doing with interest billings, but gave partner partners, bankers and tax-collectors a reliable report on how the investment was faring. It inspired the great German poet Goethe to sing the praises of an accountancy system – probably the only instance of a poet choosing so prosaic a subject.

But our governments did not take as kindly to accrual accountancy – or for that matter any other system of accountancy that revealed how government investments were really doing rather than hiding that information.

To understand how that could come about we must move to France, and more specifically to the group of economists under the influence of Fernand Braudel, who were sociologists as much as economists. They were grouped around a publication called *La Revue Économique*, that unfortunately no longer exists because economic theory has become standardized to serve those in the saddle. I chanced to come in contact with that French group in a remarkable way. I had been impressed that economic theory was being controlled to serve the group in political power. To achieve this economists had to violate a basic principle of logic You cannot flap a principle of logic around as though it were a pancake. If I hold a loaded pistol to my head and press the trigger, I fall dead. From that, however it is impossible to assume that because I fall dead that I have suicided. It could have been a heart-attack or countless other non-suicidal causes. But these other causes were simply referred to by economists as "externalities" and the market is elevated as a self-balancing entity.

From my readings of history and economic theory and considerable business experience I reached the conclusion that price is only partly determined by the market, but increasingly by the growing importance of essential services provided by government and paid for by taxation. That growing layer of taxation that is not market-determined moves by its own laws and as the need for public services grows, the market itself becomes ever less self-balancing. I dubbed this the "social lien" and traced its behavior.

Nobody is simple-minded enough to believe that when he moves from a town of 20,000 to New York City his living costs will stay the same. But economists do just that, when humanity as a whole makes such a move. Nobody can keep track of the cities on all inhabited continents with a population of five million people and more. Greater Mexico City alone has 30 million inhabitants. Obviously such cities need far costlier infrastructures and cultural institutions unthinkable in a smaller town.

It is incredible that it was left for me to identify such "structural price increase" rather than simply an excess of market demand over market supply. I sent a lengthy manuscript to some 30 publications on economic theory throughout the world. This was purchased by *La Revue Économique*, which had Fernand Braudel on its editorial board and carried it in its May, 1970, issue as a 60-plus page article. It was in that way that a very productive, open-minded school of French economists came to my attention, and I to theirs. Only later did I come to understand why *La Revue* had snapped up my manuscript. Two French economists had sought to verify the claim of conventional economists that major price rises reflect a basic excess of demand compared with supply. Their quite independent researches in different locales and time periods. failed to turn up such a relationship. They concluded that there had to be another factor involved that had still not been identified. And then the postman brought my manuscript out of nowhere.

It was not long, as I burrowed through the rich independent economic enquiries that the independent thinkers among French economists had achieved, before I came across the work of François Perroux. For our purpose today his greatest achievement – absolutely indispensable for an understanding the current Obama performance – is his theory of the "dominant revenue." This he defined as the theory that presents the revenue of the economic group with economic power and can be taken as an index of the well-being of society as a whole. In Britain, during and after the Napoleonic Wars it was the large feudal land-owners whose rents from their lands were screwed ever higher behind high tariffs. But by the mid 1830s John Watt's steam engines replacing hand-labour in the factories had led to the industrialists achieving the repeal of the Corn Laws with free trade, which permitted the survival wages the industrialists paid their work force to drop steeply.

The dominant revenue worked in quite other dimensions as well. So long as the factory workers were illiterate, economists could do their reasoning with one version or another of the labour theory of value. Adam Smith used three different ones according to the purpose he had in hand. But when workers were learning to read, and a flock of highly distinguished socialist and anarchist leaders after their defeat on the barricades that had sprung up in almost every Central and Western European capital reached Britain as refugees. These included Karl Marx and Friedrich Engels themselves and family members of theirs were soon organizing open air meetings almost within earshot of Buckingham Palace. That ruled out labour theories of value as incendiary stuff. And then the economists shifted from the factories to the fancy consumers galleries where value was equated with the degree of enjoyment the consumers derived from a given product. No coincidence that marginal value theory arose within a few years from one another in at least three European centers.

It was a most revealing case of the "dominant revenue." A good example was its handling of unemployment, which was proclaimed simply not to exist. What was mistaken for it, was simply the workers deriving greater pleasure from leisure in their parlors than from a job at the wage offered.

Served up with a misplaced pinch of infinitesimal calculus to establish its credibility amongst the mathematical illiterate, it embarked on a mighty career that is performing yeoman services under Obama today.

The "Dominant Revenue" Lay in Shards

Our purpose for this grand detour that I have taken my readers is to note that amongst the dates that he cites as proof that cleaning up the deficit has been no help for aspirants to the US presidency, he mentions the period of 1992 to 1996, only to bring up Ross Perot's failure to attain the presidency by featuring the need to control the deficit, but wholly overlooks something far more momentous and relevant to Obama's quandary today. Roosevelt had had a good measure of luck in reining in the Depression largely because the "dominant revenue" lay in shards. Prominent industrialists like Thomas Edison and Henry Ford would have nothing to do with the defense of banking or bankers that had gone bust in their thousands by the time F.D. Roosevelt took over. And the first thing he did was to proclaim a bank moratorium that lasted a full month without a bank's doors open throughout the land. The only banker in the Roosevelt cabinet was not from Wall Street, but from Salt Lake City. Had there been a functioning "dominant revenue" in existence, it is a moot point that Roosevelt could ever had manage to put through his *Glass-Steagall Act* that barred the banks from acquiring interest in the non-banking financial pillars.

The reason for that law should today be clear rather than suppressed. Once the banks get their hands on the cash and near cash reserve set aside by these non-banking financial pillars for their own business, they automatically use it as money base for their own bank-money-creation.

During the 1980s the *Glass-Steagall* law was progressively disregarded and the Bank for International Settlements came to serve as the war-room to plan and execute the return of banking to the glorious freedom of the 1920s that had brought on the Great Depression. In 1988 the Bank for International Settlements (BIS), looked not to the liquidity of banks, but to their capital, that had, of course, become tied up in promising deals – the reader will note that stock brokerages, insurance, and mortgages – which started the present economic crisis were the non-banking pillars forbidden the banks by *Glass-Steagall* but had been disregarded with disastrous effects. So in 1988 the banks were allowed to load up with government bonds with nothing down after satisfying just the *existence* of their capital without a word about its *liquidity*. One thing led to another, and the BIS management overlooking what would happened to bonds bought entirely on credit with which the banks were overloaded if interest rates shot up to lick inflation defined as anything higher than a flat price level. Of course, the value of bonds acquired by the banks years earlier with far lower rates would drop. That is precisely what happened in 1992, when the Mexican banks closed their doors and shorted their own currency. BIS announced that interest rates would go up until "inflation" were reduced to zero. BIS, the US and Canada set up the largest standby fund – $51 billion (US) to prevent a collapse of the international credit system. It was not used, but the crisis so shook the confidence of President Clinton that he did the unthinkable – he finally paid heed to the urging of the government's auditors and brought in accrual accountancy into the government's books. This – taken back to 1959 – resulted in an additional $1.5 trillion of capital assets of the Washington government that had been left off the books. Moreover, unable to make a clear, forthright state of something that questioned the "dominant revenue" it appeared as "Savings." Savings, however, it was not since the term usually refers to cash or short-term securities of top quality.

In Canada the Auditor General, encouraged by the US measure, refused to approve the balance sheets of the federal government unless accrual accountancy was brought into its ledgers. But the Liberal government resisted – the "dominant revenue" had not surrendered. Finally, a compromise was reached with the Auditor General agreeing that since no new money had been brought into the treasury, it was not to be used as a reason for bringing in new spending programs.

However, that still leaves government investment in *human* capital out in the cold both in the US and Canada.

And undoubtedly the most important lesson learned from World War II was that human capital is the most profitable investment a government can make. It was a most costly lesson not available cheaply from correspondence schools. At the end of hostilities Washington lost no time in sending hundreds of economists in to Japan and Germany to study the wartime destruction and from it predict how long it would take before those two once great trading powers could reassume such roles. Some sixteen years later, one of these economists wrote papers to the effect that it was astounding how wide of the mark their forecasts had been. His name is Theodore Schultz of the University of Chicago and he attributed their failure as prophets to their having concentrated on the physical damage of the war, and overlooking that the highly educated, skilled, and disciplined work force had come through the struggle essentially intact. If we grossly understate our adaptation of the estimate of the physical damage quoted above and allow for the drop in the purchasing power of the US dollar and add one trillion as a gross understatement of the real investment we would arrive at a figure of $3.5 trillion in the US. Taking the usual 10% proportion of corresponding size of such major statistics for Canada we would come to some $350 billion for Canada.

A brief remark on the special nature of human investment by government. It should, of course, include such items as care and improvement of the environment, care of the aged. By its very nature the expenditure of such prepaid investment is in itself an investment. The offspring of educated parents are more readily educated, since a major part of their education takes place at home, healthier, and better adjusted. We will never cease repeating that whatever the outlay of Stratford-on-Avon may have been on teaching Billy Shakespeare English is still bringing in dividends to Britain. The inefficiencies of human-capital-impoverished countries such as the African continent, and those of a heavy feudal background such as Russia, or most Latin American countries is evident in their performance in peace and war.

Moreover, a real investment, fully prepaid will replace a demeaning, ever shrinking begrudging charity, a demoralizing squandering of previous investment.

That a person of Obama's talent is not allowed to see and make use of the most convincing lessons of our history is a tribute to the suppressed insights of forgotten economists of leading stature such as Schultz and Perroux.

William Krehm

Chasing One's Tail, Faster and Faster

You wonder whether this was the sort of internationalism that inspired love of your non-neighbor and Esperanto.

The Globe and Mail, that like all the world's print papers, has its own major budgetary problems, delves into the problem (1/08, "Factory Floor Blues" by Karim Hardesy): "Mike Andrade stands in the middle of a narrow, fluorescent-lit hallway that runs the length of several city blocks, pointing out the work being done behind the glass doors in this stretch of offices and labs.

"There was a time when this area of Celestica Inc. was a massive production line, operating in a 65-acre Toronto plant that was once a hub of IBM's thriving North American manufacturing operations. It was, says Mr. Andrade, Celestica's senior vice-president, wide open and with a parquet floor 'as far as the eye could see.'

"Now, Celestica is transforming as a company, from solely a producer to one that will also offer design, repair, service, and branch into new areas such as aerospace and health care – sectors that are increasingly outsourcing their electronic work.

"The labs and offices work on the best way to repair satellite TV boxes, new electronic components for washing machines and designs for social panels.

"The company's efforts, as outlined by chief executive officer Craig Muhlhauser, now faces two challengers. First, new markets and products need to be nurtured: they aren't yet fully mature. And, secondly the older manufacturing base, from which Celestica still gets the lion's share of its revenue, is cursed with overcapacity.

"Mr. Muhlhauser, now in his third year as CEO, will need to stay vigilant in both areas.

"Celestica is part of the electronics manufacturing services business – commonly known as EMS base – an industry that provides data storage servers, and builds electronics for other brands. Many RIM Blackberrys, Apple MacBooks and Cisco networking devices are made primarily by EMS companies.

"The industry can be brutal, with tight profit margins, customers who present locked-in design specifications and are willing to change to rival suppliers for the tiniest savings, and competition from Asian providers, where most EMS work, including Celestica's, is now done.

"'If we just manufacture in high-cost geographies without adding value, we're not being profitable,' Mr. Muhlhauser said. Since he took over in 2006, Celestica has cut 35% of its work force."

Let's Consult Aristotle

At this point we can do no better than to consult Aristotle that bright Macedonian student of the Greek philosopher Plato, and in turn, teacher of Alexander the Conqueror: (1) (10) Aristotle XiX Nicomachean Ethics in 23 Volumes, XiX, the Nicomachean Ethics, Harvard University Press, 1975, p. 5: "Every art and investigation, and likewise every practical pursuit or undertaking, seems to aim at some good hence it has been well said that the Good is That at which all things aim. But as there are numerous pursuits and arts and sciences, it follows that their ends are correspondingly numerous: for instance, the end of the science of medicine is health, that of shipbuilding a vessel, that of strategy is a victory, that of domestic economy wealth. Now in cases where several such pursuits are subordinate to some single faculty – as bridle-making and the other trades concerned with horses' harness are subordinate to horsemanship, and this and every other military pursuit to the science of strategy, and similarly other arts to different arts again – in all these cases, I say, the ends of the master arts are things more to be desired than all those of the arts subordinate to them; since the latter are pursued for the sake of the former….

"If therefore among the ends at which our actions aim there be one which we wish for its own sake, while we wish the others only for the sake of this, and we do not choose everything for the sake of something else (which would obviously result in a process *in ad-finitum* so that all desire would be futile), it is clear that this ultimate End must be the Good and indeed the Supreme Good. Will not then as knowledge of this Supreme Good be also of great practical importance for the conduct of life? Will it not better enable us to attain what is fitting, we ought to make an attempt to determine at all events in outline what exactly this Supreme Good and of which of the theoretical or practical sciences it is the object."

In the light of this wise conclusion formulated some 2,350 years ago by the wise philosopher, how do we grade this latest development of the nationalization of the world economy? Where will we find the spirit of world brotherhood that was advertised as the goal of the internalization of the world economy? Under which bed or crouching low in what cupboard?

The Science of Politics

Aristotle concludes: "Now it would be agreed that it must be the object of the most authoritative of the sciences – some science that is pre-eminently a master-craft. But such is manifestly the science of Politics; for it is this that ordains which of the sciences are to exist in states, and what branches of knowledge the different classes of citizens are to learn, and up to what point. And we observe that even the most highly esteemed of the faculties, such as strategy, domestic economy, oratory, are subordinate to the political science. Therefore, the Good of man must be the science of Politics."

But let us continue with the *G&M* piece. "The competition from China is now well entrenched and immense. Taiwan's Hon Hair Precision Industry in 2007 employed around 270,000 staff at just one of its EMS complexes in Shenzhen, China. Twelve of Celestica's 31 plants and four of its eight multipurpose 'mega-sites' are in Asia.

"'Original equipment manufacturers like to get a 5% cost reduction per year, and they expect a lower cost every quarter, so that squeezes EMS's,' said Michael Palma, a senior research analyst at IDC in San Mateo, Calif.

"What an EMS like Celestica needs to do is 'change the nature of the conversation,' going beyond manufacturing and jumping into added value services, Mr. Palma said."

Obviously there has been a grand departure from Aristotle's thought procession to the highest good of Man to an enthroned abstract process of increase of more continued and ever mounting increase.

"'Prove to the brand companies that you can make them money not just save them money.' It's an area Mr. Muhlhauser specializes in. He was known for fostering good customer relationships while an executive at Ford and General Electric. And he is no longer taking all comers; 'Celestica is opportunity-rich,' he says, and is in a position to only accept contracts that offer the highest margin."

Replacing Aristotle's Man, sits Mr. Ever-Increasing Process, but are we mistaken if we seem to detect a crease of concern on his imperial brow directly beneath the imperial crown? Returning to the *G&M* article: "But analysts say Celestica needs to increase its revenue in the shorter term, after suggesting a 25%, year-over-year drop last quarter."

Could it be that elbowing out Aristotle in his concern for MAN, which we today call human capital, we have come to worship abstract Process of Increase, which mathematicians tell us is the embodiment of the exponential curve in which the rate of increase grows to keep up with the rate of increase already attained until the whole shatters.

"New customer and program wins in telecommunications and the industrial, aerospace and defence sectors of the last years could help rebalance a consumer-focused portfolio toward higher-margins, the company says in its annual report.

"Celestica has been absorbing heavy losses, due to goodwill writedowns and costs relating to restructuring. On an operating basis it has been profitable, and remained so despite the revenue drop. Analysts took note, with Deutsche Bank pointing to 'steady improvement' and the CBIC World Markets saying: 'the focus on operational efficiency and profitability will reward shareholders.'

"Its operating margin was 2.7% last quarter, but it is aiming for 3 to 3.5%. The low margins are 'the nature of the beast' in the industry, said Ross Conwath of Info-Tech Research Group in London, Ont.

"EMS companies are never as busy as well-functioning auto plants. They are too bound up by short-term contracts, the short-term needs of their customers, frequent changes in products and the occasional relocation of production.

"Celestica is not happy with its own performance, Paul Nicoletti, chief financial officer, said in a conference call that 'the company is firmly committed to breaking the cycle of running our network [at] 50% to 60% [capacity], which we have been operating at for far too long.

"And so, Celestica announced $75 million to $100 million (US) cost-cutting program, which will likely mean reductions to 'non-core sites in higher-cost geography sectors,' said Mr. Muhlhauser in the conference call."

W. Krehm

Just What Do We Think We are Doing in Afghanistan?

Let us lend an ear to a long-established US think-tank. *The Wall Street Journal* (08/08, "Going Local: The Key to Afghanistan" by Seth G. Jones, a political scientist at the Rand Corporation and adjunct professor at Georgetown University, and author of *In the Graveyard of Empires: America's War in Afghanistan*, W.W. Norton): "The rapidly deteriorating situation in Afghanistan is now President Barack Obama's war, one he pledged to win during his election campaign, and defeat the Taliban and al Quaeda. One of the biggest problems, however, is that since late 2001, the US has crafted its Afghan strategy on a fatally flawed assumption: the recipe for stability is building a strong central government capable of establishing law and order in rural areas. This notion reflects a failure to grasp the local nature of Afghan politics.

"In many countries where the US has engaged in state-building, such as Germany and Japan after World War II, US policy makers inherited a strong central government that allowed them to rebuild from the top down. But Afghanistan is different. Power has often come from the bottom up in Pashtun areas of the country, the focus of today's insurgency.

"It is striking that most Americans who try to learn lessons from Afghanistan's recent history to turn to the failed military exploits of the British or Soviet Union. Just look at the list of books that many newly deployed soldiers are urged to read, such as Lester Grau's *The Bear Went Over the Mountain* and Mohammed Yousaf and Mark Adkin's *The Bear Trap*, which document some of the searing battlefield lessons that contributed to the Soviet defeat. Yet, outside some anthropologists, few people have bothered to examine Afghanistan's stable periods. The lessons are revealing.

"The Musahiban dynasty, which included Zahir Shah, Nadir Shahm and Daoud Khan, ruled Afghanistan from 1929 to 1978. It was one of the most stable periods in modern Afghan history, partly because the Musahibans understood the importance of local power. Many US policy makes have not grasped this reality, still clinging to the fantasy that stabilizing Afghanistan requires expanding the central government's writ to rural areas.

"Some Afghans had to learn this lesson the hard way. Amanullah Khan, who ruled Afghanistan from 1919 to 1929, tried to

Euthanasia Discussion in Quebec

The Globe and Mail (16/07, "Quebec physicians tentatively propose legal euthanasia" by Rheal Seguin, Quebec) informs us of an important humane step in human relations: "With great caution, the Quebec College of Physicians is prepared to cross the line on the controversial debate over euthanasia and propose that it be included 'as part of the appropriate care in certain particular circumstances.'

"After examining the issue for three years, the College's task force on ethics concluded that Quebec society has evolved to the point where it could tolerate euthanasia in specific circumstances. The task forces recommendation will likely be part of a 'reflection' document the College will release next fall, hoping that a public debate on the issue will pressure the federal government to eventually amend the criminal code.

"'We are being very cautious in our approach,' said the College's secretary, Yves Robert.

"'Avoiding the debate contributes to the general hypocrisy around this issue. To say that it doesn't happen because it is illegal is completely stupid…. We have to stop hiding our head in the sand,' Dr. Robert said.

"It is common knowledge that physicians often have no choice but to constantly increase medication such as morphine to alleviate the pain and suffering of terminally ill patients.

"'Sometimes, the pain is so unbearable that the amount of painkillers or analgesics used to control it can be fatal. And this, according to the Quebec College of Physicians, can be viewed as a form of euthanasia.'

"'The question here is to decide whether a drop in dosage or an increase in dosage constitutes a criminal act,' Dr. Robert said. 'We may go so far as to recommend that in certain cases, where pain is unbearable, the amount of the analgesic required could correspond to a form of euthanasia.'

"The College wants to avoid a divisive confrontation between those who are for or against euthanasia, saying such a debate would solve nothing.

"Instead, the debate should be about the doctor's role in accompanying a terminally ill patient toward the inevitability of death, offering as much dignity and medical assistance as possible. 'There's not a politician or a lawyer that can tell me what that entails,' Dr. Robert said.

"The College says there are three conditions required in order to amend the Criminal Code, which currently defines euthanasia as a criminal act. The first would require that the decision be made in accordance with the patient's will. A physician alone could not decide, Dr. Robert said. The second condition would require that clear rules be established to protect society from abuses. And thirdly, the doctor has to be part of the decision-making process, and not simply someone who carries out the orders.

"Quebec physicians are adamant in stating their position excludes assisted suicides, which is practiced in Switzerland and in some parts of the US. There have been a few rare cases where Canadians have died at the assisted suicide clinic Dignitas in Switzerland, but the College opposes the practice.

"Right-to-die groups in Quebec believe the province's College of Physicians have taken 'a bold, cautious and realistic' approach that will have considerable impact on the rest of the country.

"The social worker, Yvon Bureau, who spent 25 years promoting the right to euthanasia, called the College's proposal a major step forward.

"'I believe this is huge,' Mr. Bureau said. 'We need to avoid having people commit suicide or die under terrible circumstances. About 80% of the Quebec population supports the right to medical assistance in dying. All of this would take place in the course of the relationship between the doctor and the patient as well as the family.'

"The College of Physicians is expected to table its final proposal in November." ■

create a strong central state in the image of Ataturk's Turkey and Reza Shah's Iran. This proved disastrous. The central government's attempt to push into rural areas sparked social and political revolts, first in Khowst in 1923 and then in Jalabad in 1928. By 1929, local rebellions became so serious that Amanullah was forced to abdicate, and Afghanistan deteriorated into several months of anarchy.

"Masses of rural Afghans today still reject a strong central government actively

Chinese Oil Firms Embrace the Planet

With much of the rest of the world straining their eyes to detect a revival of private customer trading, it is becoming difficult keeping track of the colossal and ubiquitous shopping of China's oil corporations in just about every nook and cranny where oil has been found.

The Wall Street Journal (11/08, "Chinese Oil Firms Bid $17 Billion to Expand" by Aries Poon) tells a heady tale: "Hong Kong – China National Petroleum Corp. and Cnooc Ltd. have proposed paying at least $17 billion for all of Repsol YPF SA's stake in YPF, its Argentine unit, two people close to the talks said.

"The potential deal, which could be the biggest overseas investment of China, highlights the country's growing thirst for energy resources globally and its willingness to offer big money for access. It also underlines the ambition of CNPC to build its presence in South America and elsewhere.

"A deal would be another example of how Chinese companies are now working together to buy foreign energy assets after years of working alone.

"But the potential acquisition faces significant hurdles. A deal could be politically sensitive in Argentina, where YPF is the country's leader in both upstream operations – the exploration for and production of oil – and downstream operations involving refining and marketing."

Historic South American Military Patterns Turn Up in Oil

And it should never be forgotten that the Argentine liberator Jose de San Martin established the Argentine Republic in the South and proceeded to liberate the southern half of the Spanish-speaking part to meet the liberators of the northern half of the continent the armies under Simon Bolivar from Venezuela in imperial Lima, Peru. Long gone are the Spaniards but the same historic pattern seems to want to assert itself in oil as has been very evident in Venezuela. Far less so in the Argentine. That leaves little space for Chinese mega-oil companies.

Unconsciously, much history is shaped as much in our subconscious as in our conscious minds. And the fact that South America that conquered its political independence in so dashing a way, fills some gaps in the economic freedoms it has attained in matters economic.

"Objections could be raised if it's believed that China's biggest state-owned oil firm, and Cnooc, China's biggest offshore oil-and-gas producer, would have significant influence over Argentina's supply and pricing of strategic natural resources.

"The Argentine government holds no stake in YPF, but has the right to veto important decisions such as a transfer of ownership. The Argentine Planning Ministry, which oversees energy, didn't immediately respond to requests for comment.

"One of the people close to the discussions said CNPC believed it would be able to resolve any political consumer objections to a potential deal.

"Spain, meanwhile, could object to seeing some key assets of Repsol, the country's largest oil company, purchased by China. Spain's industry ministry could not be immediately reached for comment.

"The Chinese side discussed their offer with Repsol executives in a two-and-a-half-hour evening meeting on July 30 in Europe, according to a document seen by Dow Jones Newswires.

"A Repsol press official on Monday denied the company had met with CNPC and Cnooc, and said the company had no further comment.

"China's resource majors have snapped up other oil and other assets recently, as the country seeks to lock in energy supplies.

"China Petrochemical Corp., the Chinese state-owned oil company known as Sinopec, in June acquired Switzerland-based oil-explorer Addax Petroleum Corp. for $7.2 billion. In April, CNPC purchased Kazakh oil producer MangistauMunai-Gas jointly with Kazakhstan's state-owned KazMunaiGas for $3.3 billion.

"China's state energy companies are also showing more team-work in chasing foreign deals than previously. This year Sinopec and Cnooc have together struck deals for oil and natural gas assets in Angola and the Caribbean. In July they agreed to buy jointly a 20% stake held by US oil producer Marathon Oil Corp. in an oil block off Angola for $1.3 billion.

"Chinese oil companies have also signed oil-for-loans agreement with Russia and Brazil."

Not Every Effort a Success

"But not all China's efforts have been successful. In June, a $19.5 billion bid by Aluminum Corp. of China, or Chinalco, to raise its stake in Anglo-Australian mining giant Rio Tinto, collapsed amidst shareholder and political concerns. An earlier, successful deal by Chinalco, in which it paid $14 billion for an initial 9% stake in Rio in February 2008, was China's largest foreign investment in the resources sector.

"Repsol has been looking to sell its 84% stake in YPF to earn more cash to pay off debt. On July 30, Repsol said its second-quarter adjusted profit plunged 62% to €265 million ($375.5 million) from a year earlier, citing dramatically lower refining margins and oil prices. It said its net debt was €10.41 billion.

"In 2007, Repsol sold a 14.9% stake in YPF to Argentine's Grupo Petersen for $2.24 billion. The remainder is held by minority shareholders.

"The Chinese side, with CNPC taking a leading role, first put forward the offer in late June, one of the people familiar with the discussions said. On July 21, Repsol responded to CNPC and agreed to continue the negotiations, the person said.

"Light, sweet crude oil started 2009 near $58 a barrel and has since risen to more than $70 a barrel, which could be an important factor in the negotiations.

"A CNPC spokesman said he had no information on the issue. YPF declined to comment on a potential deal. Grupo Petersen referred requests for comment to YPF.

"CNPC is aiming to take a majority stake in YPF. Cnooc would likely have a smaller share, people said."

And so the underground rumbles go on as China continues on her shopping spree.

W.K.

meddling in their affairs. In southern and eastern Afghanistan, which are dominated by Pashtuns, many consider the central government a foreign entity. 'My allegiance is to my family first,' one tribal elder from Kandahar told me earlier this year. 'Then to my village, sub-tribe and tribe,' he continued, noting that the government played no meaningful role in his daily life."

The Afghan Social Pyramid Stands on Its Cusp

"'I have often been struck by the disconnect between the center and periphery when traveling through areas where as recently as this year, some villagers had never heard of President Hamid Karzai, who has led the country since 2001. In a few cases, they even thought US military forces I was traveling with were Soviets, not realizing that the Soviet army withdrew in 1989. Time has a

Whether You are Setting Up Your Own Business or Retiring, the System is Not Helpful for the Little Guy

The New York Times (25/06, "A Bead on Ordinary Investors: Mutual Funds with Targets, and Misfires" by Leslie Wayne) paints the picture depending on his promised retirement fund to find that it's really not there: "Washington blessed them as a way to put your 401(k) on automatic pilot and glide safely towards retirement.

"But popular target-date mutual funds have badly missed the mark – and now regulators are asking why.

"The Securities and Exchange Commission and the Labor Department are examples why the funds, which were supposed to become safer as their investors grew older, seemed to get riskier instead.

"Big mutual fund companies like Fidelity and Vanguard promised target-date funds would shift automatically from high-growth investments, like go-go tech stocks towards safer ones, like bonds, as investors neared the year of retirement – a 'target date' like 2010, 2020, or 2030.

"Labor Department officials evidently found the concept persuasive. In 2007, they issued an unusual rule that protects employers who automatically send workers' 401(k) money to target funds if, later, the employees lose money. That so-called safe harbor unleashed a flood of money into the funds.

"But as the stock market plummeted last year, some 2010 funds – which many investors thought would be invested safely by then to protect their nest-eggs – lost 40% of their value. That showing was even worse than that of the Standard & Poor's 500, which fell 38.6%.

"Mary L. Schapiro, the chairman of the Securities Exchange Commission is now questioning whether fund companies misled investors around the risks associated with target-date funds, a concern the mutual fund industry says is unjustified.

"Data collected by the SEC shows that target-date funds vary widely in terms of their investment risks even when they use similar target years or names. Even though federal officials put a stamp of approval on target-date funds, there are no clear standards about how they should work.

"Funds marketed to people hoping to retire in 2010, for instance, have anywhere from 21% to 79% of their holdings in stocks, Ms. Schapiro said in a speech in New York last week, citing data collected by Morning-Star.

"No hard and fast rules exist for how to balance a portfolio as retirement approaches. A lot of variables come into play, including age, sources of income and appetite for risk. Some financial planners recommend that people who are at or near retirement age, and comfortable with some risk, invest about 40% of their portfolios in stocks.

"But Ms. Schapiro said the SEC was concerned that funds which the same target dates vary so widely in their investments and returns. The average 2010 fund had more than 45% of its holdings in stocks last year. The Fidelity Freedom 2010 Fund was 50% in stocks and lost a quarter of its value, according to Morningstar. The Alliance-Bernstein 2010 Fund was 57% in stocks and fell by a third.

"Funds leaning toward safer bonds, by contrast, fared far better. A Wells Fargo 2010 fund that was heavily invested in bonds lost just 11%, while a Deutsche Bank fund also favored fixed-income investments was down just 4%.

"Target-date funds have exploded since 2006, when Congress enabled companies to make them the automatic choice for employees who do not specify where they wanted to invest their 401(k) savings. The move, a boon for the mutual fund industry, occurred over the objections of insurance companies, whose money market-style 'stable value' funds had been the default choice for 401(k) investments. About $182 billion has been poured into target-date funds, and fund companies have set up scores of them.

"Now, in a reversal, a number of bills before Congress seek to provide greater disclosure of fees, more accurate marketing and improved financial advice to workers investing in target-date funds and other 401(k) funds.

"'What we have is the Wild, Wild West of investing,' said David A. Krasnow, an asset management firm, at a hearing on June 18 held by the SEC and the Labor Department. 'Many people in target-date funds got run over by a truck and didn't know why.'

"Critics of target-date funds maintain that these investments are often opaque and difficult to understand. Mutual fund companies often create them by bundling existing mutual funds, some with good track records and some with worst records. Thus the 'fund of funds' concept enables mutual fund companies to collect more assets and fees, but can make it hard for investors to understand what these funds contain or how they are being charged.

"The SEC is looking into whether putting a date in a fund's name should be prohibited, whether there is enough information about the risk of these funds and whether they are properly structured for a safe retirement. There is also legislation calling for greater fee disclosure, more objective investment advice and the inclusion of low-cost index funds in workers 401(k) plans.

"A study by Envestnet Asset Management and Behavorial Research Associations found a range of misconceptions, including that employees thought target-date funds would provide a guaranteed return, that their money would grow faster in target-date funds than in other investments, and that these funds allowed workers to put away less money and still be able to retire."

W.K.

way of standing still in Afghanistan.

"The lessons of Amanullah Khan were not lost on the Musahibans. While they believed it was important to build a strong army and competent government beurocrats, dealing with rural Afghanistan required extraordinary caution. They exempted a range of Pashtun tribes from military service and established a fairly effective tribal engagement strategy in southern and eastern Afghanistan.

"Zahir Shah supported village-level defense forces, called arbakai, to establish order in Eastern Afghanistan. These village-level forces were used for defensive purposes and organized under the auspices of legitimate tribal institutions. But the results were clear: law and order were established by locals, not the central government. When rebellions occurred, as they sometimes did, the government could temporarily move into rural areas and crush them.

"The Soviet-backed regimes never learned the Musihaban secret, and tried to establish order from the top down. The US and much of the international community made a similar mistake beginning in 2001, conceiving of success as emanating from a powerful central government. But this reflects a quintessential Western understanding of the nation-state, not grounded in today's reality. 'I'm afraid we are still looking for the solution only in Kabul,' a senior US government official recently told me. 'It is a false hope.'

"After the overthrow of the Taliban regime the US regime and its allies began building an Afghan national army and police force. They also supported presidential elections in 2004 and parliamentary elections in 2005/ But there were no systematic efforts to encourage elections at the provincial or district level, where most Afghan political energies are focused. The US did, however, back a handful of war-lords, usually detested by Afghans because they operate outside the tribal system.

"The Taliban and other insurgent groups are most attuned to local dynamics. In southern Afghanistan, for example, Taliban commanders have developed a fairly effective bottom-up strategy to co-opt or coerce tribal and other local leaders. They often send individuals from the same tribe, subtribe or clan into an area to convince locals that resistance is futile and that the Afghan government is a corrupt, puppet regime…. When Taliban fighters fail to co-opt local leaders, they sometimes assassinate them, But neither the Afghan government nor the

Surprise Bills at the Doctor's

It's nothing that could have come out of Hippocrates' Oath.

The Wall Street Journal (08/05, "Beyond Co-Pay: To Ensure They Get Paid, Doctors Seek Entire Bill for Patient Share Upfront" by Anna Wilde Matthews): "Insured patients typically expect to make a small co-payment when they see a doctor, and later get billed for anything else they owe. But physicians no longer want to wait for their money.

"Medical clinics are increasingly asking people to fork over their entire out-of pocket charge as they're walking out after a visit. That could include the amount the patient towards their health plan's deductible and a percentage of the cost of care under a co-insurance requirement. Patients who are uninsured also are being asked upfront or at least signed up for a payment plan. And physician practices have started demanding patients pay in advance for outpatient surgeries and expensive imaging scans, a practice that hospitals have long enforced.

"A questionnaire sent to its medical-practice customers by NaviNet Inc., which provides a Web service that allows doctors to communicate with insurers, found that more than 650 respondents were trying to get money beyond just co-payments during patients' visits. Settling the bill before leaving the doctor's office represents a new style of payment that patients are still getting used to. Jen Brull, a family physician in Plainsville, Ohio, says the staff in her office had to teach people that just like when I go to Wal-Mart I have to pay before I leave, I have to pay at the doctor's office."

Hippocrates, it seems, is running a grocery chain listed on the stock exchange these days.

"Doctors say they have to request their fees while patients are still at the office because bills sent later typically recover only about half of what a practice is owed, according to McKinsey & Co. The figure drops to just 10% and 20% when patients are uninsured. In today's economy, many doctors say the problem has worsened. Also the share of physicians' revenue that comes from patients rather than insurers is growing because health plans are including ever-larger deductions and other out-of-pocket charges.

"'The days of coming up with just a $10 co-pay – that ship sailed a long time ago,' says Jeff Drasnin, a pediatrician in the Cincinnati area. Collecting at time of service has 'cut out a tremendous amount of bad debt we used to write off,' he says.

"Medical practices are able to come up with instant bills partly thanks to new electronic services rolled out over the past few years by insurers including Humana Inc., UnitedHealth Group Inc., Highmark Blue Cross Blue Shield in Pennsylvania, and the Blue Cross Shield Plans in Texas and Illinois, which are units of the nonprofit Health Care Service Corp. After seeing patients, doctors can enter into the system the billing codes for the care they provided and have these quickly reviewed by the health plan, which then details what the patient owes.

Some consumers say they prefer the retail-style billing. 'When you walk away, you know you're done with all your responsibility,' says Joe Girst, of San Antonio, Texas. Mr. Girst made a $35 co-payment last week before seeing a doctor at San Antonio Orthopaedic Group for a sore wrist. He then paid his $46 co-insurance tab as he left the clinic. The 48-year-old, who works for a medical-device maker, says he was happy to avoid 'that mystery bill that shows up six weeks later.'

"For patients worried about a health concern and trying to absorb a doctor's advice, attempting to understand a detailed medical bill before leaving the office can mean more stress. Adding to the hassle, some practices don't rely on health plan's detailed analysis, but rather charge based on cost estimates or projections, which aren't always accurate. Later, patients may have to go over the bill again when they get their insurer's formal statement….

"Even if you pay whatever the doctor's office requests before you walk out of the clinic door, you should carefully watch for the final explanation of benefits from your insurer. If it says you owe a different amount than the doctor's office collected, you can call and request a refund."■

US is playing at the local level, and it has prevented them from achieving their key objectives.

"America's original goal for sending forces to Afghanistan was to uproot the al Quaeda terrorists and their supporters after the September 11, 2001, attacks. Sadly, this goal has still not been achieved. Nearly eight years after the attacks, US and other Western intelligence indicates that al Quaeda is still the most significant threat to the US homeland. Al Quaeda's key sanctuary has moved from key areas like Jalalabad in 2001 to the Federally Administered Tribal Areas of Pakistan. That's about the distance from New York City to Philadelphia.

"Earlier this year, the head of US Central Command, Gen. David Petraeus, noted that the Afghanistan-Pakistan border 'is the headquarters of the al Quaeda senior leadership' who are planning attacks on the US British PM Gordon Brown also warned that 'three quarters of the most serious plots investigated by the British authorities have links to al Quaeda operating from the border region.

"The successful March 2004 terrorist attacks in Madrid, July 2005 plot to blow up airplanes flying from Britain to the US and Canada, and more recently thwarted plots in Germany, Denmark, Spain and France have a common theme. They all link back to al Queda or other affiliated terrorist groups operating from the Afghanistan-Pakistan border.

"What's more, the two most successful insurgent groups in Afghanistan, the Taliban and Haqqani network, have developed a close strategic relationship with al Quaeda.... If Americans should have learned anything from September 11, it was the US cannot accept a situation where al Quaeda and its allies enjoy a sanctuary to plan and train for terrorist attacks against the US.

"The reality, then is that the US is stuck in Afghanistan and Pakistan for now. But as violence levels continue to increase, it is at a critical juncture. With mid-term US elections coming next year, White House officials are demanding measurable progress in Afghanistan. Now is a pivotal time to fundamentally rethink America's strategy."

And, of course, this is of critical importance for Canada. For the limited official end of Canada's official mission in Afghanistan will have come by then. But at that point we can foresee that Washington will employ every possible pressure to prolong the presence of Canadian forces to support Washington's less than brilliant intervention. Now is the time for Canadians to start working on their politicians to make sure that we are not drawn in to trading further Canadian lives so that Washington can continue to exercise its insensitivity to the peculiarities of the rest of the world.

W.K.

Credit Bubbles in India's Slums

Our readers will remember the near-reverence with which we read the dispatches from India some of whose credit companies, unsullied by too great a concern about profit, had brought credit to the Indian and other slums in minute qualities. Unfortunately the credit meltdown and the slackening concern about the other fellow and (and who after all asked him to raise a family?) has for the few years dimmed these inspiring reports. And, indeed, since then the big bank crisis pushed them off the screen entirely. What happened to them? That we learn from a recent reportage in *The Wall Street Journal* (13/08, "A Global Surge in Tiny Loans Spurs Credit Bubble in a Slum" by Ketaki Gokhale): "Ramanagaram, India – A credit crisis is brewing in 'microfinance,' the business of making the tiniest loans in the world.

"Microlending fights poverty by helping poor people finance small businesses – snack stalls, fruit trees, milk-producing buffaloes – in slums and other places where it's tough to get a normal loan. But what began as a social experiment to aid the world's poorest has also shown it can turn a profit.

"That has attracted private-equity funds and other foreign investors, who've poured billions of dollars over the past few years into microfinance world-wide.

"The result: Today in India, some poor neighborhoods are being 'carpet-bombed' with loans, says Rajalaxmi Kamathm a researcher at the Indian Institute of Management Bangalore who studies the issue. In India, microloans outstanding grew 72% in the year ended March 31, 2008 totalling $1,24 billion, according to S-Dhan, an industry association in New Delhi.

"'We fear a bubble,' says Jacques Grivel of the Luxembourg-based Finethis, a $100 million investment fund that focuses on Latin America, Eastern Europe and Asia, though it has no exposure in India. 'Too much money is chasing too few good candidates.'

"Here in Ramanagaram, a silk-making city in southern India, Zahreen Tai noticed the change. Suddenly, in the shantytown where she lives, a lot of people wanted to loan her money. She borrowed $125 to invest in her husband's vegetable cart. Then she borrowed more.

"'I took from one bank to pay the previous one. And I did it again,' says Ms. Taj, 46 years old. In four years she took a total of four loans from two microlenders in progressively larger amounts – two for $209, another for $293, and then $356.

"At the height of her borrowing binge, she says, she bought a television set. 'The arrival of microfinance increased our desire for things we didn't have,' Ms. Ta says, 'We all have dreams.'

"Today her house is bare except for a floor mat, and a pile of kitchen utensils. By selling her appliances and jewelry, she cut her debt by $94. That's equal to roughly a quarter of her annual income.

"Around Ramanagaram, the silk-making city where Ms. Taj lives, the debt load is stirring up social tension. Many borrowers complain that effective rates – which can vary from 24% annually to 39% annually – fuel a cycle of indebtedness.

"Alpana Killawals, a spokeswoman for the Reserve Bank of India, said in an email that the central bank doesn't as a practice cap interest rates for microlenders, but does press them not to charge 'excessive' rates.

"Meanwhile, local mosque leaders have started telling people in the predominantly Muslim community to stop paying their loans. Borrowers have complied en masse."

Muslim Leaders Advise Stopping Payments of Ransom Rates

"The mosque leaders are also demanding that lenders give them an accounting of their finances. The lenders say they're not about to comply with that.

"The repayment revolt has spread to other communities, including the nearby city of Channapatna, and could reach further across India, observers say.

"'We are very worried about this,' says Vijayalakshmi Das of FWWBIndia, a company that connects microlenders with financing from mainstream banks. 'Risk management is not a strong point for the majority for the majority' of local microfinance providers. She adds, 'Microfinance needs to learn a lesson.'

"Nationwise, average Indian household debt from microfinance lenders almost quintupled between 2004 and 2009 to about $135 from $27 or so, according to a survey by Sa Dhan, the industry association. These sums are obviously tiny by global standards. But in rural India, the poorest often subsist on just a few dollars a week.

"Traditionally, microlenders were non-profits focused on community service. In recent years, however, many of the larger producing firms have registered with the Indian central bank as a type of for-profit finance company. That places them under greater regulatory scrutiny, but also gives them wider access to funding.

"This change opened the door to more private-equity money. Of the 54 private-equity deals (totalling $1,19 billion) in India's banking and finance sector in the past 18 months, microfinance accounted for 16 deals worth at least $245 million, according to Venture Intelligence, a Chemmai-based private-equity research service.

"'We've seen a major mission drift in microfinance, from being a social agency first,' says Arnab Mukherji, a researcher at the Indian Institute of Management in Bangalore, to being "primarily a lending agency that wants to maximize its profit.'

"Making loans in poorest India sounds inherently risky. But investors argue that rural developing world has remained largely insulated from the global economic slump.

"International private equity funds started taking notice of Indian microfinance in March 2007. That's when Sequoia Capital, a venture capital firm in Silicon Valley participated in a $11.5 million share offering by SKS Microfinance Ltd. of Hyderabad, India, one of the world's largest microlenders.

"'SKS showed the industry how to tap private equity to scale up,' said Arun Natarajan of Venture Intelligence.

"Numerous deals followed with investors including Boston-based Sandstone Capital, San Francisco-based Valiant Capital, an affiliate of Silicon Valley Bank."■

Car Leasing: Solution or Problem?

The Wall Street Journal (29/07, "GM Plans a Return to Car Leasing" by John D. Stoll) is a good example of the bumbling that our policy-makers are led into by trying to solve vast, existential problems, by avoiding them to concentrate on perpetuating vested interests.

"General Motors Co. and its financing affiliate GMAC Inc. are eyeing on August 1 return to the auto-leasing market, according to people familiar with the matter, after massive government bailout packages allowed both companies to get back on their feet. GM and Chrysler Group LLC pulled out of leasing in August 2008 amid a steady decline in vehicle resale values, a sales slump and troubles at their respective lending affiliates.

"At the time, leasing represented about 20% of GM's new-car business in the US and was causing losses for GM and other car makers. Many of their key competitors, including Ford Motor Co., Daimler AG and Toyota Motor Corp., scaled back leasing but didn't pull out of the business completely.

"In a recent conference call with analysts and reporters, GM said many of the company's former lease customers have decided to purchase vehicles instead from GM or chose to buy a used car or defect to another auto maker. GM, which filed for bankruptcy in June and emerged from court early in July, has said credit availability still remains a key drag on auto sales.

"Details of GM's leasing plans are still being hammered out, but people familiar with the program said the company is looking at various models across its four-brand lineup as candidates for leasing. These include the Cadillac CTS, which competes in a luxury market that is heavily dependent on lease deals.

"GMAC spokeswoman Gina Proia said her company 'continues to evaluate ways to support' GM and 'leasing is one of the options we are evaluating.'

"A GM executive working on the plans said the auto maker has talked with several banks as well to obtain financing for leasing. 'Credit is easing, banks have capacity and [resale] values have been steadily increasing,' the executive said.

"After running into serious liquidity problems in late 2008, both GM and GMAC, a former subsidiary, have been propped up by more than $60 billion in government funds. GMAC's balance sheet was strengthened by $12 billion in federal capital in the second quarter alone.

"GM sold 51% of GMAC in 2006 to Cerberus Capital Management LP., and was forced to give up an additional 40% of its stake after the December bailout of the lending firm. Currently, GM owns 9.9% of GMAC, which has become a bank holding company thanks to the bailout.

"Despite GM's shrinking stake, the auto maker and GMAC remain contractually bound as preferred partners when it comes to new-vehicle financing. GMAC recently added Chrysler's early-June emergence from bankruptcy. It is unclear when, or if Chrysler will return to leasing.

"Although GM dealers have been able to finance some buyers via lease programs through credit unions and other lenders over the last 12 months, those deals have represented a negligible part of its sales.

"Historically GM and GMAC were able to team up to offer cheap leases. GM would use marketing dollars, earmarked as vehicle incentives, to subsidize the cost of a vehicle lease that GMAC would originate and fund.

"There are several factors behind GM's willingness to tiptoe back into offering new-vehicle leases at its dealerships, including the firming up of resale values for used cars and trucks."

But note there are other obscure considerations that can be decisive in determining which way the government will choose in handling a major crisis that may put an end to the society that we live in. For example, instead of introducing accrual accountancy in its books that will give the world an idea of what the government deficits are, our governments still write off their investment in human capital in a single year, whereas the debt incurred to finance it is carefully "amortized" over the likely usefulness of the investment in education, health, the environment and much, much else is "depreciated" in a single year and thereafter treated only as "debt."

The debates on the subject in the press and parliament and US Congress refer to this entirely as "debt" when the most important lesson that came out of WWII was – as recognized by the work of hundreds of US economists sent to Japan and Germany after the Peace was that human capital is the most important investment a government can make.

In 1996 Washington recognized that with respect to the physical investments a government could make. And from a devastating crisis in that day, that recognition led to a drop in interest rates and a period of tremendous growth. Why do our governments avoid breathing that – very conservatively – $3.5 trillion of prepaid human investment await recognition and being reinvested to handle the present crisis? By very conservative calculation the Canadian figure for such prepaid human capital could not be less than $350 billion.

There is this further relationship that is no detail: much of this prepaid investment in human capital that is not even recognized as such, is in fact not just "spending" but is itself "investment." The children of educated parents tend to be easier to educate and healthier. Britain is still receiving dividends on whatever Stratford-on-Avon spend to teach Billy Shakespeare the glories of the human language and the follies of governments.

William Krehm

A Tip of the Hat to the 1920s

We have over some decades tried getting across to economists that flipping over propositions as chefs do pancakes, doesn't work. If I hold a pistol to my head and press the trigger, I fall dead. However, if a man falls dead, that doesn't mean necessarily that he has shot himself. He may have suffered heart-failure.

Nobody in his right senses moving from a town of 20,000 to New York City is silly enough to believe that his cost-of-living will remain the same. How then can they take for granted that is possible when humanity is making just such a move?

But it is not dunderheadedness alone at fault here, but something more sinister. The late French economist François Perroux put his finger on what underlies this mania with his theory of the "dominant revenue." This he defined as the revenue of the class in the economic saddle whose revenue is accepted as an index of the nation's welfare. For example, after the Napoleonic Wars the large landowners in Britain, whose ground-rents from whom they farmed out their lands was kept high by tariffs on foodstuffs – the Corn Laws. But then the steam-driven equipment of John Watt took over the factories. That shifted the "dominant revenue" to the industrialists who to squeeze the most revenue out of their monopoly espoused free trade at home and abroad. That would sink the subsistence wages of their workers and on their foreign markets still lower.

British economists of the day explained that interest by drawing upon some version of the labour theory of value to support their argument. That was fine so long as the British worker was illiterate. But they were rapidly learning to read. And the socialist leaders defeated in the struggles on the barricades being thrown up in most European capitals – usually socialists from the north and anarchists in the south – were pouring into Britain as refugees. And they started organizing soap-box speeches in Hyde Park.

And to reach their conclusions most of them used some version of the labour theory of value. So long as the British workers were illiterate labour theories of value were fine, but the workers were rapidly learning how to read, the same theories were becoming subversive. Hence, the scene of value assessment and creation was shifted from the grimy factory to the elegant selling outlets and measured not by the amount of "average labour" needed to produce a commodity but by the pleasure derived from consuming it – probably the most radical shift in "dominant revenue" theories of all times, since it installed greed in its most abstract unlimited form. To give it a little pseudo-scientific glitter a bit of misplaced differential calculus was added.

And now *The Wall Street Journal* (08/06, "US, in Nod to China, to Sell More TIPS" by Rob Capeland and Maya Jackson Bandall) brings us the next step in lifting the "dominant revenue" of our day beyond Parliament or any one tampering with the power of this ultimate "dominant revenue" of greed enthroned. We quote: "The Treasury Department, responding to the growing demand from China and other investors, will boost the sale of inflation-protected bonds that hold their value as consumer prices rise.

"The decision to increase sales of Treasury-Protected Securities, or TIPS, is part of a broader effort to ensure there is enough demand for Treasury bonds to help the US finance its swelling budget deficit. The Treasury has issued a record amount of debt in the past year, and the department said Wednesday it will sell a record $75 billion next week. For the quarter ending September 30, Treasury estimates that it will need to borrow $406 billion, up from $343 billion the quarter before.

"In particular, Treasury officials need to ensure demand from China, the largest holder of US government debt. Last week's auctions of fixed rate notes saw lukewarm response from China and other investors. Chinese officials had indicated they want inflation-protected securities, especially as the US economy starts to recover.

"'Inflation is the No. 1 worry,' said March Chandler, global head of currency strategy for Brown Brothers Harriman & Co. 'This is the government saying we will take the inflation risk away from you.'

"Even with an increase, TIPS would remain a fraction of the overall market for Treasuries. Of the $6.66 trillion of government bonds issued between Octtober 1, 2008, and June 30 this year, just $44 billion were TIPS.

"The Treasury could easily sell as much as $10 billion more, said Jeffrey Elswick, a director of fixed income at Frost Investment Advisors LLC. But those extra sales mightn't be such great news for existing owners of inflation-protected notes. If the Treasury continues to ramp up TIPS sales, it will 'cheapen' the bonds of existing investors, said Don Martion, a financial planner with Mayflower Capital in Los Altos, Calif.

"The value of the securities fell after the announcement, sending the gap between TIPS and comparable nominal notes to a two-month high. The gap ended at 1.93 percentage points, signaling that investors expect annualized inflation of 1.93% over the next decade.

"The Treasury also said it may issue 30-year TIPS in place of 20-year TIPS."

What is lost in this article and in the government's release is the trend the "inflation" in the value-loss of the government debt was in fact an important hint of the amortization of the debt incurred for investments by the government that corresponds to the depreciation of whatever "investments" the government made. Now the borrowing remain "unamortized" for the year of their guaranteed "constant" (read "unamortized") debt.

William Krehm

Are Regulators Getting Tougher on Banks or Just on Their Clients?

It is called a "memorandum of understanding." But "memorandum" is from the Latin "to remember." And here the essential part of the tale is deliberately forgotten – it has to do with the reasons for the nationalization of the Bank of Canada in 1938, and the terms of that nationalization that permitted the Government of Canada to do its capital financing from its own bank so that the interest – less handling expenses came back to it. All this is still valid and in our law books.

The provinces, too, are allowed generous borrowing quotas under the *Bank of Canada Act*, but the interest paid on it would go substantially not to the provinces since they are not shareholders of the central bank, but to Ottawa that is. But that could serve as the basis for friendly cooperation instead of the constant tensions between the two levels of government. And, oh, the municipalities, today the ultimate victims left saddled with the bulk of the unseemly cost of the speculative orgies of our banks, could do much of their essential capital financing under the provisions for "corporations" with the guarantee of either federal or a provincial government.

Of course, the net interest paid would always go to the BoC's one shareholder the Government of Canada. But that could be negotiated in a friendly way rather than with the current hissing and grinding of teeth. And using double-entry or "Accrual Accountancy that that Crusading Order brought back almost a thousand years ago from the Holy land would record the progress of the arrangement.

Rather than that we get a tangle of bureaucratic measures from several offices that did little enough to prevent our deregulated, speculative banks from getting us into this mess, and are certain to be unable to lift us out of it.

The Wall Street Journal (31/07, "Regulators Are Getting Tougher on Banks" by Damian Paletta and Dan FitzPatrick) tells a tale couched in dense bureaucratese: "Federal regulators have escalated the number of wounded banks they have essentially put on probation, with some of the targeted banks complaining that the crackdown has been too harsh.

"The Federal Reserve and the Office of the Comptroller of the Currency, two of the primary US banking regulators, have issued more of the so-called memorandums of understanding so far this year than they did for all of 2008, according to data obtained from the agencies under *Freedom of Information Act* requests.

"At the current rate of at least 285 so far, the Fed, OCC, and Federal Deposit Insurance Corp, are on track to issue nearly 600 of the secret agreements for the full year, compared with 399 last year. Memorandums of understanding can force financial institutions to increase their capital, overhaul management or take other steps."

Not in the Light of Day

Above all, what is hidden from the public eye? But are the bureaucrats who got the US and the world into this ever-deepening mess to be trusted, with what they are up to, to get them out of it?

"Such sanctions typically aren't publicly disclosed to avoid possibly rattling depositors and shareholders. Institutions with memorandums this year range from Bank of America Corp, regional BancGroup Inc., based in Montgomery, Ala., to Berkshire Bancorp Inc., a New York bank with just 12 branches.

"The sharp increase comes as Congress considers changes proposed by the Obama administration that would overhaul the way the US government oversees banks. Many bankers and analysts believe those changes would result in an even more assertive regulatory apparatus. Regulators have been criticized for going too easy on banks and security firms. Many bankers and analysts believe those changes would result in an even more assertive regulatory apparatus. Regulators have been criticized for going too easy on banks and security firms.

"Regulators say that their tougher stand now could prevent some struggling banks from failing as borrowers fall behind on their payments and the US economy slog through recession. A total of 64 banks have failed this year, up from 25 in 2008.

"Regulators' natural response is, 'Oh my goodness, we've got to toughen up,' Charles Plosser, president of the Federal Reserve Bank of Philadelphia, said in an interview.

"Some bankers counter that the regulatory squeeze is making it even harder for them to make good loans that would help them recover. 'Its frustrating and aggravating,' said Pat Sheaffer chairman and CEO of Riverview Bancorp of Vancouver, Wash., which has $920 million in assets and 18 branches.

"In January, the Office of Thrift Supervision issued Riverview a memorandum of understanding that requires the bank to increase its total risk-based capital, a measurement of financial strength, to 12% from 10.7% as of December 31 Mr. Sheaffer said there was little dialogue with the agency before the requirement was imposed.

"The OTS didn't return phone calls seeking comment.

"James Miller Jr., CEO of Fidelity Southern Corp., said he was surprised to be hit with a memorandum of understanding in December because the Atlanta bank's exposure to residential real estate is low in comparison to others in the area.

"Regulators want Fidelity to reduce its residential real-estate construction lending to no more than 100% of total capital, down from about 120%. Since the agreement, the bank has lowered its exposure to 110%.

"'I am not about to say anything about my regulators,' Mr. Miller said. The bank got $483 million in capital from the taxpayer-funded Troubled Asset Relief Program right after it signed the memorandum. 'I concluded that regulators were satisfied with how we were running our bank,' he added. In the past, the bank has faced criticism that its regulation was too uneven, with examiners in some areas of the US accused of being too easy on banks, while examiners in others were much tougher. 'There is an awful lot of talk among bankers that…8, 10 and 12% will be targets FDIC will want to see going forward, even for healthy banks,' said Ted Awerkamp, CEO known as Tier 1 capital, Tier 1 risk-based capital and total risk-based capital. The Quincy, Ill., bank holding company entered a memorandum with the Fed earlier this year."

Memorandums of understanding can lead to sterner, public sanctions if a bank is seen as not doing enough to correct problems.

W.K.