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Human Capital at Work

The New York Times (13/07, "How Microbes Defend and Define Us" by Carl Zimmer) reports how our biological destinies may depend on little-known microbes: "In 2008, Dr. Alexander Khoruts, a gastroenterologist at the University of Minnesota, took on a patient suffering from a vicious gut infection of *Clostridium difficile*. She was crippled with constant diarrhea which had left her in a wheelchair wearing diapers. Dr. Khoruts treated her with an assortment of antibiotics, but nothing could stop the bacteria. His patient was wasting away, losing 60 pounds over the course of eight months. 'She was just dwindling down the drain, and she probably would have died,' Dr. Khoruts said.

"Dr. Khoruts decided his patient needed a transplant. But he didn't give her a piece of somebody else's intestines, or a stomach, or any other organ. Instead, he gave her some of her husband's bacteria.

"Dr. Khoruts mixed a small sample of her husband's stool with saline solution and delivered it into her colon. Writing in the *Journal of Clinical Gastroenterology* last month, Dr. Khoruts and his colleagues reported that her diarrhea vanished in a day. Her *Clostridium difficile* infection disappeared as well and has not returned since.

"The procedure – known as bacteriotherapy or fecal transplantation – has been carried out a few times over the past few decades. But Dr. Khoruts and his colleagues were able to do something previous doctors could not: they took a survey of the bacteria in her intestines before and after the transplant.

"Before the transplant, they found her gut flora was in a desperate state: 'The normal bacteria just didn't exist inside her,' said Dr. Khoruts. 'She was colonized by all sorts of misfits.'

"Two weeks after the transplant, the scientists analyzed the microbes again. Her husband's microbes had taken over. 'That community was able to function and cure her disease in a matter of days,' said Janet Janson, a microbial ecologist at Lawrence Berkeley National Laboratory and a co-author of the paper. 'I didn't expect it to work. The project blew me away.'

"Scientists are regularly blown away by the complexity, power, and sheer number of microbes that live in our bodies. 'We have over 10 times more microbes than human cells in our bodies,' said George Weinstock of Washington University in St. Louis. But the microbiome, as it is known, remains mostly a mystery. 'It is as though we have these other organs, and yet things are parts of our bodies that we know nothing about.'

"Dr. Weinstock is part of an international effort to shed light on those puzzling organs. He and his colleagues are cataloging thousand of new microbe species by gathering their DNA sequences. Meanwhile, other scientists are running experiments to figure out what those microbes are actually doing. They're finding that the microbiome does a lot to keep us in good health. Ultimately, researchers hope, they will learn enough about the microbiome to enlist it in the fight against diseases."

The Marvelous Universe of the Microbiome

"'In just the last year, it really went from a small cottage industry to the big time,' said David Relman of Stanford University.

"The microbiome first came to light in the mid-1600s, when the Dutch lens-grinder Antonie van Leeuwenhoek scraped the scum off his teeth, placed it under a microscope and discovered that it contained

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Human Capital from page 1

swimming creatures. Later generations of microbiologists continued to study microbes from our bodies but they could only study the ones that could survive in a laboratory. For many species, this exile meant death.

“In recent years, scientists have started to survey the microbiome in a new way: by gathering DNA. They scrape the skin or take a check swab and pull out the genetic material. Getting the DNA is fairly easy. Sequencing and making sense of it is hard, however, because a single sample may yield millions of fragments of DNA from hundreds of different species.

“A number of teams are working together to tackle this problem in a systematic way. Dr. Weinstock is part of the biggest of these initiatives, known as the Human Microbiome Project. The \$150 million initiative was started in 2007 by the National Institutes of Health. The project is gathering samples from 18 different sites on the bodies of 300 volunteers.

“To make sense of the genes that they’re gathering, they are sequencing the entire genomes of some 900 species that have been cultivated in the lab. Before the project, scientists had only sequenced about 20 species in the microbiome. In May, the scientists published details on the first 178 genomes. They discovered 29,693 genes that are unlike any known genes. (The entire human genome contains only around 20,000 protein-coding genes.) “This was surprising to us, because these are organisms that have been studied for a long time,” said Karen E. Nelson of the J. Craig Venter Institute in Rockville, MD.

“The new surveys are helping scientists understand the many ecosystems our bodies offer microbes in the mouth alone, Dr. Relman estimates, there are between 500 and 1,000 species. ‘It hasn’t reached a plateau yet: the more people you look at, the more species you get,’ he said. The mouth in turn is divided up into smaller ecosystems, like the tongue, the gums, the teeth. Each tooth – and even each side of each tooth – has a different combination of species.

“Scientists are even discovering ecosystems in our bodies where they weren’t supposed to exist. Lungs have traditionally been considered sterile because microbiologists have never been able to rear microbes from them. A team of scientists at Imperial College London recently went hunting for DNA instead. Analyzing lung samples from healthy volunteers, they discovered 128 species of bacteria. Every square centimeter of

our lungs is home to 2,000 microbes.

“Some microbes can only survive in one part of the body, while others are more cosmopolitan. And the species found in one person’s body may be missing from another’s. Out of the 300 to 1,000 species of microbes identified in people’s mouths, for example, only about 100 to 200 live in any one person’s mouth at any given moment. Only 13% of the species on two people’s hands are the same. Only 17% of the species living on one person’s left hand also live on the right one.

“This variation means that the total number of genes in the human microbiome must be colossal. European and Chinese researchers recently catalogued all the microbial genes in stool sample they collected from 124 individuals. In March they published a list of 3.3 million genes.

“The variation in our microbiomes emerges the moment we are born.

“‘You have a sterile baby coming from a germ-free environment into the world,’ said Maria Dominguez-Bello, a microbiologist at the University of Puerto Rico. Recently, she and her colleagues studied how sterile babies get colonized in a hospital in the Venezuelan city of Puerto Ayacucho. They took samples from the bodies of newborns within minutes of birth. They found that babies born vaginally were coated with microbes from their mother’s birth canals. But babies born by Caesarian section were covered in microbes typically found on the skin of adults.

“‘Our bet was that the Caesarian section babies were sterile, but it’s like they’re magnets,’ said Dr. Dominguez-Belin.

“‘We continue to be colonized every day of our lives. ‘Surrounding us and infusing us is this cloud of microbes,’ said Jeffery Gordon of Washington University. We end up with different species, but these species generally carry out the same essential chemistry that we need to survive. One of these tasks is breaking down complex plant molecules. ‘We have a pathetic number of enzymes encoded in the human genome, whereas microbes have a large arsenal,’ said Dr. Gordon.

“In addition to helping us digest, the microbiome helps us in many other ways. The microbes in our nose, for example, make antibiotics that can kill dangerous pathogens we sniff. Our bodies wait for signals from microbes to fully develop. When scientists rear mice without any germ in their bodies, the mice end up with stunted intestines.

“One way the immune system fights

pathogens is with inflammation. Too much inflammation can be harmful so we have immune cells that produce inflammation-reducing signals. Last month, Sarkis Mazmanian Jule L. Round at Caltech reported that mice reared without microbiome can't produce an inflammation-reducing molecule called 11-10.

"The scientists then inoculated the mice with a single species of gut bacteria, known as *Bacteroides fragilis*. Once the bacteria began to breed in the guts of the mice, they produced a signal that was taken up by certain immune cells. In response to that signal, the cells developed the ability to produce 11-10.

"Scientists are not just finding new links between the microbiome and our health. They're also finding that many diseases are accompanied by dramatic changes in the makeup of our ecosystems. The Imperial College team that discovered microbes in the lungs, for example, also discovered that people with asthma have a different set of species than healthy people. Obese people also have a different set of species in their guts than people of normal weight.

"In some cases, new microbes may simply move into our bodies when disease alters the landscape. In other cases, however, the microbes may help give rise to the disease. Some surveys suggest that babies delivered by Caesarian section are more likely to get skin infections from multiple-resistant *Staphylococcus aureus*. It's possible that they lack the defensive shield of microbes from their mother's birth canal.

"Caesarian sections have also been linked to an increase in asthma and allergies in children. So have the increased use of antibiotics in the US and other developed countries. Children who live on farms – where they can get a healthy dose of microbes from the soil – are less prone to getting autoimmune disorders than children who grow up in cities.

"Some scientists argue that these studies all point to the same conclusion: when children are deprived of their normal supply of microbes, their immune systems get a poor education. In some people, untutored immune cells become too eager to unleash a storm of inflammation. Instead of killing off invaders, they may damage the host's own body.

"For more than a century scientists have been investigating how to treat patients with beneficial bacteria. But probiotics as they are sometimes called, have had limited success....

"Dr. Khoruts and his colleagues have

carried out 15 more fecal transplants, 13 of which cured their patients. They're now analyzing the microbiome of their patients to figure out precisely which species are wiping out the *Clostridium difficile* infections. Instead of a crude transplant, Dr. Khoruts hopes that eventually he can give his patients what he jokingly calls 'God's probiotic' – a pill containing microbes whose ability to fight infections has been scientifically validated.

"Dr. Weinstock, however, warns that a deep understanding of the microbiome is a long way off.

"In terms of hard-boiled science, we're falling short of the mark,' he said. A better

picture of the microbiome will only emerge once scientists can use the genetic information Dr. Weinstock and his colleagues are gathering to run many more experiments.

"It's just old-time science. There are no short-cuts around that,' he said."

However, it is an example of exciting pioneering occurring in so many scientific areas. All of which highlights the ever mounting importance and value of human capital. A wrong time, most certainly, for governments to wipe out from their thinking and their accountancy the key value of human capital as the most rewarding investment a society can make.

William Krehm

Long-term Economic Pain

The New York Times (27/07) under the above heading sums up the matter: "The pain coursing through American families is all too real and no one seems to know what to do about it. A rigorous new analysis for the Rockefeller Foundation shows that Americans are more economically insecure now than they have been in a quarter of a century, and the trend lines suggest that things will only get worse.

"Rampant joblessness and skyrocketing medical costs are among the biggest factors tearing at the very fabric of American life so painfully put together in the early post-World War II decades.

"The analysis was done by a team of researchers led by Professor Jacob Hacker of Yale University. They created an economic security index, which measures the percentage of Americans who experience a decrease in their household income of 25% or more in one year without the financial resources to offset that loss....

"Simply stated, more and more families are facing utter economic devastation, completely out of money, with the jobs, savings and retirement funds gone, and nowhere to turn for the next dollar.

"Economic insecurity has been increasing for at least a generation.

"In 1985 when the unemployment rate was 7.2%, the portion of American families that could be counted as economically insecure by the terms of this index was 12%. Professor Hacker explained that the percentage would naturally tend to rise or fall with improvements or deterioration in the economy.

"But...over the past few decades the per-

centages of insecure Americans relative to any given level of the economy has tended to steadily rise. So in 2002, coming out of a mild recession, there was a 5.8% unemployment rate, but the percentage of economically insecure families had jumped to 17.

"All of the data for 2009 are not yet in, but the research team projects, conservatively, that more than 20% of Americans experienced a 25% or greater loss of household income...over the prior year – the highest in at least a quarter of a century.

"A decrease of this magnitude in available income is a heavy blow. As the study points out, 'The typical individual who experiences a decline of at least 25% in household income requires between six and eight years for income to return to the previous level....'

"The bottom is falling out for increasing numbers of Americans, and with the national employment situation stuck in an extended horror zone there is little to stop the free fall.

"According to the study, 'Between 1985 and 1995, the typical (median) drop among those experiencing a 25% or greater available income loss was about 38.2%; between 1997 and 2007 it was 41.4%.

"Only the very well-to-do are out of the range of this buzz saw. 'The fact that Americans are facing a very real and growing risk of large-scale economic loss is true across the spectrum, said Mr. Hacker. 'It's true of blacks more than whites, but it's true of whites as well. It's true of less affluent people...but it's true of the affluent as well....

"Policy makers seem bewildered by the

terrible economic state of ordinary working Americans, including those once considered solidly in the middle class. Despite warnings back in 2008 that we were on the verge of another great depression, the big financial institutions and corporative America seemed to be doing just fine now. But aver-

age Americans are hurting with no end of pain in sight.

“More than 14 million people are out of work and many more are either underemployed or so discouraged that they’ve just stopped looking. Big corporations, sitting on fat profits even as the economy continues

to struggle, have made it clear that they are no interested in putting a lot more people to work any time soon.

“Long-term solutions that have to do with extensive job creation and a strengthening of the safety net are required. But that doesn’t seem to be on anyone’s agenda.”■

On the Ambiguities of Closed Minds

While assessing the economy’s prospects of recovery versus the finality of economic collapse, our political leaders, unwittingly, are betraying what they are outdoing themselves to cover up: the absence of anything that could pass for accountability.

The Wall Street Journal (23/07, “A Set of Scribbled Notes Helped Settle AIG Probe” by Thomas Catan and Amir Efrati) tells a skewed tale: “Joseph Cassano was once portrayed as a villain of our times.

“His derivatives unit helped drag insurance giant American International Group into near-collapse, prompting a \$182 billion federal bailout in 2008 that remains contentious today. *Vanity Fair* dubbed him: ‘The Man Who Crashed the World.’

“Prosecutors, envisioning a high-profile criminal case, found invective-strewn recorded phone calls appearing to suggest Mr. Cassano misled investors about AIG’s bets on subprime mortgages, according to people familiar with the matter. They interviewed AIG senior management and the company external auditor, and came away thinking Mr. Cassano hadn’t properly disclosed multi-billion-dollar accounting changes that drastically cut the size of the estimated losses, these people said.

“Yet in May, the Justice Department closed its probe without bringing charges. The Securities and Exchange Commission soon followed suit.

“A *Wall Street Journal* examination of how the probe fell apart shows the tremendous complexity of the financial system in 2007-8. Helping scuttle the probe was a set of cryptic notes scribbled by an auditor on the bottom of a spreadsheet and buried among millions of pages of documents.

“In June, a relaxed-looking Mr. Cassano appeared before a panel set up by President Barack Obama to investigate the causes of the financial crisis. Mr. Cassano defended his actions at AIG, including the big accounting changes. He said he would have saved the government a lot of money if it had hired him to help liquidate the deriva-

tives unit he once headed. Mr. Cassano declined to comment on this article.

“Big financial crises are usually followed by big criminal convictions. Charles Keating became the face of the Savings and Loan crisis of the 1980s, just as Michael Milken symbolized the collapse of the junk-bond market later that decade. In the early 2000s, WorldCom’s Bernie Ebbers and Enron’s Jeffrey Skilling were imprisoned for their role in accounting frauds.

“Nearly three years after the greatest financial collapse in 80 years, there have been no similar landmark convictions, with the notable exception of Ponzi schemer Bernard Madoff. At the heart of prosecutors’ conundrum: bankers may have been foolhardy, rash or even unethical. But in doing so, did they commit any crimes?

“Unlike previous investigations, prosecutors haven’t found physical evidence of fraud, such as false documents designed to hide crimes. Nor have prosecutors been able to convince lower-level employees to plead guilt and testify against senior executives.

“Instead, today’s fraud cases have been aimed around contrasting bankers’ public statements to investors with their private emails and phone conversations. The aim is that they intended to deceive investors by withholding crucial information. So far, industry executives and their lawyers have been able to argue that poor business – not deliberate deception – fueled the errors.”

I have a different interpretation of the phenomenon. It is further evidence of the utter disregard of the ever greater importance of recognizing the key importance of human capital for allowing mankind to preserve and expand what was learned at tremendous cost during the Great Depression and World War II.

Hardly had the mass slaughter stopped when Washington sent hundreds upon hundreds of economists to Japan and Germany to study the destruction to foretell how long it would be before the two defeated Axis leaders would become formidable traders

on world markets again. Some sixteen years later, one of these Theodore Schultz of the University of Chicago, published a book in which he explained why he and his colleagues had been so wrong in their forecasts.

It was, he decided, because they concentrated on the physical destruction and attributed little importance to the fact that the highly educated, and talented work force had come through the conflict essentially intact. From this in 1961 he concluded that human capital is the most rewarding investment a government can make.

For this Schultz was celebrated, decorated and after a few years the very memory of his name and work suppressed. That more than anything else explains the hopeless mess that the governments of the world are making of setting the economy right again today. Treating the most crucial *investment* – human capital – as debt when it has been prepaid, and its renewed budgeting has all the earmarks of further investment can only lead society like sheep into the slaughterhouse. Translated into actual budgetary terms, atomic weaponry and space exploration for strategic military advantage is one of the few uncontested expenditures of our most powerful governments today.

High technological advance which obviously is indispensable for the survival of a rapidly expanding, urbanized world population is being curried and ridden as a one-legged horse.

To bring sanity and responsibility into our economic system we must turn to our universities to live up to their name – sites for the meeting and interaction of great human thinking. The literature of the great economists, logicians philosophers, natural scientists, our history, must be freed to assess what has currently come to pass as economic science. Failing that, guaranteed doom lies ahead.

Nothing less than that must be the program at the COMER Congress that will take place shortly.

William Krehm

Can Our Unbridled Mega-banks Afford "The Best Investment Society Can Make?"

It is not put quite that openly, but the theme haunts the issue of *The New York Times* (25/06) as a nightmare. Right on page 1 we have "School is Turned Around but Cost Gives Pause" by Sam Dillon: "Los Angeles – As recently as 2008, Locke High School here was one of the nation's worst failing schools, and drew national attention for its hallway beatings, bathroom rapes and rooftop parties held by gangs. For every student who graduated, four others dropped out.

"Now, two years after a charter school group took over, gang violence is sharply down, fewer students are dropping out, and the test scores have inched upward. Newly planted olive trees in Locke's central plaza have helped transform the school's concrete quadrangle into a place where students congregate and do homework.

"It's changed a lot," said Leslie Maya, a senior. "Before, kids were ditching school, you'd see constant fights, the lunches were nasty, the garden looked disgusting. Now there's security, the garden looks prettier, the teachers help us more."

"Locke High represents both the opportunities and challenges of the Obama administration's \$3.5 billion effort, financed largely by the economic stimulus bill, to overhaul thousands of the nation's failing schools.

"The school has become a Mecca for reformers, partly because the Department of Education Web site hails it as an exemplary turnaround effort.

"But progress is coming at considerable cost, an estimated \$15 million over the planned four-year turnaround, largely financed by private foundations. That is more than twice the \$6 million in federal turnaround money that the Department of Education has set as a cap for any single school.

"Skeptics say that the Locke experience may be costly to replicate."

But what happened to "the greatest lesson to come out of World War II"? Since it has been lopped out of the official record, and made unmentionable even in publications of the caliber of *The New York Times*, we may be pardoned for telling the tale once again. It can in fact be found already retold on page 9 of this issue. There, too, the reader will find reference to the book published by Theodore Schultz in 1961, in which he

concluded that their prediction had proved wide of the mark, because they had concentrated on the physical destruction and paid little attention to the detail that the human capital had come out of the conflict almost intact. Schultz went further, and from that concluded that human capital was the most rewarding investment a government could make. That conclusion has been forgotten and government investments in human capital appears on the budgets of virtually all the countries of the world today not as investment but as debt. Clearly that leaves public accountancy and public morality standing on their heads. It does, however, empower those in the saddle to sell or lease for peanuts: bridges, highways, real estate, carried on their books at zero value.

A Truncated Tale

But let us resume the *Times*' truncated tale: "When people hear we spent \$15 million, they say, 'You're insane' said Marco Petruzzi, chief executive of Green Dot Public Schools, the non-profit charter group that has remade Locke. 'But when you look closely, you see it's not crazy.'

"Locke High, with 3,200 students sprawls across six city blocks in south-central Los Angeles. The school's principal in 2007 complained publicly that the Los Angeles United School District had made it a dumping ground for problem teachers.

"Kevin Rauda, a senior, recalled a teacher who read newspapers in class instead of teaching. In spring 2008, only 15% of students passed state maths tests.

"Green Dot, which operates charter schools in Los Angeles and one in the Bronx, won control of Locke from the district in 2008 and began a turnaround effort.

"In August 2008, Kevin King, a retired police lieutenant hired by Green Dot, toured Locke's campus and found broken windows, smashed lights, and security cameras that did not work. Teachers' cars were parked helter-skelter, including on some handball courts; gang members were selling drugs on others.

"Kids couldn't even go to the bathroom without being pocket-searched or hassled," Mr. King said.

"He put together a new security force to expel the gangs. Green Dot fixed the lights

and cameras, painted over graffiti, reorganized the parking, and hired bus companies to transport 500 students who previously walked dangerous streets to school.

"Green Dot divided Locke into small academies. Several, modeled on the charters it operates elsewhere, opened in fall 2008 with freshman classes of 100 to 150 students and are to reach full enrollment of 500 to 600 students by fall 2011.

"Other academies concentrate on remedial classes for older students, including some returning from jail. Another focuses on preparing students for careers in architecture.

"Green Dot required Locke's 120 teachers to reapply for their jobs. It rehired about 40, favoring teachers who showed enthusiasm and a belief that all Locke students could learn. The campus stays open each day until early evening for science tutoring, band and other activities.

"State test scores administered in spring 2009, just months after the Green Dot makeover began, Locke remained among California's lowest-performing schools. Still, a dozen students said in recent interviews that the school was safer and instruction had improved.

"Hundreds of school districts across the nation will soon be trying similar makeovers, prodded by the Obama administration's push to remake the nation's worst schools, and the availability of \$3.5 billion in federal money.

"But if they rely on federal money alone, they will have to spend less than Green Dot.

"Under rules set by Congress, districts can apply for up to \$8 million for each failing school, to be spent over three years.

"During a Senate hearing in April, Senator Al Franken, Democrat of Minnesota, congratulated Mr. Petruzzi on the Locke transformation, but also suggested its reli-

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ance on philanthropic donations would make it difficult to imitate.

“I’m thinking, how salable is this,” Mr. Franken said.

“In interviews, Mr. Petruzzi and other Green Dot officials offered a budget overview. Before and since Green Dot’s takeover, tax dollars have financed Locke’s annual operating budget of upward of \$30 million, which during the four-year turnaround will total about \$115 million, he said.

“By then expenditures will have exceeded that four-year, tax-supported budget by

about \$15 million, with philanthropies making up most of the difference. Over the four years, Green Dot is to spend about \$2 million on increased security and busing. It spent about \$700,000 to create a classroom for a new architectural academy.

“Green Dot has also spent several million dollars for additional classroom space because hundreds of students who had cut school or dropped out now show up for class, Mr. Petruzzi said.

“Dividing Locke into academies resulted in extra personnel costs, Mr. Petruzzi said,

because each academy has its own principal and other staff members.

“Another cost: the salaries of two psychologists and two social workers who help students endure hardships like losing a sibling to gang warfare, or being evicted. They have helped prevent suicides this year, said Zeus Cubias, an assistant principal.

“Some new services have cost Green Dot nothing. Ms. Maya’s grades have improved since a teacher noticed that she could not see the blackboard. Her parents are unemployed, and she had no money for glasses. But she had her eyes tested at a mobile eyes clinic that visited Locke in October, where vision Service Plans, a nonprofit provider, donated eye-glasses to her and 200 other students.

“Experts are debating whether Locke is a good model for other turnarounds.

“Justin Cohen, a turnaround expert at MassInsight, a Massachusetts nonprofit organization, said most districts could expect to spend \$2 million to \$3 million over three years to overhaul a failing school. Costs often include teacher training and extending the school day, he said.

“I don’t doubt they’re putting all those resources to good use,” Mr. Cohen said of Locke’s \$15 million costs. “But that’s high.”

“Tim Cawley of the Academy for Urban School Leadership, a non-profit group leading several turn-around efforts in Chicago, disagreed, arguing that even expenditures surpassing \$15 million on a big school could be a smart national investment.

“We’re wasting billions every year by not fixing these schools,” Mr. Cawley said, “because the students they’re not educating end up filling our prisons.”

Note well that we’ve pretty well circled the conceptual globe before hearing the word “investment” that has been so thoroughly ripped out of permissible concepts. But it gives us the measure of the immense job done to have buried what had been recognized as “the best investment a government could make.” At a time when the governments of the world are seen as choking in debt, would it not be a short-cut to what was recognized as the greatest lesson to have come out of World War II?

That confusion of our government’s “best possible investment can make” with a charity-case for keeping needy citizens out of jail implies a reversal in not only the wealth structure but the power structure of our society. In essence our society is being run without accountancy that can stand the light of day.

W.K.

William Krehm

The Holy Spirit of High Finance

The New York Times (01/21, “Banks’ Derivatives Activity Falls Under IRS Scrutiny” by Lynnley Browning) informs us: “Federal authorities are scrutinizing certain financial derivatives that may enable Wall Street banks to avoid collection of billions of dollars in withholding taxes on stock dividends.

“The instruments, known as equity swaps, mimic ordinary shares and give investors like hedge funds the benefits of stock ownership, including payments similar to dividends, without actually owning the shares. Big banks also benefit from the swaps because, under federal tax rules, the banks may avoid paying a 30% tax that is normally levied on stock trades.

“The Internal Revenue Service is examining whether banks are using the swaps to mask who really owns the shares underlying the instruments, thereby avoiding collecting dividend withholding taxes.

“In effect, the IRS suspects that the banks are disguising who owns the stock to help their offshore hedge fund clients avoid the withholding tax the banks are supposed to collect. Mark H. Leeds, a tax lawyer at Greenberg Traurig, said on Wednesday that the scrutiny indicated the IRS increasingly viewed equity swaps as ‘evidence of tax avoidance.’

“In a directive issued last Thursday, the IRS instructed its field agents on how to audit American banks with an eye to ‘uncovering and developing cases related to certain swap transactions’ that may have been executed to avoid tax with respect to US source dividend income paid to offshore hedge funds and foreign investors.

“The audit guidelines reflect suspicions that all cross-border equity swaps are tax-avoidance transactions, even though the

IRS’s own regulations treated these transactions favorably,” Mr. Leeds said.

“Tax lawyers regard the directive significant because it concerns a vast, unregulated market and could lead to tax disputes between the IRS and Wall Street banks. The exact size of the equity swaps market is difficult to ascertain, but the Bank of International Settlements puts the notional value of all equity-linked swaps and forwards, which are similar derivatives, at nearly \$1.7 trillion as of last June.

“The IRS made rooting out abuses with equity swaps a top priority in March. A bill in the Senate, which passed the House last December, would sharply curtail the tax benefits on equity swaps.

“In September 2008, a Senate subcommittee issued a scathing report ‘Dividend Tax Abuse,’ that accused Wall Street banks of marketing and selling complex taxes on dividend payments.

“The report said trades in equity swaps had flourished over the last 10 years and grown lucrative for Wall Street banks.

“In an equity swap, an investor like a hedge fund typically offers to lend a certain amount of stock to a bank. In return the banks promises to pay the hedge fund, at a future date, any gains and dividends on the stock, and to return the stock when the contract expires. Because the swaps are derivatives, no shares actually change hands.

“The IRS directive identified four types of swaps: cross in-cross out, cross in-inter-broker dealer out, cross-in foreign affiliate out, and synthetic equity transactions.”

It can be summed up with as reference to most religions developing a Holy Spirit, that is here, there, impossible to quantify, or nail down, or diminished.

Has Our Planet Been Abused Beyond Control?

The New York Times (01/05, “New Attempt to Divert Oil With a Dome” by Clifford Krauss) recounts a shattering interplay of deep oil drilling in the Caribbean gone amok in an interplay of unruly storms in the upper atmosphere: “Houston – Unable for six weeks to plug the gushing oil well beneath the Gulf of Mexico, BP renewed an effort Monday to use a dome to funnel some of the leaking crude to a tanker on the surface.

“A similar attempt failed three weeks ago, but officials said they had resolved some of the technical problems that forced them to abort last time.

“If successful – and after the string of failures so far, there is no guarantee it will be – the containment dome may be able to capture most of the oil, but it would not plug the leak. Its failure would mean continued environmental and economic damage to the gulf region, as well as greater public pressure on BP and the Obama administration, with few options remaining for trying to contain the spill any time soon.

“A lasting solution for the leak may be months away, after engineers complete the drilling of a relief well, which would allow them to plug the leaking well with cement.

“On Monday, engineers positioned submarine robots that will try to shear off a collapsed 21-inch riser pipe with razor-like wire studded with bits of industrial diamonds. If that is achieved, officials will need at least a couple of days to position a domelike cap over the blowout preventer, which failed to shut off the well when the Deepwater Horizon oil-rig exploded on April 20, killing 11 workers.

“The trapped oil would then be funneled through a hose to ships floating near the well.

“But, like all of BP’s efforts so far, this method has never been tried at such depths before this spill. Moreover, if kinks in the riser are now reducing the amount of oil escaping, cutting the riser could unleash a greater flow. And the greatest worry of all may be the arrival of hurricanes in the gulf. Hurricane season officially begins on Tuesday.

“Engineers and technicians working on the response said that an active hurricane season, predicted by meteorologists, could not only push more oil ashore, but also cause weeks of delays in efforts to contain

the spill.”

It was as though resentful nature and overreaching human hubris were in league to block the overweening ambitions of human arrogance.

“Once a hurricane appears to be heading for the gulf, officials will have to disconnect the hose from the container on top of the well and retreat to port, leaving an unabated flow of oil into the water.

“‘Safety first,’ said Andrew Gowers, a BP spokesman. ‘We build in hurricane preparedness in operations and that requires us to take the necessary precautions.’

“Such precautions may stall the drilling of relief wells for weeks or more if a hurricane threatens.

“‘Will hurricanes trump the capping procedures or even the whole operation?’, said Donald Van Nieuwenhuise, director of petroleum geoscience programs of the University of Houston. ‘That’s the wild card.’

“Pressure is building on the Obama administration from Congress to take greater control over relief operations, and residents in the gulf region, are increasingly directing their frustration at BP as more oil washes ashore each day.

“Tony Hayward, BP’s chief executive, drew criticism on Sunday when he said his company’s sampling of water had suggested that all the leaking oil was coming to the surface, despite several reports from independent researchers that underwater plumes were stretching for miles.

“Representative Edward J. Markey, Democrat of Massachusetts and chairman of the House Energy and Environment Subcommittee, said Monday that he had sent a letter to Mr. Hayward requesting documentation to substantiate his claims.

“Meanwhile, attention turned to the latest dome effort.

“‘Everything is at stake,’ said Larry Goldstein, a director of the Energy Policy Research Foundation, an organization partially financed by the oil industry. ‘If this doesn’t work, you are looking at August before you can kill the well. That would mean that oil would be seeping into the Gulf, into our wetlands and into our way of life at the rate of 15,000 or 20,000 barrels a day – you pick the number.’

“An immediate challenge lies in severing the riser without causing an even bigger leak. Carol M. Browner, the White House envi-

ronmental and energy adviser, has warned that the well could leak an additional 20 percent. The hope is that this would be a temporary problem until the containment dome is installed.

“The dome procedure began two days after a maneuver known as a ‘top kill’ was aborted late Saturday, when officials were unable to stanch the flow of oil with heavy drilling mud and other materials.

“‘This is a containment operation that is more straightforward,’ Robert Dudley, BP’s managing director, told CNN on Sunday morning. He said containing most of the escaping oil until a relief well can be drilled is ‘not a bad outcome compared to where we are today.’”

The Missing Information on Rescue Apparatus

“Mr. Dudley and other senior company officials have said they do not expect that the operation, even if this fails, will worsen the flow of oil significantly. BP officials said a week ago that they estimated that a 10 to 15% increase was possible until the cap is firmly in place.

“But a technician working on the project expressed concerns that engineers cannot be sure how much more oil might escape if the operation fails.

“‘We’re all concerned about it,’ said the technician, who spoke on condition of remaining unnamed because he is not authorized to speak publicly for the company. ‘We simply do not have the data about the internal geometry of the blowout preventer’ to determine what volume of oil is being contained by the damaged blowout preventer and any damaged equipment or debris inside it.’

“During the previous attempt to install as containment dome, icy water rushed into the box and filled it with natural gas hydrates – ice crystals formed from water and natural gas under the high pressure a mile under the sea. There was no room left for escaping oil in the dome, which also became buoyant and rose to the surface.

“This time, tubes will deliver heated salt water and antifreeze to the vessel in an effort to prevent the formation of hydrates.

“But the technician said that the formation of hydrates was still possible and they could still rush into the vessel through the narrow crack between it and the top of the

blowout preventer.

“Greg McCormak, director of the Petroleum Extension Service at the University of Texas, Austin, said he believed there was a good chance that the new effort would work, ‘if they can stop the hydrates from

forming.’ But he cautioned that a waste case scenario existed in which hydrates disrupted the effort and more oil is released from the severed riser.”

Invaded and offended through every possible aperture, Nature seems clawing and

growling and threatening with every limb. Perhaps we should lower our greedy grabbing and learn to live in a measure of peace with her. But to make that possible we must learn to live in peace with ourselves.

W.K.

Learning to Live and Fly as Bankrupts or Stop Cooking the Books

As we go to press the imminent declaration of bankruptcy of Japan Airlines Corp. is not likely to lower the demand from US passengers. That is only the latest indication that bankruptcy has become a life style imposed on Americans. American bankers would seem to prefer it to serious accountancy.

But let us quote *The Toronto Star* (11/01, “Japan Air braces for bankruptcy impact by Mary Schoangenstein of Bloomberg News): “All of the largest US airlines except AMR Corp.’s American Airlines and Southwest Airlines Co. have been through at least one bankruptcy during the past two decades. In September 2005, half of the US airline capacity was operating under Chapter 11 protection. ‘There shouldn’t be any impact,’ said Jerry Glass, president of Washington-based F&H Solutions and a former executive at US Airways Group Inc., which filed for bankruptcy in 2002 and again in 2004. ‘US passengers are used to seeing their airlines being in bankruptcy and continuing to operate with no disruptions whatsoever. So it really doesn’t affect bookings.’

“Japan Air’s largest banks are prepared to agree to a bankruptcy court-led restructuring, according to four people familiar with the matter. Japan Air is set to file for bankruptcy the week of January 18, and the Enterprise Turnaround Initiative Corp. will agree to private financial aid, said a person familiar with the negotiations who declined to be identified.

“Because bankruptcies are less common in Japan than in the US, Japan will have to communicate to the public that a bankruptcy doesn’t mean operations will stop, said Michael Derchin, an analyst at FTN Equity Capital Markets Corp. in New York.”

Another way of putting it would be: “In the US bankruptcy has been imposed on society as a life style that turn out very convenient for the large banks, and far more useful for enforcing the large banks’ effective control over society.”

Indeed, it was on the basis of Japan’s effective reshaping of its society after its

crushing defeat in WW II that the Japanese achievement inspired Washington to grasp what was the greatest lesson to emerge from WW II. Immediately after the armistice the US government sent many hundreds of economists to Japan and Germany to assess the destruction to predict how long it would take for these great trading powers to be in shape to resume such roles again. Some 18 years later one of these Theodore Schultz of the University of Chicago wrote a book explaining how wide of the market their forecast had been. He went further and concluded that he and his colleagues had concentrated on the physical destruction and assigned no importance to the fact that the highly educated, disciplined and talented work force had come out of the struggle virtually intact. He concluded with a stroke of genius: human capital is the most profitable investment a government can make.

Japanese Strategy Permitted Higher Proportion of Profit Retention

The Japanese did not stop there but confirmed such a conclusion. Even while under the tutelage of the American victor, they reshaped their economy to emerge from their crushing defeat with a strengthened, and completely reformed economy. They decided that rather than counting on textile imports, for which they had to import the raw materials, they would concentrate on heavy engineering that would permit them to retain a far higher proportion of the profits from such sales within the country. So bit step by step they produced the iron and steel capacity, then the engineering products where Japanese ingenuity played an ever increasing role. kept their currency competitively low by investing much of their profits abroad.

All the while, while showing the proper respect for the American advice, which was never lacking, they in fact avoided taking it seriously.

The impending bankruptcy of JAL is seen as something traumatic whereas with

American lines it is a hard fact of American life.

On the reports of the impending bankruptcy of JAL, “Andrea Huguely, a spokeswoman for Texas-based American Airlines, declined to comment on any impact from a JAL bankruptcy, saying such reports are ‘just speculations.’

“John McCulloch, Oneworld chief executive officer, didn’t return a call seeking comment.

“In addition to American and JAL, Oneworld includes British Airways PLC, Hong Kong-based Cathay Pacific Ltd., Finland’s Finnair Oyj, Spain’s Iberia Lineas Aer de Espana, Chile’s Lan Airlines, Hungary’s Malev, Grupo Mexicana de Aviacion, Australia’s Qantas Airways, and Royal Jordanian Airlines.

“American, joined by private equity firm TPG, is considering boosting its pending \$1.1 (US) JAL investment offer, people familiar with those talks said on Jan. 7 Delta is ‘willing and able’ to raise more capital beyond its \$1 billion package, which includes a \$500 million investment, President Ed Bastian said.

“American and Delta also have said they will pursue their offers even if JAL files for bankruptcy. Delta is the world’s largest airline, based on passenger traffic, followed by American. Delta is continuing talks with JAL and Japanese government officials ‘about a long-term strategic partnership that would provide hundreds of millions in additional revenue to JAL annually,’ said spokeswoman Betsy Talton.”

For a few years Schultz was honored and even awarded for his great discovery, and then after a few years, even his name is mentioned except – we would prefer being wrong on this – by COMER.

That, however, explains why American airlines have embraced bankruptcy as almost the normal state in which airlines operate, while the Japanese Air Lines must just now begin to acquire that degrading art.

W.K.

Erasing the Most Important Economic Lesson to Come Out of World War II has Stood Official Policy on Its Head

Elsewhere in this issue of *ER* and in just about in every issue of *ER* since its first publication we have made the point that higher prices are not necessary inflation, identified as a rise in prices due to an excess of demand. For propositions cannot be reversed and remain valid. Example: if I hold a loaded pistol to my head and push the trigger, I fall dead. But that does not make the reverse relationship valid. If I fall dead, it does not mean that I have suicided. It might have been heart failure.

In its May 1970 issue what was the leading journal on economic theory in France, *La Revue économique*, carried a 70-page article of mine developing the idea that not all rising prices indicate an excess of demand over supply. It could be that more of the production is not sold on the market, but is paid for by taxation which turns up in market price. This I dubbed the “social lien.” It was only after the essay appeared that I learned why it had been purchased and published without delay. I had sent the manuscript to no less than 30 publications throughout the world, but only after it appeared did I realize why it had been snapped up.

On the editorial board of *La Revue économique* there was not only the greatest economic historian of his day, but two statisticians who had studied the price increase in relation to market supply and demand and found that there was no correspondence between the two. They concluded that an unknown factor having nothing to do with the relationship of market supply and supply existed, but had still not been identified. At which point the postman delivered my unsolicited solution to their problem.

To distinguish higher prices due not to an excess of market demand from price increases due to the increasing portion of the national product that had to do with taxation that paid for government services paid by the private sector. In the very favorable review of the essay carried in the economic journal of the University of Cambridge, the critic particularly praised the title I applied to the newly recognized factor in the price

level – the “social lien.”

That led to decades of collaboration with the leading school of French economic reformers, particularly with the late François Perroux, whom I brought to a meeting at the University of Waterloo, arranged by John Hotson. Thus COMER was born.

History from classical Athens forward was our treasure trove as was the greatest lesson to have come out of World War II. As soon as the Armistices were signed Washington had sent many hundreds of economists to Japan and Germany to assess the war damage and estimate how long it would take for those two former great trading powers to recover.

Years later, in 1961, one of these economists, Theodore Schultz, of the University of Chicago, published a book explaining why the forecasts of his colleagues had been so wide of the mark. It was, he concluded, that they had concentrated on the physical destruction, and had attributed little importance to the fact that the highly trained and gifted human forces had come out of the war virtually intact. From this he concluded that human capital, which would include not only education and health services but the environment, was the most rewarding investment governments can make.

It is not only prepaid, but spending that capital has all the features of further investment. I need only mention that the children of educated parents are more readily educated, healthier, and socially adjusted. For his great conclusion Schultz was celebrated, awarded the Bank of Sweden Nobel Prize for Economics, but within a few years purged from the memory of economists who might wish to retain their posts in universities, government or just about any other institution.

And in that way, not only Schultz’s name, but his epoch-making conclusion have been forgotten. I know of no other organization than COMER that mentions him today. The “greatest investment that a government can make” is today treated as government debt to justify slashing budgets for education, health,

the environment, and even physical infrastructures of a rapidly urbanizing world.

And, in Canada, where the legislation that nationalized the central bank in 1938 to this day remains on the law books, is disregarded. Our government finances its needs by borrowing money, when it could finance them at a nominal cost through its own bank.

Along with an understanding that money is backed only by the creditworthiness of government, this explains the financing during a quarter of a century of a prosperous postwar during which Canada was enabled to catch up with a decade of deep depression and welcome millions of mostly penniless immigrants from devastated Europe. But all this has been buried as our society has reverted to the making the world safe for speculative banking.

Once you mistake human capital for plain debt to be dealt with by cutting investments in human capital and higher interest rates you are standing matters on their head, eliminating anything that could be mistaken for accountancy.

This leads us to the lead article in *Resource World Magazine*, Vol. 8, Issue 7, “Why bullion is outperforming stocks – investing doesn’t have to be an either or decision” by Nick Barishelf, President/CEP, Bullion Management Group Inc.

Bullion Is a Safe Haven During Turbulent Times

We quote: “When choosing between mining stock and physical bullion and physical bullion, it is essential to remember that these belong to different asset classes with entirely different risk/reward attributes. Mining stocks and bullion perform quite differently when the global economic environment is in turmoil, as is the case today.

“Banking crises, trillion-dollar deficits and the accelerating depreciation of many of the world’s major currencies do not create positive conditions for equity markets, which is why investors are fleeing to the safety of physical bullion.”

Note well: not only is there a flight to the long outgrown notion that gold is money which was replaced by the realization that it is the credit of a government that really is what backs a currency, but it has to be actual bullion since the credit of gold-producing or gold-trading concerns is no long dependable. But let us proceed with this most interesting quotation.

“This flight to bullion was confirmed

during the stagflationary 1970s....

“While shares of Homestake Mining, the largest North American producer at the time, increased by an impressive 800% during the 1970s, physical gold increased 1,500%; during the same time period. While it is true that many junior mining companies outperformed both bullion and Homestake in the 1970s, producing impressive returns for their shareholders, many other juniors faded into obscurity resulting in painful losses.

“The volatility associated with junior mining companies versus blue chip producers and physical bullion makes them a purely speculative choice. However, if you have a high risk tolerance and a good advisor, then a small allocation to junior mining corporations may be appropriate, especially those with established ounces in the ground. Juniors with a new discovery can generate substantial gains, but they are still highly speculative investments that can be very volatile.”

Bullion Outperforms Mining Stocks During Financial Crises

“While mining stocks can generate impressive returns during an uptrend in precious metals prices, they do not outperform bullion during times of crisis, as in the financial meltdown of 2008....

“When global economic conditions deteriorate, investors inevitably seek a safe haven for their wealth, rather than more speculative investments....

“Blue chip gold stocks like Goldcorp and Barrick Gold can be good investments because, unlike juniors, they are less likely to wither away to nothing and frequently offer dividends. But timing is crucial because gold producers’ shares can also be quite volatile.

“Other precious metals investment options might include Mining Exchange Traded Funds [ETFs] which hold a basket of gold producers, but be prepared for a daily roller coaster ride. Regardless of the type of investments chosen, every investor’s portfolio should be diversified and include precious metals....”

During very sharp market declines, mining stocks tend to become correlated to the broad equity markets rather than the price of bullion.

In short, just about everything that was learned during a decade of depression and five years of war has been erased from our government’s memory.

W. Krehm

An Updated Maginot Line in Contested Outer Space

The New York Times (26/01, “In Digital Combat, US Finds No easy Deterrent” reported by John Markoff, David E. Sanger and Tom Shanker, and written by Mr. Sanger) discloses an advanced military cybernet dimension to what had up to now been seen as a concern for freedom of peaceful information on the internet. We quote: “Washington – On a Monday morning earlier this month, top Pentagon leaders gathered to simulate how they would respond to a sophisticated cyber attack aimed at paralyzing the nation’s power grids, its communications systems or its financial networks.”

All this reaches some years back when Google Inc. was criticized for going along with Chinese restrictions on what could be reported by internet companies active in China. But Google was merely proceeding with supreme caution in handling what it was encountering extended far beyond the freedom of news reporting. It is now clearly involving a cyber attack – a term we must get accustomed to – the working backward to invade and paralyze power grids, communication systems and/or financial networks.

“The enemy [would have] all the advantages: stealth, anonymity and unpredictability. No one could pinpoint the country from which the attack came, so there was no effective way to deter further damage by threatening retaliation. What’s more, the military commanders noted that they even lacked the legal authority to respond – since it was never clear if the attack was an act of vandalism, an attempt at commercial theft, or a state-sponsored effort to cripple the US perhaps as a prelude to a conventional war.

“What some participants in the simulation knew – and others did not – was that a version of their nightmare had just played out in real life, not at the Pentagon where they were meeting, but in the far less formal war rooms at Google Inc. Computers at Google and more than 30 other companies had been penetrated, and Google’s software engineers quickly tracked the source of the attack to seven servers in Taiwan, with footprints back to the Chinese mainland.

“After that, the trail disappeared into a cloud of angry Chinese government denials, and then an ugly exchange of accusations

between Washington and Beijing. That continued Monday, with Chinese assertions that critics were trying to ‘denigrate China’ and the US was pursuing ‘hegemonic domination’ in cyberspace.

“These recent events demonstrate how quickly the nation’s escalating cyber battles have outpaced the rush to find a deterrent, something equivalent to the cold-war-era strategy of threatening nuclear retaliation.”

Drawing on the Language of Nuclear Deterrence

“So far, despite millions of dollars spent on studies, that quest has failed. Last week, Secretary of State Hillary Rodham Clinton made the most comprehensive effort yet to warn potential adversaries that cyber attacks would not be ignored, drawing on the language of nuclear deterrence.

“States, terrorists and those who would act as their proxies must know that the US will protect our networks,” she declared in a speech that drew an angry response from Beijing.

“Those who disrupt the free flow of information in our society or any other pose a threat to our economy, our government and our civil society.

“There is, in fact, an intense debate inside and outside the government about what the US can credibly threaten. A diplomatic demarche, or formal protest, like the one the State Department said was forthcoming, but still has not delivered, in the Google case? Economic retaliation? Criminal prosecutions?

“Inside the National Security Agency, which secretly scours overseas computer networks, officials have debated whether evidence of an imminent cyber attack on the US would justify a pre-emptive American cyber attack – something the president would have to authorize. In an extreme case – evidence that an adversary was about to launch an attacks intended to shut down power stations across America – some officials argue that the right response might be a military strike.

“We are now in the phase that we found ourselves in during the early 1950s, after the Soviets got the bomb,” said Joseph Nye, a professor at the Kennedy School at Harvard. “It won’t have the same shape as the nuclear

deterrence, but what you heard Secretary Clinton doing was beginning to explain that we can create some high costs for attackers.

“When the Pentagon summoned its top regional commanders from around the globe for meetings and a dinner with President Obama on January 11, the war games prepared for them had nothing to do with Afghanistan, Iraq or Yemen. Instead, it was the simulated cyber attack – a battle unlike any other they had engaged in.

“Participants in the Pentagon war game emerged with a worrisome realization. Because the Internet has blurred the line between military and civilian targets, an adversary can cripple a country – say freeze its credit markets – without ever taking aim at a government installation or a military network, meaning that the Defense Department’s advanced capabilities may be brought to bear short of a presidential order.

“‘The fact of the matter,’ said one senior intelligence official, ‘is that unless Google had told us about the attack on it and other companies, we probably never would have seen it. When you think of that, it’s really scary.’”

Another Maginot Line?

“William J. Lynn, III, the deputy defense secretary, who oversaw the simulation, said in an interview after the exercise that America’s concepts for protecting computer networks reminded him of one of defensive warfare’s great failures, the Maginot Line of pre-World War II France.

“Mr. Lynn, one of the Pentagon’s top strategists for computer network operations, argues that the billions spent on defensive shields surrounding America’s banks, businesses and military installations provide a similarly illusory sense of security.

“‘A fortress mentality will not work in cyber,’ he said. ‘We cannot retreat behind as Maginot Line of firewalls. We must keep maneuvering. If we stand still for a minute, our adversaries will overtake us.’”

“But if it is obvious that the government cannot afford to do nothing about such breaches, it is also clear that the old principles of retaliation – you bomb Los Angeles, we’ll destroy Moscow – just do not translate.

“Even Google’s engineers could not track, with absolute certainty, the attackers, who appeared to be trying to steal their source code and, perhaps, insert a ‘Trojan horse’ – a backdoor entry to attack – in Google’s search engines.”

That in fact is one of the scariest aspects

of the situation. We have repeatedly observed that the hopeless attempt to “lick inflation,” which really refers to a refusal to recognize the increasing amount of human capital that must be invested and is misrepresented as inflation, would recognize the growing essential investment in human capital for what it is. Mistaken for “inflation” to be suppressed with high interest rates this must lead our government into the next world war as the only final gamble. Add to this the anonymity of cybernetic attacks, and you have the perfect way for the final ultimate

gamble. Put it all together and if society survives another world war, there will be nobody clearly responsible for having brought it on. The war guilt will be as innocent as the current fight against “inflation” and the cyber attacks. Everything is based on unproven presumptions from our government’s supposed fears of “inflation” to the cyber attacks and the final war that could mark “paid in full” over a devastated civilization. A fog of anonymity spreads ultimate guilt into a false innocence of ambiguity.

William Krehm

The New York Times Turns a Critical Eye on the Politics of Big Finance

In its issue of 30/06, *The New York Times* offers a stupendous bit of research on the privileged handling of the mega-banks by the supposed defendants of a nation’s interest (“Documents on Bailout of AIG Show How Big Banks Benefitted” by Louise Story and Gretchen Morgenson): “At the end of the American International Group’s meeting last month, a shareholder approached the microphone with a question for Robert Benmosche, the insurer’s chief executive.

“‘I’d like to know, what does AIG plan to do with Goldman Sachs?’ he asked. ‘Are you going to get – recoup – some of our money that was given to them?’”

“Mr. Benmosche, steward of an insurer brought to its knees two years ago after making many risky, outsize financial bets and paying billions of dollars in claims to Goldman and other banks, said he would continue evaluating his legal options. But, in reality, AIG has precious few.

“When the government began rescuing it from collapse in the fall of 2008 with what has become a \$182 billion lifeline, AIG was required to forfeit its right to sue several banks – including Goldman, Société Générale, Deutsche Bank and Merrill Lynch – over any irregularities with most of the mortgage securities it insured in the pre-crisis years.

“But after the Securities and Exchange Commission’s civil fraud suit filed in April against Goldman for possibly misrepresenting a mortgage deal to investors, AIG executives and shareholders are asking whether AIG may have been misled by Goldman into insuring mortgage deals that the bank and others may have known were flawed.

“This month, an Australian hedge fund sued Goldman on similar grounds. Goldman is contesting the suit and denies any wrongdoing. A spokesman for AIG declined to comment about any plans to sue Goldman, or any other bank with which it worked. A Goldman spokesman said that his firm believed that ‘all aspects of our relationship with AIG were appropriate.’”

A Legal Waiver

“Unknown outside of a few Wall Street legal departments, the AIG waiver was released last month by the House Committee on Oversight and Government Reform amid 250,000 pages of largely undisclosed documents. The documents, reviewed by *The New York Times*, provide the most comprehensive public record of how the Federal Reserve Bank of New York and the Treasury Department orchestrated one of the biggest corporate bailouts in history.

“The documents also indicate that regulators ignored recommendations from their own advisers to force the banks to accept losses on their AIG deals and instead paid the banks in full for their contracts. That decision, say critics of the AIG bailout, has cost taxpayers billions of extra dollars in payments to the banks. It also contrasts with the hard line the White House took in 2008 when it forced Chrysler’s lenders to take losses when the government bailed out the auto giant.”

The Dubious AIG Bailout

“As a Congressional commission convenes hearings Wednesday exploring the AIG bailout and Goldman’s relationship

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with the insurer, analysts say that the documents suggest that regulators were overly punitive towards AIG and overly forgiving of banks during the bailout – signified, they say, by the fact that the legal waiver undermined AIG and its shareholders' ability to recover damages.

“Even if turns out that it would be a hard suit to win, just the gesture of requiring AIG to scrap its ability to sue is outrageous,” said David Skeel, a law professor at the University of Pennsylvania. “The defense may be that the banking system was in trouble, and we couldn't afford to destabilize it anymore, but that just strikes me as really going overboard.”

An Anarchy of Dimension

The Globe and Mail (19/06, “Cyber-Bullying – Toronto Police warn teens of ‘sext crimes’” by Ann Hui) writes: “One of the last times Samantha Beattie spoke to her 13-year-old sister Hope Witsell, Hope said she would not give in to her harassers. Not long after, Hope was found dead after hanging herself in her bedroom.

“They were calling her names like whore, slut, things like that,” said Ms. Beattie, 25.

“The harassment had begun months earlier, after a ‘sext’, or text message containing sexually explicit material showing an image of the young Florida teen's bare breasts began circulating around school. Hope had taken the photo herself and sent it to a boy she liked, but eventually it was found by the boy's girlfriend who distributed it around the school.

“Over a year later, police say, they're involved in a ‘rash of investigations’ related to similar ‘sexting’ harassment in Toronto. Sergeant Kim Scanlan with the Toronto Police said Friday that the spike could be due to the fact that kids are entering summer holiday and away from day-to-day supervision, compounded by the fact that mobile technology is more widely available than ever before....”

“Detective William McGarry said the typical narrative is this: ‘A boyfriend and a girlfriend share private images with each other. They think it's private, and everything is great. But then the relationship breaks up, and then one party starts sharing it with his friends. Then other people see it, and so on.’

“In many cases, the photos are then used to harass or even extort from the other party,

“This really suggest they had myopia and were looking at it entirely through the perspective of the banks,” Mr. Skeel said.

“Regulators at the New York Fed declined to comment on the legal waiver but disagreed with that viewpoint.

“This was not about the banks,” said Sarah J. Dahlgren, a senior vice president for the New York Fed who oversees AIG. “This was about stabilizing the system by preventing the disorderly collapse of AIG and the potentially devastating consequences of that event for the US and global economies.”

“This month, the Congressional Oversight Panel, a body charged with reviewing the state of financial markets and the

circulated at school, sent to the child's home or posted online.

“Once the image goes out of their hands,” he said, “they really have no control over it.”

“Current technology takes over. What a bed-partner to have! Earlier puberty, probably having to do with modern diet, also gets under the bed covers!

“The majority of those who have filed complaints are teenagers,” McGarry said.

“Noni Classen, director of education of at the Canadian Centre for Child Protection, said for some teenagers ‘sexting’ has become so normalized that they don't stop to think about consequences. Celebrities who have had their ‘sexts’ made public like High School Musical's Vanessa Hudgens, have only contributed to this. ‘They're thinking in the here and now,’ she said. ‘They think it's no big deal.’

“And while a child sending nude photos of him or herself to another consenting individual does not constitute a crime in Canada, the further distribution of that photo by anyone else does.

“Judy Arnall, a Calgary-based parenting instructor at the University of Calgary, recommends parents talk to their kids about ‘sexting’ and make sure they know the consequences of their actions. ‘You can't plant seeds in those minds, because those seeds are already there,’ she said. ‘What you're doing is telling them, “I'm okay for talking about this.”’”

Parenthood, too, has been made more multi-dimensional by our rampant technology.

W.K.

regulators that monitor them, published a 337-page report on the AIG bailout. It concluded that the Federal Reserve Bank of New York did not give enough consideration to alternatives before sinking more and more taxpayer money into AIG. 'It is hard to escape the conclusion that FRBNY was just going through the motions,' the report said.

"About the \$46 billion of the taxpayer money in the AIG bailout was used to pay to mortgage trading partners like Goldman and

Société Générale, a French bank, to make good on their claims. The banks are not expected to return any of that money, leading the Congressional Research Service to say in March that much of the taxpayer money ultimately bailed out the banks, not AIG.

"A Goldman spokesman said that he does agree with that report's assertion, noting that his firm considered itself to be insulated from possible losses on its AIG deals.

"Even with the financial reform legislation that Congress introduced last week,

David A. Moss, a Harvard Business School professor, said he was concerned that the government had not developed a blueprint for stabilizing markets when huge companies like AIG run aground and, for that reason, regulators' actions during the financial crisis need continued scrutiny. 'We have to vet these things now because otherwise, if we face a similar crisis again, federal officials are likely to follow precedents set this time around,' he said."

W.K.

Call to the People of the World to Support Iceland Against the Financial Blackmail of the British and Dutch Governments and the IMF

January 5, 2010, is a historical day for Icelanders. The Icelandic President Olafur Ragnar Grimsson had a tough decision to make, and difficult choices to make. To listen to the 23% of the nation that signed a petition calling on him to put the state guarantee for 5.4 billion dollars to be paid to the British and Dutch governments to a national referendum.

Or to ignore the nation and sign the bill for the government, after the bill had been passed through the parliament with a narrow vote on December 30, 2009 after months of acrimonious debate, tainted with secrecy and dishonesty on the part of the government. Every day throughout the debate, new information would emerge and documents would leak to local media or wikileaks.

Yesterday, the people of Iceland finally had a chance to have something to say about their fate, because if the state guarantee is accepted it will mean that Iceland will become like a third world country, spending its GDP largely on paying interest on foreign debt. Last summer, a bill for a state guarantee was passed that had a significant meaning not only for Iceland, but also for other nations around the world facing the same problems of private debt being forced on taxpayers.

The bill included a reasonable and fair way of handling the interest and the debt: Icelanders would pay, but only a certain percentage of their GDP, and if there were to be another financial black hole, they would not pay during that time. Thus it comes as no surprise that the Dutch and British governments reacted so swiftly with a condemnation of Iceland's citizens for having

the audacity to think they have the right to exercise their democratic rights in deciding for themselves what is in the best economic interests of their nation.

Let's also put this debt into perspective: 320,000 people live in Iceland, each and every person on the island, including children and the elderly, the disabled and the poor, would have to pay around \$30,000 under the bill. The danger if Icelanders will accept this enormous burden is that the entire welfare system would simply collapse with no money to run it. On January 5 the Icelandic president had the courage, backed up by his nation, to place the interest of the people before that of the banks.

Of course there has been an incredible spin by the government-controlled media, attacking the nation and the president for this simple and fair demand. The UK and Dutch media were also full of misleading news, saying the nation had demanded not to pay, and that we would become isolated and there were even suggestions that the British navy should flex its muscles against this nation which has no military. As if the terrorist act they imposed on us was not enough during the darkest hour of our crises to bring us further down!

The spin is failing because people around the world are finally starting to hear our side of the story, and other suppressed nations have perhaps seen this as a sign that they can also rise up against the corporocracy in our world where those with the money have as a rule always won. Let's hope the nation will not be coaxed into fear of isolation and let's hope the people of the world will join in this experiment of letting the interest of the peoples rise above the interests of banks,

corporations, and international bullies such as the IMF. We need your support. I will soon issue a comprehensive report on the entire Icesave saga.

Love and rage from Iceland Birgitta Jonsdottir Party group chairman for The Movement in the Icelandic Parliament Documentation. I append links to the files about Icesave that were leaked to wikileaks, and which show how the EU member states blackmailed Iceland into the same corner the government helped push into by accepting the Icesave bill. This file also contains letters between the main financial adviser to the Iceland Finance Minister and Mark Flanagan of the IMF: <http://file.wikileaks.org/leak/icesave-eu7.pdf>, www.rense.com/general89/dottr.htm.

Birgitta Jonsdottir
Birgitta Jonsdottir is the leader of The Movement, a group within the Icelandic Parliament which has emerged from the mass struggle of Icelanders against the financial blackmail brought to bear against their country by the governments in London and The Hague, with the backing of the IMF, in the wake of the insolvency of three large Icelandic banks in the midst of the Lehman Brothers-AIG world financial panic of September-October, 2008. Birgitta Jonsdottir is a courageous leader in the fight for national sovereignty, independence, dignity, and the economic well-being and future of her country.

RENEW TODAY!
(SEE PAGE 2)

A Varied Strategy to Use the Churches to Achieve Citizen Status for Huge Illegal Latino Population

The New York Times (23/12/09, "Latino Leaders Use Churches in Census Bid" by Julia Preston) reports embracing and varied efforts to utilize the coming population census to move the status of the huge Latino illegal immigration toward full citizenship: "Miami – Fearing that millions of illegal immigrants may not be counted in the 2010 census, Latino leaders are mobilizing a nationwide drive to urge participation in the survey, including an intense push this week in evangelical Christian churches.

"Latino groups contend that there was an undercount of nearly one million Latinos in the 2000 census, affecting the drawing Congressional districts and the distribution of federal money. The organization are far better organized for next year's census, but they say that if illegal immigrants – an estimated eight million of whom are Latino – are not included, the undercount could be much greater.

"One study suggests that Congressional delegations in eight states with large Latino population could grow if all Latinos – the nation's largest minority at some 47 million – are counted."

"The Latino position has some powerful arguments in support of their determination to trade census registration for nothing less than a program of legalizing the illegal Latino population in the US.

"Without the American plan to impose an economic straitjacket on the Americas, and indeed on the world – Globalization and Deregulation – there would not have been such a flood of illegal immigrants seeking work and a livelihood in the US. To get into the US many of them had to borrow money from relatives in Latin America to pay for being smuggled into the US. And now the illegal immigrants are left stranded without jobs and even the means of repaying the debt incurred with their families in Latin America. It is understandable why the huge Latino population of the US should feel strongly that now that opportunity beckons, it would be sinful not to make full use that the state authorities need to qualify for the full federal grants allotted according to population.

"The obstacles to an accurate count are significant. Many illegal immigrants are likely to be reluctant to fill out a govern-

ment form that asks for their names, birth dates and telephone numbers. And the count comes three years into an immigration crackdown initiated by President George W. Bush but continued less visibly under President Obama.

"Several of the nation's largest associations of Hispanic evangelical churches have agreed to join the census campaign. But it has caused dissension among others, with one evangelical pastor leading a call for a boycott of the census, saying it would put pressure on the Obama administration and on Congress to grant legal status to illegal immigrants."

A Variety of Latino Responses

"Some Roman Catholic leaders, moreover, have said they are reluctant to urge Latino parishioners to participate without greater assurances from the administration that illegal immigrants will not be identified or detained through the census.

"The Constitution calls for all residents to be counted, and last month the Senate rejected a measure by Senator David Vitter, Republican of Louisiana, that would have included only United States citizens in the official tally.

"In October, census officials said they would not ask the Department of Homeland Security to suspend immigration raids during the census period, reversing a policy from 2000, when an immigration moratorium was observed. But census officials say there is no change in a long-standing policy that they do not share identity data with the Department of Homeland Security or any other agency.

"Latino political leaders see full participation in the census as the culmination of heightened activism that began in the spring of 2006, when hundreds of thousands of Latinos marched in the streets to protest legislation then in Congress that would have toughened laws against illegal immigration.

"We want to tap into that same spirit," said Arturo Vargas, executive director of the National Association of Latino Elected and Appointed Officials Educational Fund, known as Naleo, a bipartisan group that is a main organizer of the census drive.

"We have to go back to everybody and say, 'Just as you marched, just as you voted, now you have to be counted.'"

"One strategy is to encourage Latino immigrants to return the census by mail, rather than waiting for a census taker's knock on the door, which could frighten illegal immigrants wary of immigration agents.

"To that end, groups like Naleo, the National Council of La Raza and others are moving to tap the expanding social networks and the power of persuasion of evangelical churches, which have seen huge growth among Latinos in the last decade. At a recent meeting with religious leaders in Miami, Naleo unveiled a poster for churches to use during the Christmas season. It depicts Mary and Joseph, recalling that they went to Bethlehem to participate in a census.

"Así nació Jesús," the poster says. "That's how Jesus was born." A new ally in Miami is Pastor Jose Victor Dugand, who can be found most days in his church in the southwest part of the city singing Christian rock music with a Latin lilt and expounding bilingually on the Bible.

"Even on hectic weeknights, worshippers come by the hundreds to pray at his Ekklesia Global Church, bringing worries about lost jobs in South Florida's battered economy as well as fears of immigration authorities. Lately, Mr. Dugand tells his followers how they can increase their political influence and draw federal money to the community by participating in the census.

"I think we need to come to the light – we need to be counted," he said. "Right now, I believe the government is totally off in the figures. We need to have a number closer to reality, so we can have better representation politically." But the Rev. Miguel Angel Rivera, a New Jersey pastor who heads a smaller coalition of evangelical clergy has called for a boycott of the census.

"We need to empower the undocumented immigrants by asking them not to participate," Mr. Rivera said, "as a way to protest the lack of commitment from this Congress to do what is right and moral, which is comprehensive immigration reform."

"He is touring the country with his boycott call.

"Nearly 12 million Latinos voted in November 2008, an increase of two million votes over 2004, according to an analysis by Andres Ramirez, as researcher of NDN, a Democratic advocacy research organization.

Now, in the first census since Hispanics passed blacks to become the second largest population group in the US. Hispanics want to extend their voting power with a census count that would support more elected representatives for their communities.

“An analysis by NDN and America’s Voice, an immigrant advocacy group, pro-

jected that a full count of Hispanics would lead to a significant redrawing of the Congressional map, with six states picking up the Congressional seat (Florida, Georgia, Nevada, Oregon, South Carolina, and Utah), while Arizona would add two and Texas as many as four.”

In short the redrawing of the voter map

that was begun in the Revolutionary War, continued in the Civil War, and continued to this day. It was Washington that launched Globalization. There is no way of making that somewhat more liveable than by providing a haven for the millions left jobless and homeless.

W.K.

China Outpriced

The New York Times (17/07, “As Labor Costs Rise in China Textile Jobs Shift Elsewhere” by Vikas Bajaj) reports: “Gazipur, Bangladesh – The eight-lane highway leading from the Bangladeshi capital, Dhaka, narrows repeatedly as it approaches this town about 30 miles north, eventually depositing cars into a muddy, potholed lane bordered by mangroves and small shops.

“But this is no mere rural backwater. It is the sort of place to which foreign manufacturers may increasingly turn, if the rising wage demands of factory workers in China prompt companies to seek new pools of cheap labor elsewhere.

“Already, in factories behind steel gates and tall concrete walls, tens of thousands of workers, most of them women, spend their days stitching T-shirts, pants and sweaters for Wal-Mart, H&M, Zara, and other Western retailers and brands.

“One of the Bangladeshi companies here, the DBL Group, employs 9,000 people making T-shirts and other knitwear. Business has been so good that the company is finishing a new 10-story building with open floors the size of soccer fields, planted with row after row of sewing machines.

“Our family needed the money, so we came here,” said Maasuda Akthar, a 21-year-old sewing machine operator for DBL.

“As costs have risen in China, long the world’s shop floor, it is slowly losing work to countries like Bangladesh, Vietnam and Cambodia – at least for cheaper, labor-intensive goods like casual clothes, toys and simple electronics that do not necessarily require literate worker and can tolerate unreliable transportation systems and electrical grids.

“Li & Fung, a Hong Kong company that handles sourcing and apparel manufacturing for companies like Wal-Mart and Liz Clairborne, reported that its production in Bangladesh jumped 20% last year, while China, its biggest supplier, slid 5%.

“Bangladesh is getting very competitive,” William Fung, Li & Fung’s group managing

director, told analysts in March.

“The flow of jobs to poorer countries like Bangladesh started even before recent labor unrest in China led to big pay raises for many factory workers there – and before changes in Beijing’s currency policy that could also raise the costs of Chinese exports. Now, though, economists expect the migration of China’s low-paying jobs to accelerate.

“And while workers in Bangladesh and other developing countries are demanding higher pay, too – leading to a clash between police and protesters earlier this week in a garment hub outside Dhaka – they still earn much less than Chinese factory workers.

“Bangladesh, for instance, has the lowest garment wages in the world, according to labor rights advocates. Ms. Akthar, who is relatively well paid by local standards, earns about \$64 a month. That compares to minimum wages in China’s coastal industrial provinces ranging from \$117 to \$147 a month.

“The Chinese firms that are beginning to get into trouble are producing textiles, rubber footwear and things like that,” said Barry Eichengreen, a professor of economics and political science at the University of California. “And there are a lot of countries in South Asia and East Asia and in Central America that would like to fill this space.”

“But Bangladesh has its own challenges to overcome.

“China’s combination of a vast population of migrant workers, many with at least elementary school education, along with modern roads, railways, and power grids in its industrial provinces, has bestowed it with manufacturing capabilities that countries like Bangladesh cannot offer. Beijing also provides low-cost loans and other incentives that other countries have trouble matching.

“Most of Bangladesh, meanwhile, suffers blackouts six to seven hours a day because it has not invested enough in power plants and natural gas fields – deficiencies that the

government is working on but that will not be eliminated quickly.

“The country has a literacy rate of only 55% – compared with more than 92% in China. As a result, workers in this country are only one-fourth as productive as the Chinese in making shirts, jackets and other woven clothes, according to a report by the Center for Policy Dialogue, an independent research organization based in Dhaka.

“Despite its handicaps, Bangladesh nearly doubled garment exports from 2004 to 2009. And the industry now employs about three million people, more than any other industrial segment in this largely agrarian country of 160 million. From June through November last year, garment exports accounted for more than 50% of the country’s total exports of \$7.1 billion.

“Among developing countries, Bangladesh is the third-biggest exporter of clothing after mainland China, which exported \$120 billion in 2008, and Turkey, a distant No. 2, according to the World Trade Organization.

“And with nearly 70 million people of working age, Bangladesh could probably absorb many more of China’s 20 million garment industry jobs.

“Still, some of the changes in China could prove to be mixed blessings for Bangladesh. If China allows its currency, the renminbi, to trade more freely, Bangladeshi exports would become more competitive.

“But a stronger renminbi could also hurt Bangladesh by raising the price of machinery and fabric imported from China, its biggest supplier, said assistant professor of economics at the Yale School of Management. Over time, Bangladesh could buy more from other countries, like India, but those countries first would need to building up significant production capacity.”

These countries are not only hobbled by an extreme lack of human capital, but of the possibility of acquiring it.

W.K.

Richest Country in the World Skimps on Medical Services

The Wall Street Journal (29/07, “Americans Cut Back on Visits to Doctor” by Avery Johnson, Jonathan D. Rockoff and Anna White Mathews) reports: “Insured Americans are using fewer medical services, raising questions about whether patients are consuming less health care as they pick up a greater share of the costs.

“Insurers, lab-testing companies, hospitals and doctor-billing concerns say that patient visits, drug prescriptions and procedures were down in the second quarter from year-ago levels. ‘People just aren’t using health-care like they have,’ said Wayne DeVeydt, WellPoint Inc.’s chief financial officer, in an interview Wednesday.

“Others say that consumers are beginning to forgo elective procedures like knee replacements. ‘We have a very weak economy and it’s just a different environment for the elective parts of health care,’ said Paul Ginsberg, a health economist who runs the Center for Studying Health System Change and has been analyzing health-company earnings. But ‘this could go beyond the recession. Being a less aggressive consumer of health care is here to stay.’

“Continued weak demand could eventually cut downward pressure on spiralling health-care costs, a long-sought goal of policy makers. It could also force insurers to lower premiums.

“The new trend comes amid a broader drop in health-care use as more Americans lose their jobs and their health insurance. Such cutbacks have happened before in recessions, but the drop seems to be more pronounced this time.

“More Americans are buying high-deductible health plans that force them to bear more of the upfront costs for health services. Some 18 million Americans bought high-deductible plans this year, compared with 13 million last year, according to Paul Mango, a director of consulting firm McKinsey & Co.

“At the beginning of the year, Dan and Natalie Johnson of Gig Harbor, Wash., used the website eHealthInsurance.com to buy a new plan with a high deductible of \$5,500 for their family. Their previous coverage had no deductible.

“Now the couple says they are thinking twice before scheduling doctor visits.

Recently, when their 16-year-old daughter’s allergy prescription ran out, Mr. Johnson called the allergist’s office to ask for a renewal, without coming in for an appointment, as she would have done under their previous insurance.

“And this spring, their son, 14, got his athletic physical at a local urgent-care clinic that charged just \$40, instead of a doctor’s office, which would have cost about \$90. ‘We don’t want to go through our savings going to the doctor,’ says Mrs. Johnson, a photographer.

“All this raises the question of whether, after a year of national attention on out-of-control health costs before the federal health overhaul passed in March, the trend portends a lasting change in the way Americans use the medical system.”

The Topsy-turvy Case of Health Insurance

“Just a year ago, insurers reported surging health-care usage. Back then, more consumers were signing up for Cobra, the federal program that allows people who have lost their jobs to keep their insurance. The government has extended a subsidy to cover 65% of the cost of coverage, which can be prohibitively expensive.

“However the Cobra subsidies only covered the unemployed for 15 months, and people have hit the limit and dropped coverage. What’s more, people who have lost their jobs since the end of May don’t qualify for the Cobra subsidies.

“To be sure, the change in behavior could be short-lived. On an earnings call last week in which it reported a decline in hospital admissions, a United Health Group Inc. said it thought utilization would rise again in the second part of the year as Americans exhaust their deductibles and insurers start paying for services. Both Aetna Inc. and WellPoint said the utilization fall-off was news as of this year, and they had not seen the trend previously even as the economy has deteriorated.

“What’s more, the federal health overhaul could cause usage to surge again. The new law will hand insurance cards to many Americans in 2014, which could unleash pent-up demand.

“Carl McDonald, an analyst at Citigroup

Investment Research said the last time he saw utilization fall off was in 2003, adding that usage also dipped in the early 1990s. But he added the drop is bigger this time.

“The declines in utilization has boosted profits for insurers, who set their prices to cover anticipated medical costs. Insurance industry prices and profits have been under fire by Democrats and regulators this year. Insurers have justified high premiums by pointing to out-of-control medical costs. But the recent profits could make it difficult for insurers to argue that continued price increases are necessary.

“On Wednesday, Aetna said usage of health-care fell in the second quarter, feeding a 42% increase in profits. WellPoint reported a 4% earnings bump, saying that hospital admissions and usage of prescription drugs had dropped compared with a year earlier.

“After the earnings releases Rep. Pete Stark (D., Calif.) called on the companies to reduce their premiums since they are paying out less in medical care. In an interview, Aetna’s chief financial officer Joseph Zubretsky said companies might eventually have to do just that. ‘If utilization stays down, it will have a favorable impact on rates,’ he said....

“Another sign that people are forgoing doctor visits or getting less care came from athena-health Inc., which provides billing services and electronic health records for more than 1,700 medical groups.

“Physician visits and hospital admissions are dropping this year, according to Thomson Reuters. Doctor visits have declined each month this year, including a 26% drop in May 2010 compared to May, 2009.... Likewise, hospital admissions dropped in three of the first four months of this year compared to those months last year, including being down 2.3% in April 2010 from April 2009.”

This would be a negative enough process, but it particularly outrageous in the light what celebrated as greatest lesson to have emerged from World War II that we have recounted elsewhere in this issue.

The Depression of the 1930s had also produced its great lessons. By the time President Roosevelt was inaugurated in 1933, 38% of the banks in the US had already closed their doors, and one of the first acts of the new president was to declare a bank moratorium during which all banks were closed. And during that period Roosevelt, whose knowledge of economics was not great, listened to just about anyone who had advise to give. From this open-minded

concern emerged the *Glass-Steagall* law of 1935, that forbade commercial banks to acquire interest in “non-banking financial pillars” – in those days these consisted of stock brokerages, insurance and mortgage companies. The reason? If the banks were allowed to lay hands on the reserves that these other pillars needed for their own businesses and used them as base for their own speculations, a skyscraper of speculation would ensue.

That brought on the present increasingly hopeless world crisis. The great speculative

banks learned their lesson of the 1930s to perfection. They have resisted control and enjoyed government backing. That explains the present disaster that the world economy has become. Not only has the great achievement of Theodore Schultz been expunged from official memory, but the equally important lessons of the 1930s have been forgotten by the leading parties once given to social and democratic reform. They have been not only remembered by our speculative banks but improved upon and combined with the suppression of Schultz’s

great discovery. The combination of cravenness on the part of the social reformists and the aggressiveness of the speculative banks and the choice of former bankers as key advisers by our governments, can seal the fate of society.

And, in Canada, all the while stubbornly erased from their very memories by once great reformist parties – Liberals and the NDP – is a nationalized central bank whose powers are still ignored in this stricken land.

W. Krehm

Human Creativity Denied is Producing Muddled Employment Paradox

The New York Times (25/05, “Machines, Not Apt at Chitchat Make Strides in Using Speech” by Steve Lohr and John Marroff) reports on some jumbles of contradiction in evaluating society’s investment in human capital as an asset or as liability. We quote: “Hi, thanks for coming,” the medical assistant says, greeting a mother with her 5-year-old son. ‘Are you here for your child or yourself?’

“‘The boy,’ the mother replies. ‘He has diarrhea.’

“‘Oh no, sorry to hear that,’ she says looking down at the boy.

“The assistant asks the mother about other symptoms, including fever (‘slight’) and abdominal pain (‘he hasn’t been complaining’).

“She turns again to the boy, ‘Has your tummy been hurting?’ ‘Yes,’ he replies.

“After a few more questions, the assistant declares herself ‘not that concerned at this point.’ She schedules an appointment with a doctor in a couple of days. The mother leads her son from the room, holding his hand. But he keeps looking back at the assistant, fascinated, as if reluctant to leave.

“Maybe that is because the assistant is the disembodied likeness of a woman’s face on a computer screen – a no-frills avatar. Her words of sympathy are jerky, flat and mechanical. But she has the right stuff – the ability to understand speech, recognize pediatric conditions and reason according to simple rules – to make an initial diagnosis of a childhood ailment and its seriousness. And to win the confidence of a little boy.

“‘Our young children and grandchildren will think it completely natural to talk to machines that look at them and understand them,’ said Eric Horvitz, a computer scien-

tist at Microsoft’s research laboratory who led the medical avatar project, one intended to show how people and computers may communicate before long.

“For decades, computer scientists have been pursuing artificial intelligence – the use of computers to simulate human thinking. But in recent years, rapid progress has been made in machines that can listen, speak, see, reason, and learn, in their way. The prospect, according to scientists and economists, is not only that artificial intelligence will transform the way humans and machines communicate and collaborate, but will also eliminate millions of jobs, create many others and change the nature of work and daily routines.”

How in the greater and deeper battle that threatens our society – whether investment in human capital is really an investment – the most rewarding a society can make – or is just another debt that must be discharged – so that our deregulated banks may resume their gambling with the very survival of our society as we have known it.

The *Times* article steers clear of this greater question raised by these *avatar* machines. Sooner or later, however, society will have to face it. But for that it will have to exhume our buried history, economic theory, scientific method, and so much else.

But back to the *Times* piece: “The artificial intelligence technology that has moved furthest into the mainstream is computer understanding of what humans are saying. People increasingly talk to their cell phones to find things, instead of typing. Both Google’s and Microsoft’s search now respond to voice commands. More drivers are asking their cars to do things like find directions or play music.

“The number of American doctors using speech software to record and transcribe accounts of patient visits and treatments has more than tripled in the past three years to 150,000. The progress is striking. A few years ago, supraspinatus (a rotator cuff muscle) got translated into ‘fish banana.’ Today, the software transcribes all sort of medical terminology letter perfect, doctors say. It has more trouble with other words and grammar, requiring wording changes in about one of every four sentences, doctors say.

“‘It’s unbelievably better than it was five years ago,’ said Dr. Michael A. Lee, a pediatrician in Norwood, Mass., who now routinely uses transcription software. ‘But it struggles with “she” and “he,” for some reason. When I say “she,” it writes “he.” The technology is sexist. It likes to write “he.”’

But the confusion between government investment being an investment – “the most rewarding a government can make” and a debt that must be paid off even by selling crucial social assets is far more important because the latter view affects the survival of both our “he’s” and “she’s.”

The penalty for neglecting that point could be society’s survival.

Warning about that – related to our concern – is alluded to in the *Times* piece: “Smart machines, some warn, could be used as tools to isolate corporations, government and the affluent from the rest of society. Instead of people listening to restive customers and citizens, they say, it will be machines.

“‘Robot voices could be the perfect wall to protect institutions that don’t want to deal with complaints,’ said Jaron Lanier, a computer scientist and author of *You Are Not a Gadget* (Knopf 2010).”

W.K.

Industries Squandering Society's Human Capital to Revive Their Profits

The New York Times (26/07, "Industries Find Surging Profits in Deeper Cuts" by Nelson D. Schwartz) reports: "By most measures, Harley Davison has been having a rough ride. Motorcycle sales are falling in 2010, as they have for each of the past three years. The company does not expect a turnaround any time soon.

"But despite that drought, Harley's profits are rising – soaring, in fact. Last week Harley reported a \$71 million profit in the second quarter, more than triple what it earned a year ago.

"This seeming contradiction – falling sales and rising profits – is one reason the mood on Wall Street is so much more buoyant than in households, where pessimism runs deep and joblessness shows few signs of easing.

"Many companies are focusing on cost-cutting to keep profits growing, but the benefits are mostly going to shareholders instead of the broader economy, as management conserves cash rather than bolstering hiring and production. Harley, for example, has announced plans to cut 1,400 to 1,600 more jobs by the end of next year. That is on top of 2,000 job cuts last year – more than a fifth of its work force.

"As companies this month report earnings for the second quarter, news of healthy profits has helped the stock market – the Standard & Poor's 500-stock index is up 7% for July – but the source of those gains raises deep questions about the sustainability of the growth, as well as the fate of more than 14 million unemployed workers hoping to rejoin the work force as the economy recovers.

"Because of high unemployment, management is using its leverage to get more hours out of workers," said Robert C. Pozen, a senior lecturer at Harvard Business School and the former president of Fidelity Investments. "What's worrisome is that American business has gotten used to being a lot leaner, and it could take a while before they start hiring again."

"In some ways the ability to rise in the face of declining sales is a triumph of productivity that makes the United States more globally competitive. The problem is that companies are not investing those earnings, instead letting cash pile up to levels not reached in nearly half a century.

"As long as corporations are reinvesting, the economy can grow," said Ethan Harris, chief economist at Bank of America Merrill Lynch. "But if they're taking those profits and saving them, rather than buying new equipment, it hurts overall growth."

Income Diverted to a Sector that Doesn't Spend

"There's no question that there is an income shift going on in the economy," Mr. Harris added.

"Companies are squeezing their labor costs to build profits.

"The trend is hardly limited to Harley. Giants like General Electric and JPMorgan Chase, as well as smaller companies like Hasbro, the toymaker, all improved their bottom lines despite slowing sales in the second quarter. Among the S&P, and companies that have reported second-quarter results, more than one in 10 had higher profits on lower sales, nearly twice the number in a typical quarter before the recession, according to Thomson Reuters.

"Whole industries are operating at new levels of profitability," said David J. Kostin, chief United States equity strategist at Goldman Sachs. "In the downturn, companies managed to maintain higher profit margins than ever before."

"Profit margins – the percentage of revenue left over after expenses – crumble in most recessions, as overall sales fall but fixed costs like infrastructure, commodities and rent remain the same. In 2002, during the recession that followed the bursting of the technology bubble in addition to the September 11 attacks, margins fell to 4.7%. Although the recent downturn was far more severe, profit margins bottomed out at 5.9% in 2009 and quickly rebounded. By next year, analysts expect margins to hit 8.9%, a record high.

"The difference this time is that companies wrung more savings out of their work forces, said Neal Soss, chief economist for Credit Suisse in New York. In fact, while wages and salaries have barely budged from recession lows, profits have staged a vigorous recovery, jumping 40% between late 2008 and the first quarter of 2010.

"Harley Davidson's profit gain last quarter was helped by a turnaround in its financ-

ing unit, as well as more efficient production, but the company is still cutting.

"Harley has warned union employees at its Milwaukee factory that it would move production elsewhere in the US if they did not agree to more flexible work rules and tens of millions in cost-saving measures.

"The last thing we're worried about is when are we going to have to add more capacity, because what we're really doing is reconfiguring our entire operation," Keith Wandell, the company's chief executive, said on a conference call with analysts last week.

"Harley's evolution is part of longer-term shift in American manufacturing, said Rod Lache, an analyst with Deutsche Bank.

"At Ford, revenue in its North American operations is down by \$20 billion since 2005, but instead of a loss like it had that year, the unit is expected to earn more than \$5 billion in 2010. In large part, that is because Ford has shrunk its North American work force by nearly 50% over the past five years.

"These companies have cracked the code of a successful industrial turnaround," Mr. Lache said. "They're shrinking the business to a size that's defensible, and growing off that base."

"To be sure, sales are rising for many companies, albeit at a much slower pace than the increase in profits. Among the 175 companies in the S&P 500 that have reported earnings for the second quarter, revenues rose 6.9% on average while profits jumped 42.3%, according to Thomson Reuters.

"Still, even at corporations where both the top and bottom lines are expanding, the focus remains on keeping profits high, not rebuilding work forces decimated by the recession.

"When Alcoa reported a turnaround this month in profits and a 22% percent jump in revenue, its chief financial officer, Charles D. McLane Jr., assured investors that it was not eager to recall the 37,000 workers let go since late 2008. "We have a tight focus on spending as market activity increases, operating more effectively and minimizing rehires where possible," he said. "We're not only holding headcount levels, but are also driving restructuring this quarter that will result in further reductions."

"Michael E. Belwood, a spokesman for

Alcoa, said more than 17,500 of the former workers were employed at units Alcoa has since sold, but added that the company 'had to be resized to match the realities of the recession.'

"We're keeping a close eye on costs because there is still uncertainty about the stability of this recovery,' he said."

Obviously, he is squandering vital human capital with this zeal. An unemployed industrial worker who has been jobless for a year or two is likely to get too rusty for re-employment in a period of ever more rapid technological change. To say nothing about the health and education of his children, the strain on his family. That is simply not in

the books of such industrial statesmanship. Come to think of it, our governments today have no serious accountancy, otherwise they would be aware the shattering waste of valuable human capital that is currently being perpetrated.

Rather than refinancing the speculative banks that have brought on this mess, the government should use its credit to build hospitals, schools, libraries. That will, first round, provide new employment and purchasing power. But once the schools and hospitals are completed they will go on providing employment of a permanent sort to teachers, janitors, maintenance workers, and retrain the unemployed workers, and

introduce serious accountancy that does not confuse society's most important investment with debt. And as for the universities – they should be reminded that the very name of their institution implies interdependence of all science and learning. Not only our history, but the ideas evolved during the Depression of the 1930s that kept banks out of stock market gambling, should be dusted off and introduced to their economic faculties. And the latter in turn must be guaranteed the freedom of speaking their full mind. Refusing to allow them to do so is further destructive handling of society's human capital.

William Krehm

Mistaking Human Capital for Debt Debases Our Statistics

The Toronto Star (17/07, "Expert 'certain' StatsCan didn't back census move" by Bruce Champion-Smith) illustrates how the suppression of the guiding notion of human capital strips our statistics of reliability, and leave our government experts groping in the dark: "Ottawa – Industry Minister Tony Clement's claim that Statistics Canada supports Ottawa's plan to replace the long-form census with a voluntary survey doesn't hold water, Canada's former top statistician says.

"Facing a barrage of criticism for his decision to axe the 61-question census form, Clement has begun telling reporters that the move was made with the consultation and support of StatsCan officials.

"But Ivan Fellegi, who served as chief statistician of Canada for 23 years before retiring, says he can't believe that his former colleagues would have endorsed a government move many experts say will produce suspect and unreliable data.

"I can't possibly imagine that they would have said this is not going to have a quality impact,' Fellegi said in an interview. 'I'm morally certain that they would have said the opposite. I'm absolutely 100%, totally convinced about that fact.

"On Friday, Clement shed more light on the government's quiet decision last month to scrap the so-called long-form census. The long form, sent to one in every five households, asked more detailed questions on topics such as income, employment, and the home.

"Clement is replacing it with the National Household Survey, which will go to 30% of households. The existing eight-question

mandatory short form will continue to be distributed as well.

"But despite mounting furor that the move will cost researchers valuable data, Clement insisted Friday it was Statistics Canada that suggested the change after what he called public opposition to the census.

"There are Canadians around this country who were concerned about answering... very intrusive questions about their personal lives,' he said. 'I said to StatsCanada, 'Give us some options. Is there a way that we can have a balance, get the data that everyone hankers for...but at the same time do so in a way where they can opt out if they have a conscientious objection?' he said.

"StatsCan gave me three options, each of which they thought would work. I chose one of those options with their recommendation.'

"He said he asked whether the voluntary survey would produce 'robust' data. StatsCan replied 'in no uncertain terms' that it would.

"But that claim doesn't hold water, Fellegi told the *Star* hours later. 'I am as sure about the fact that Statistics Canada wouldn't have done so as I can possibly be,' he said.

"Other experts have warned the move to a voluntary survey rather than a detailed mandatory census form will produce 'useless' data.

"Fellegi also took aim at Clement's claim that public complaints about the census have consistently gone up. 'It's the opposite course,' Fellegi said, noting that Canada's privacy commissioner has received just three complaints in the past 10 years about the

census. 'There's been a significant decrease in that number, not that it was ever high.'

"Statistics Canada issued a one-sentence statement Friday, saying it wouldn't give its side of the story.

"Clement said his government will not reverse its decision, even as opposition to the widely panned change continues to pile up.

"The Toronto District School Board says it depends on the data to forecast school enrolment and even its share of provincial funding. And it notes many other community agencies also rely on the data.

"The province of Manitoba has already written Clement to express 'its serious concern' that Ottawa is reversing four decades of census-taking in Canada. And it says the fact that the Conservatives did this without any apparent consultations is 'very disquieting.'"

However, it all harks back to the suppression of the most important lesson to come out of World War II, the proof that human capital is the most fruitful investment a government can make. Though paid for in advance, and giving rise to further investment absolutely essential in a world of growing population, rapid urbanization, about to source its minerals and fuels from a moon of the outlying planet Saturn, our gambling mega-banks have twisted what was learned in World War II – the "most important investment a government can make" into plain debt.

Unless this is corrected, it can only lead to the ultimate desperate gamble – the next war, which with the nuclear armament will be plunged into as the ultimate blind gamble.

W.K.

Correspondence

Request for information Regarding “Human Capital”

July 17, 2010

Hello, Mr. Krehm,

I was very pleased to hear you speak at the Canadian Action Party Town Hall meeting on July 14. I enjoyed hearing your thoughts and explanations about human capital as it relates to the importance of investing in the health, education, and general well-being of a nation's citizens, including protecting and refraining from polluting our environment. All of these issues and the serious neglect of them by the present government, and increasingly over the thirty and more years since the Bank of Canada ceased to be used appropriately by successive governments, are issues very close to my heart.

You also mentioned your disappointment regarding the G20 event. I was equally dismayed by the lack of any meaningful accomplishment, for the sake of Canadians.

I would be grateful for any literature you can send me that I may study and work into contributions for our website, our policy meetings, and development of a clear and integrated statement from the party on this issue. The indications fit very well with other policies we have been working on over the past year, and I believe we could bring them to a focus under this one topic.

Thank you very much for encouraging the party to take up this essential issue!

Sincerely,

Doris Foster

Human Capital

July 31, 2010

Hello,

I, Gordon Scott, heard from William Krehm during a CAP conference call when he expounded on the need for our society to recognize the value of human capital.

I was able to understand some of what was said but I feel that I should explore the subject further. We were told by Mr. Krehm that some material is available from you that would help me accomplish this goal.

How do I go about accessing this information? While I am able to use the internet, it is not my favourite means of communication.

Most sincerely,

D.O.G.S.

(D.O.G.S. stands for “De Ole Guy Scott.” This is a lead-in to my e-mail address which is deolgy@sympatico.ca, which is sig-

nificant because I am in my 90th year.)

Thank you for getting back so promptly.

I am primarily interested in developing/ exploring the concept of “human capital.” I think I have an inkling. For instance I, with no motivation apart from a wish to co-operate with one of my sons and his wife when they asked if they could use the area behind my house that hasn't been receiving any attention for at least ten years for a vegetable garden. I said they could and began investing what I think of as “human capital.” I cut cedar poles. I took down the remains of the old fence. I moved three trees that were not too large to move and cut down others that were too large. I used a weed trimmer to keep the turf that they weren't going to use this year. I won't go any further, but I think of the effort that I have made as an investment of human capital.

To accomplish what I have done has cost relatively little cash. In light of the fact that I am in my 90th year, the effort has cost me somewhat.

Cheers,

D.O.G.S.

Issues of Alignment

June 7, 2010

The Editor:

The COMER reports are a refreshing read for me. I was thrilled when a woman I know who works for your organization, introduced me to the *Journal of the Committee on Monetary and Economic Reform*. For many years I have been on the same page with many of your editorials. One can only hope Canadians will recognize what is happening on more than one front politically in our great country. So many times in the past I have made effort to discuss issues of “alignment” with our political leaders. Never successfully but I will not stop working at waking people up to the dangerous pass our political leaders have pointed this country in.

Growing up I was fortunate to have luck with parents, luck with school and luck in business. Knowing many people who went on to political powerhouse careers. Some premiers, some in other high levels of appointed government positions. Many of them have become more interested in their own self interests and voice no concern for the direction that Canadians are being manipulated into.

“Courage is going from failure to failure without losing enthusiasm.” – Winston Churchill

Thank you for your COMER report.

Cordially yours,

David G. Pointon

June 7, 2010

To David Pointon:

Thanks for your note. It's a sticking point for me as well.

Rgds.

Jim Travers

June 7, 2010

To Jim Travers:

More often than not I feel on the same page with your editorials. It is alarming to me that nobody in the Liberal Party of Canada are in alignment with some facts as follows. The Prime Minister of Canada travels around the world talking about the Canadian government not having to assist the chartered banks here. If one looks at 2008 and 2009 news the Bank of Canada spent in the area of 80 billion dollars to purchase mortgages on the books of the Canadian banks. This was to free up lending.

The Bank of Canada by charter can loan any amount of money it wishes to the Canadian government to finance our accumulated deficit and pay interest on the debt. This all changed with the politicians in the '70s when they got together with the bankers. Ponder this fact, billions in deficit spending and interest payments borrowed from banks could all come from the Bank of Canada. This would save Canadian taxpayers billions and billions of dollars currently being paid to the banks.

I would recommend that you visit the *Journal of the Committee of Monetary and Economic Reform* at www.comer.org. The publisher-editor of this publication is William Krehm. I have voted Liberal since 1972 and for the life of me I can't figure out what our why our party leader is so off the page. Speaking with Liberals I know they are frightened about the direction the current Prime Minister is taking Canada. However any information I have sent to the Liberal Party or its leader goes unanswered. Someone needs to understand what “alignment” is all about. They are out of touch and as a Liberal I see no change in the control Stephen Harper wields in a dictatorship style. He is a mockery to the Canadian parliamentary system. I would welcome your comments. Thank you.

Cordially yours,

David G. Pointon