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President Obama is Learning the Hard Way

The New York Times (09/06, "Stimulus Talk Yields to Calls to Cut Deficits" by David E. Sanger and Sewell Chan) reports: "Washington – At a moment when many economists warn that the American recovery is likely to be imperiled by prolonged unemployment and slow growth, President Obama is discovering that the tools available to him last year – a big economic stimulus and action by the Federal Reserve – are both now politically untenable.

"The mood in both parties of Congress has turned decidedly anti-deficit, meaning that job-creation programs favored by the White House and Democratic leaders in Congress have been cut back, then cut again. It is a measure of the mood that Mr. Omaha on Tuesday hailed an initiative by his administration to cut the budget of most major government agencies by 5%, at a time when conventional theory would call for more government spending to lift the economy.

"Even the Federal Reserve is pulling in its horns. No one could expect it to cut interest rates further – they are at rock bottom."

That is exactly what we warned President Obama of in our one-sided correspondence: that not all price increases are "inflationary." Prices in a high tech, highly urbanized world, in which the average citizen is living to a far riper age than his ancestors did, and has need certainly of a high-school, and more frequently of a university training, even a doctorate, prices can go up for reasons entirely different from an excess of demand over supply. That may be summed up under the heading of "investment in human capital," which would include health care and surroundings that would allow making full use of that costly equipment. That conclusion I first published in the outstanding French economic journal of that day, *La Revue économique* (May 1970).

In it I warned that unless the new non-market factors that have entered into price-determination were recognized, the world economy would come up against a brick wall.

That in fact is what happened, when *The Times* now writes that the Fed is at rock bottom in fighting "inflation." However, that is merely proof that the ongoing price increases are not the result of continued "inflation," but of an atrocious contortion of the government's accountancy that confuses government investment in physical and human capital with debt, rather than recognizing them as capital. I have given more details of the details of the consequences of this confusion elsewhere in this issue of *ER*.

If you wipe out all history pertinent to a problem, and reduce the ever more complex, entangled economies of our day to two simplistic factors – supply and demand – and when your elected representatives and the teaching staffs at most of our universities have been savagely restricted to the official

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With this issue of *ER*, we send a hearty welcome to those attending the G20 Summit in Toronto.

We also include a respectful reminder that attempting to solve the world's ever deeper economic problems by suppressing all that we learned about the economy and human society will end up in disasters that will make BP's misfortunes at the bottom of the Gulf of Mexico look like high petroleum statesmanship.

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Obama *from page 1*

policy by the threat of losing their positions, you have a society in a depth of moral trouble deeper even that the world's current economic despair. That explains the *Times'* remark that Mr. Obama is finding that the tools "available to him last year" are no longer available.

Certainly not if he persists in seeing in our price rise "inflation" rather than a reflection of the investment in physical and human capital investment at all levels of government.

On top of that Mr. Obama made the further blunder of retaining as economic advisers top bureaucratic brass that had helped lead the world into its current quandary. Had the suppression of our economic history not been a key component of this ultimate power-grab of irresponsibly speculative banking, he could have consulted many great economists and economic historians on this crucial matter.

But back to the *Times:* "'My best guess is that we'll have a continued recovery, but it won't be terrific,' Ben S. Bernanke, the Fed chairman, said at a dinner at the Woodrow Wilson International Center for Scholars on Monday night. 'And the reason it won't feel terrific is that it's not going to be fast enough to put back to work eight million people who lost their jobs within a few years.'

"One could almost envisage the winces in the White House as Mr. Bernanke observed that even if the economy grew at 3%, which would be considered a healthy pace,. it would do little more than keep pace with the normal rate of growth of the work force.

Virtually daily White House officials have struggled to explain how their strategies to provide economic stimulus to bring down the unemployment rate square with Mr. Obama's oft-expressed commitment to tackle a record budget deficit.

"They talk about spending this year in modest amounts – while waiting for the prescriptions of the president's commission on debt reduction, which reports, conveniently, a few weeks after the midterm elections.

"In the next breath, they say that the only long-term strategy that will get Americans back to work and bring the deficit under control is promoting rapid economic growth. That is the elixir that allowed the Clinton administration, where many members of Mr. Obama's team cut their teeth, to briefly wipe out budget deficits. But it is unclear where that growth will come from – and how soon.

"So rather than promoting another broad stimulus package, the White House is pointing to a series of familiar-sounding, low-cost measures to create jobs: stimulating export-oriented manufacturing, subsidizing energy-efficiency improvements by homeowners, preventing layoffs of teachers and police officers and pressing for a new (and unpaid for) highway bill that could, like the census, create a short-term burst in hiring.

"Lawrence H. Summers, the director of the National Economic Council and the adviser at Mr. Obama's elbow, argued that the effect of last year's $787 billion spending program had not fully kicked in. 'Given fiscal lag, the *Recovery Act* is still gaining force and having increasing impact,' he said, adding that the administration's job approach 'goes beyond spending programs' to include mortgage relief for homeowners and expanding lending to small businesses. 'We will not let up on jobs as a priority until unemployment returns to normal levels.'

"Congress has enacted or is likely to an estimated $200 billion worth of additional spending to last year's package, the appetite for a big new fiscal boost has slackened.

"The anti-deficit mood is not limited to Washington. Over the last two days, Britain and Germany have announced austerity plans, in contrast to what many in Europe were arguing for a year ago. Spain and France have announced similar moves. The politics of those moves vary from country to country. In Britain, it is explained by the election of a Conservative government; in Germany by the usual postwar German aversion to deficits.

"But the crisis in Greece has focused minds across Europe, especially in Spain, Portugal and Ireland. So two weeks ahead of a meeting of the Group of 20 economic powers in Toronto, there is a widespread consensus that grand stimulus programs are a thing of the past.

"The box that Europe, the Obama administration and Congress find themselves in today – desperate to stimulate the economy and fearful of the political reaction – gives new meaning to Milton Friedman's famous line of the mid-1960s. 'In one sense, we are all Keynesians now,' he wrote to *Time* magazine… [Keynes] called for government spending to counter downward cycles in the economy. In a less-remembered continuation of that sentence, Friedman added, in another [sense] nobody is any longer a Keynesian.'

However, to deal with the issue simply as how much debt politicians are prepared to take on is to trivialize it beyond qualification. If someone unloads his check for, say $500, on a bank where he has no account and is nabbed, he will get a prison sentence. Compared to that, the scale of the current falsification of what are our governments' capital assets, the crime of the $500 crook is salted peanuts. And yet it so intimidates the media and most of our universities about the nature of government investment – both in material and human capital – as to inflict mass unemployment, that can only lead to further war and social collapse.

Yet there is no way of determining what is government debt and what is investment. without serious accountancy. Had double-entry accountancy (also known as accrual accountancy) not been brought to Europe by the Knights Templar from the Holy Land, there would have been none of the lengthy voyages that led to the discovery of the Americas and the Eastern sea-route to China. Nor would there have been the unification of the tiny feudal principalities of Europe into united nations.

The distinction between debt and investment must be clear of ambiguity. However, the mega-banks have elbowed out their governments in determining the real category of government spending.

That was one of the great lessons learned the hard way during the Depression of the 1930s. It was embodied in President F.D. Roosevelt's *Glass-Steagall* law prohibiting commercial banks from acquiring interests in "other financial pillars" – specifically in those remote days, brokerages, insurance, and mortgage companies. Commercial banks had to finance other firms' transactions, not trade on their own account as investment banks. For that would give them access to the cash reserves required for the businesses they took over. And it empowered them to gamble on their own account with the capital reserves of other businesses.

On Fictitious Bank Capitalization

That is the origin of current confusion between what is government debt and assets that has floored the world economy today. And since government credit has long ago replaced the gold standard, government credit by the central banks – certainly in Canada where the central bank was nationalized in 1938 – relatively little use is made of that facility available directly or indirectly to all three levels of our government.

About economic theory, F.D. Roosevelt knew little. But he brought to the Depression of the 1930s an open mind, and a determination to get the country out of the ditch. By the time he was inaugurated in 1933, 38% of the nation's banks had shut their doors. Instead of bailing them out with government loans, he declared a bank moratorium that lasted a month during which he consulted with economists of every stripe. As a result when the banks opened their doors again they were restricted to commercial banking. And by 1935 the *Glass-Steagall* law passed Congress forbidding them to acquire interest in other "financial pillars" such as brokerages, insurance and mortgages companies. They were confined to financing trade. And in addition, a lively, highly necessary discussion was encouraged for local initiatives to issue script that could be used only to finance local trade and massive hydro-electric projects were undertaken by the government.

In Canada, the Bank of Canada, founded three years earlier as a privately-owned institution in imitation of the Bank of England, was bought out by the Canadian government in 1938, and thus was available to handle its capital investments at a token rate of interest. That permitted Canada to finance its Second World War on more favourable terms than either US or Britain.

That made it possible for Canada not only to repair the neglect of a decade of depression and five years of war, but to assimilate millions of mostly penniless immigrants and convert our essentially agrarian economy to a modern industrial one. Only in the 1970s under the conservative government of Brian Mulroney, particularly sensitive to Washington's preferences, was this discontinued. By the 1970s it had fallen into disuse and since then Ottawa has done the bulk its financing through private banks. Yet the original powers of the nationalized Bank of Canada are still on the law books, though not made much use of. Thereby hangs an instructive tale. Eager to toe the Washington line, PM Mulroney proposed a revision of our Bank of Canada legislation that would declare "zero inflation" and the autonomy of the Bank of Canada from the Government as the law of the land. But his own caucus in the House of Commons turned him down. Since then no government has dared tamper with the fundamentals of the *Bank of Canada Act* as it appears in print. But what actually happens in practice is another matter.

Accrual accountancy was smuggled into the US Federal bookkeeping to stave off a seemingly inevitable international financial crisis brought on by the North American Free Trade Agreement that led to the collapse of the Mexican economy, that lost little time in spreading internationally. In desperation US President Clinton brought in accrual accountancy, though to avoid the economic pieties that had taken over, he called it "savings." Savings, however, usually refer to very liquid or short-term securities that can help emergency calls, and what was involved here were highways, bridges and even raw land. That however, produced a surplus on government balance sheets helped bring on an economic upswing that got Clinton his second term and the world a boom until the collapse of the very late 1990s.

That, however, still leaves out of sight and mind *human* capital, the unique value of which was undoubtedly the most important lesson to come out of World War II. Immediately after the war ended, Washington dispatched to Japan and Germany hundreds upon hundreds of economists to study the war damage and predict how long it would be before these two countries could again become formidable traders. Some sixteen years later one of these, Theodore Schultz, published a book explaining why their conclusion had been so wide of the mark. This he attributed to their having concentrated on material destruction while giving scant importance to their skilled workers coming through the conflict almost intact.

From this Schultz concluded that investment in human capital was the most profitable a government could make. For this, he was for a few years celebrated, decorated, and then completely forgotten. For that is a message that speculative banking staging its style "recovery" cannot possibly tolerate. Even the record of the thirties and how society managed to curb speculative banking had to be buried.

COMER would be happy to enlarge on our program during the coming Toronto conference.

William Krehm
Chairman, Committee on Monetary and Economic Reform

Our literature is available to conference delegates without charge.

A Summary of COMER Principles

You cannot turn a proposition around and expect it to remain valid. Example: If I shoot myself in the head, I fall dead. But from that we cannot conclude that if I fall dead, I have suicided. It could have been due to heart failure. Imagine what science would be if its practitioners flipped logical propositions over, as pastry cooks do pancakes!

Today and for the last forty years or so, when prices go up it may be due to real inflation, *defined as a shortage of available supply.* However, when prices go up it cannot be concluded that real inflation is upon us. It could be something quite different: more public services and investments in material and human government capital investments being required, because of the urbanization of societies throughout the world, and the need for modern technologies.

Over forty years ago *La Revue économique* (May, 1970), the most prestigious publication on economics in France, with the great French economic historian Fernand Braudel on its editorial board, published a 70-page essay of mine that made the point that not all price index increases can be considered "inflation" – defined as a rise in the price level due to a lack of supply to fill the existing demand. Prices may be rising because of very different neglected factors – the increase of public investment, both in physical and human capital. This effect I called the "social lien," a terminology along with the idea was praised in the economic review of Cambridge University in Britain and over a half dozen other economic publications in Europe and America. Today *La Revue économique* no longer exists and the idea of the "social lien" is never mentioned.

No other distortion of economic theory has been more damaging than that suppression. A current example, in the 06/05 *New York Times* ("Private Sector Lags in Hiring" by Mitchell Powell), we read: "A shadow fell across America's economic recovery on Friday, as the Labor Department's monthly report showed that job growth was weak in the private sector provoking a precipitous sell-off in the stock market.

"The headline numbers for May suggested reason for optimism – employers added 431,000 jobs and the jobless rate fell to 9.7%, from 9.9 in April. But the underlying data showed that almost all of the growth came from the 411,000 workers hired by the federal government to help with the Census. Most of the jobs will end in a few months.

"By contrast, the private sector created 41,000 positions, far short of expectations for 150,000 to 180,000 jobs. And the number of long-term unemployed, those Americans out of work for 27 or more weeks, remained at its highest level since the Labor Department began collecting such data in the 1940s."

There you have an example as decisive as a blow to your eye of the distinction between real inflation (or reflation) and the social lien – the price effect – government investment of capital, physical or human.

Favouring the Bankers Instead of Society

Treat that as simple market "inflation" and raise interest rates, and you make the situation far worse for society but more profitable for speculative bankers. To that same end just everything we learned from our history has been expunged. It is no longer taught or even mentioned in the economic courses of most universities.

In the first week of the first year of high school, in our algebra classes, we were taught that to solve a linear equation of first-degree variables, you need two such different equations. To solve them you can then multiply one so that the first variable has the same coordinate in either equation. Then by subtracting one equation from the other, you eliminate the variable with the same coordinate. You then subtract one equation from the other and you have the value of the remaining second term left, and bingo! Your problem is solved.

For example: $x + 3y = 7$, $x + 2y = 5$. Subtract one equation from the other and you get $y = 2$ and $x = 1$.

If you have three distinct first-degree variables, to solve them you need three equations. If you have, say, 10,000 independent variables, you would need 10,000 times that many linear equations. However, the castrated economic theory of our day continues dealing with ever more complex problems with only two variables – supply and demand.

Further examination of what this implies may be helpful. In the natural sciences and amongst sociologists, when a previously accepted relationship is proven not necessarily wrong, but only a special case of a related but essentially different cause-effect link, that is once given a different name to distinguish it from the relationship already familiar. That is not what has been done amongst economists for at least a quarter of a century. There the thousands of other independent factors are simply ignored and the supply-demand relationship is used to justify blowing up interest rates to keep prices flat, to lick. the one overriding problem recognized in official economics today.

Thus unsuspecting purchasers of housing that consisted of a package of a house mortgage with the merest slice of an unsaleable collateral mortgage in the denominator. These packages were peddled without serious enquiry of the ability of the house buyer to support the obligation incurred. There was not even serious enquiry about his finances. Why would you bother verifying the liquidity of somebody on whom you were planning to unload an unsaleable package that you were anxious to get off your hands? That would be like checking the credit standing of somebody whose pocket you were picking. But that made the honest marketing of what should be seen as an unsaleable package of a sliver of an obligation that was often not even seriously documented.

Instead, our banks took out insurance and earned themselves a further mark-up in selling their more innocent clients insurance against loss for dubious concoctions of bad collateral and a straight loan. But it should be noted that what is risky can be insured, even though the premium may be quite alpine if the deal insured is *very* risky. But what is not *risky*, but *wrong* cannot be insured at all. An example: $2 + 2 = 5$ is not risky but wrong. Insure that and eventually both the insurer and the insured or both will go bust. Strange that COMER should have been the only organization to have identified this crucial point.

Unless of course the selling – off the insured poisoned package to an innocent bidder will get rid of it at a profit for the its creators. And then – more often than not – the government usually ends up bailing out the banks that were unwise enough to have loaded up with such questionable packages. For example, the formerly government-owned mortgage traders, Fanny May and Freddy Mac, as well as the mammoth insurance-trader AIG, which the US government bailed out from its mammoth involvement in the subprime mortgage mess.

This all harks back to the suppression of lessons learned at a staggering cost during the Great Depression of the 1930s and the Second World War.

Let me mention some of those buried crucial chapters of history. By the time Roosevelt was inaugurated, 38% of US banks had already shut their doors, and the first thing that Roosevelt did on being inaugurated was to declare a bank moratorium. Not particularly knowledgeable about economics, his great merit was listening to anyone who had an idea and he chased some that led nowhere. However, he led the country part way out of the Depression, allowing WW II to do much of the rest. In 1935 he brought in the *Glass-Steagall* law that forbade commercial banks from taking over "other financial pillars" to wit, in those early times, brokerages, insurance, and mortgage companies.

The reason? Once the banks invested in such other "financial pillars," they would lay hands on their cash reserves they need for their businesses, and use these as basis for the banks' own money creation. This, with an ever bolder pace of acquiring such investment banks resulted in an ever-accelerating skyscraper moving up ever more rapidly, with elevators having ever to rise more quickly, never, ever descend. For even the mention of pause or descent would collapse the frail structure. It would reveal that it had gone on capitalizing the investment made by investing the credit obtained from cash reserves acquired in this way and then gambling that investment to finance a further investment and so ever onward and upward until it had to be bailed out by the government if its bankruptcy would be big enough to bring down the entire economy. I used to keep track of the growth of the large American banks' leverage in using not only the cash reserves of the original non-banking "non-banking financial pillars" – brokerages, insurance, and mortgage companies, and around the end of the 20th millennium it had almost risen from 10 times the banks' own resources to just below 400:1. But the banks were ploughing every bit of cash into further ever more risky investments, gambling at ever wilder leverage. Eventually, I had to include the teller's cash to meet the needs of their retail clients and their ATMs. A year or so before the end of the 20th millennium, the ratio of investments to cash had risen from 10 to 1 to almost 400 to 1. But using the cash of the tellers and the ATMs to provide a denominator for this mammoth gamble, you endanger the banks' ability to conduct their legitimate commercial banking business. So I terminated the exercise, just in time for Globalization. For all its humanitarian lingo, globalization was part and parcel of this saga of ever accelerating predatory expansion by investment banks. Interest rates, alternately lowered to attract victims and then pushed into the skies to bleed them to serve its insatiable hunger.

In fact, the banks were running out of earthly space. Significantly this was when derivatives based on rates, and rates of growth to infinity, were being applied to insure financial gambles were being developed. It was a forbidden subject at conferences. But the real feature of exponential development has never been even mentioned except by COMER – it incorporates the dynamics of the atomic bomb. It is an infinite-membered expansion with the characteristic that the rate of the rate of growth of the rate of growth, always moving up – until everything goes up in smoke. Am I making this up? Have you noticed that the current project of the great powers is to put men on Mars. Undoubtedly, this has to do with sorting out the business of interplanetary heights both in the skies and on earth. The Good Lord Himself should keep a wary eye half-open when, as it seems at present, He is inclined to take a bit of a well-deserved rest.

And meanwhile here on earth, we are still trying to understand Humanity's survival problems multiplied million-fold by sending men – and eventually of course, armament – into outer space with two equations to guide our destinies, Supply and Demand.

William Krehm

RENEW TODAY!
(SEE PAGE 2)

Its Very Name Expunged from Official Memories, Economics Struggles to Survive

"Welcome aboard the QM22, where everybody knows your name. Passengers are apt to announce 'It's so nice to see everybody!' as they board and to be greeted by choruses of 'How are you,' near cheers, hugs and kisses. They call themselves the 'Bus People.' And even have a social chairwoman, Debbie Vassiliou, a vivacious 52-year-old with a throaty voice and an infectious laugh, who sometimes arrives wearing the gold earrings the group gave her for her 50th birthday.

"But this family will soon be sundered by budget cuts.

"The QM22 – which makes two round trips daily from Jackson Heights to Midtown Manhattan, with one running on Third Avenue and one on Avenue of the Americas – will make its final run on June 25. It is being eliminated as part of a $93 million budget slashing by the financially troubled Metropolitan Transportation Authority. The Authority says QM22 costs $143,000 a year.

"'These cuts are very difficult but necessary to close our budget gap,' said Deirdre Parker, a spokeswoman for the authority. 'We suggest that people use the subways.' But the Bus People are not eager to go underground. There are about 40 in the group, most of them women, middle-age or older, who work in offices.

"'If the QM22 goes, I'm going to have to quit my job,' said Ms. Apelian, who gave her age as 'way over 65.' And said she was coaxed out of retirement to work for a public relations firm. 'I have a bad back and sciatica. There's no way I can climb the stairs in the subway.'

"The Queens-to-Midtown run was started in 1988 by the Triboro Coach Corporation and was absorbed by the transportation authority in 2006. Long-time riders said that the friendly atmosphere started right away because the original buses had sets with low backs, making conversations easier, and that the limited number of buses meant passengers kept seeing the same faces.

"'We bonded because we all live near each other,' said Dorothy Leonard, who is in her 50s and has been commuting on the QM22 since 1992.

"When Ms. Leonard got a puppy five years ago, she got a card and chew toys from her bus friends.

"The Bus People used to play the lottery together – their biggest win was about a decade ago on general Lotto – and they give one another birthday parties and bridal showers. There is an annual Xmas party in an Astoria restaurant. In April, some members gathered at a bowling alley to see an Elvis impersonator, and once or twice a year they take a trip to Atlantic City – in a rented bus, naturally….

"Drivers are included in the festivities. Tommy Shortes, who has been driving city buses for 28 years, and QM22 was his favorite. 'I have enough seniority to pick this route every time, and I will pick it until the day I retire,' Mr. Shortes said.

"But the Bus People now find themselves getting ready to observe the biggest event in QM22's history – its demise. They are planning on dinner at an Astoria restaurant, but perhaps hoping against hope that there might somehow be a reprieve, they have not had the heart to set further details.

"On this morning, as the bus pulled up to its second-to-last stop, at 34th Street and Third Avenue, Ms. Amendola called after one of the women: Bye, honey, take care. Have a good day!'

"In less than a minute, the Bus People had all gone their separate ways."

If society's population is to flourish or even survive in crowded mega-urbanized world, they need reliable spots of living space where their sense of community may catch its breath to survive. That is no indulgence. Physical capital equipment is not crowded together, but appropriately packed – both for delivery and when installed for operation.

The happenings on Bus QM22 can he viewed as a reminder that this has not been happening with people. Between the absence of serious accountancy to evaluate the importance of human capital, and assuming that and reduction of the packaging and installations of this valuable capital, can only lead to more public funds being misspent on policing, and dealing with our crime problems. The latter could be diminished with proper accountancy and social retreats where people could catch their breath, before plunging once again into the ever-accelerating urbanization and financial pressures.

A Lesson from Long Ago

On the same page of *Times* already quoted there is a further item that should remind us when properly treated for what it is that the recognition of human capital will not only prove a boon to governments' financial soundness but to its moral probity.

We quote ("163 Years Later, a President Visits to Say 'Thank You'" by Jim Dwyer): "Jacques Judah Lyons had a strong tenor voice, one that people were glad to hear in song and speech. One March night, he used it to challenge a crowd in Manhattan. Strangers in a far-off place needed their help, he said, but he knew that members of his audience had principled objections. So many of their own people, they pointed out, other Jews right in New York, were also destitute and needed assistance.

"But were the objections real, he asked, or just 'excuses which the lips utter while they are rejected by the heart?'

"He was speaking in a synagogue on Crosby Street on March 8, 1847, where he was the *chazan*, or prayer leader.

"His subject was relief for people in Ireland who were starving during a famine caused by failures of crop and government. By the end of the evening, Mr. Lyons had collected funds from the congregation, Shearith Israel, according to an account in the April 1847 issue of *The Occident*, a monthly on Jewish subjects.

"On Sunday, more than 163 years later, the congregation, now at 70th Street and Central Park West, will be visited by the president of Ireland, Mary McAleese. She will give thanks for the generosity of Shearith and another New York congregation, Shaaray Tefila, during the famine years. About $1,000 for relief was collected by Jews in New York.

"'In some of the conventional histories, the story of the contributions of the Jewish communities here has been lost to sight over the years,' said Niall Burgess, the consul general of Ireland in New York….

"The Irish famine, which ran from about 1845 to 1852, was among the first humanitarian crises to be reported in the early days of global media. People and religious groups from around the world responded with donations, as described by Christine Kinealy, a professor at Drew University. In the current issue of *Irish America* magazine.

"The first major contributions came from Calcutta, where 40% pf the occupying British Army was Irish-born. The Choctow Indians, who were displaced from their homelands in the Southeastern United States earlier in the century, sent $174 to Ireland. Money was raised from prisoners in Sing Sing, former slaves in the Caribbean, convicts on a prison ship in London, slave churches in the South. Major sources of donations included the Society of Friends and the British Relief Association, led by Lionel de Rothschild.

"The famine began with a blight on the leaf of the potato, a staple of Irish tenant farmers, and accelerated through a system of absentee landlords and colonialism. The relief efforts became tangled in bureaucratic snares and rigid commitments by British authorities to free-market solutions. Some evangelists saw an opportunity to swap soup for the conversion of Catholics.

"But there was no such agenda for most of the donors, including Shearith Israel. The congregation was formed in 1654 by Spanish and Portuguese Jews who had been living in Brazil. When 23 refugees reached New Amsterdam, the Dutch West Indies Company ordered Peter Stuyvesant to accommodate them, 'provided that the poor among them shall not become a burden to the Company or to the community, but be supported by their own nation.'

"Mr. Lyons became Chazan in 1839. He helped found Jews Hospital, now known as Mount Sinai. His appeal in 1847 on behalf of the Irish bluntly stated that the Jews who gathered on Crosby Street had almost nothing in common with the people on the tiny island. 'There is but one connecting link between us and the sufferers,' he said. 'That link, my brethren, is humanity.'

"Mr. Burgess, the Irish government's senior official in New York, learned about the gifts of the Jews here from a friend who saw some information about them in the Irish Jewish Museum in Dublin. Christine C. Quinn, the City Council speaker, connected the Irish officials with the Shearith congregation.

"The congregation has continued its charitable works since 1847. The Irish are now among the leading donors of official development aid. Mr. Burgess said that was part of the famine legacy: a few years back, President Maleese said: 'We are a first world nation with a third world memory.'"

A good thought that requires that we remember the needs of the third world that are growing and ever more disregarded in our many-millionheaded urban civilization. Its governments, however, have wiped from their memories the most important lesson to come out of World War II – the importance of a country's human capital.

W.K.

Al Capone, Bathed and Manicured, Passed Off as the Holy Ghost

The Wall Street Journal (25/05, "The Credit Raters: How we Got Here" by Dennis K Berman) recounts: "Like an Apollo moon shot, the pending financial regulatory overhaul is a noble, necessary undertaking.

"Yet its success depends on so many intricate human systems panels – oversight committees and refashioned bureaucracies – that we should prepare for multiple malfunctions along the way. The new law will hurtle us somewhere, just probably not where Congress intends. That seems especially so far for a pending overhaul of the credit-ratings companies, which famously flubbed their duties during the mortgage boom last decade.

"The Senate bill passed last week contains reams of new rules to tighten oversight. Two recent amendments, however, really set the tone for change. One by Sen. Al Franken (D., Minn.) relies on 20 pages of legal engineering, injecting the government directly into the assignment and pricing of ratings. The other, at six pages, begins the process of extracting the government from ratings altogether. It is sponsored by George Lamas (R., Fla.) and Maria Cantwell (D., Wash.)

"As Congress potentially chooses between the two, it is worth remembering how credit ratings became such a mess in the first place. The original sin is itself a regulation, an obscure 1936 rule issued by the comptroller of the currency.

"At the time, bank regulators frightened by the Depression wanted banks to hold high-quality assets.

"Who could determine that quality? Regulators suggested banks should rely on 'recognized ratings manuals' of the era, which meant the opinions of Moody's, Fitch, Standard, and Poor's [the latter two would later merge].

"Overnight, banks – which are in the very business of assessing credit quality – were effectively told to outsource the job. Go forward 70 years, and banks bought complicated derivatives tied to the mortgage market because they were rated triple-A. Even though they were stuffed with subprime mortgages.

"It didn't stop there. Over the ensuing decades, state insurance commissioners, federal pension regulators and over-seers of broker-dealers also came to rely on ratings-firm opinions as the official litmus-test of asset quality. The agency roles were further embedded in 1975, when the Securities and Exchange Commission began to formally designate rating organizations….

"What began as a kind of official suggestion had in 40 years become an entrenched, government-sanctioned system for outsourcing credit work. By the 2000s, any issuer wanting to sell a mortgage bond to an insurance company had to pass through the ratings roadblock. And it had to pay for the privilege to boot.

"'Over time, we built up this incredible reliance on ratings,' says New York University business professor Lawrence J. White. 'There are a handful of these third-party raters, and we end up deifying them and believing they are the only source of bond information.'

"In its own way, the proposal by Sen. Franken keeps firms on a pedestal. Sen. Franken's plan is to eliminate the ability of issuers to 'shop' for the best ratings, by forming what he calls a Credit Rating Agency Board inside the SEC.

"Comprised of a majority of institutional and retail investors, the board will serve as a buffer between ratings firms and issuers of newfangled 'structured products.' It will pair bond issuers with ratings firms, employing methods that could include a 'lottery or rotating assignment system to reduce conflicts of interest,' according to the text of the bill.

"The new board will have the power to regulate the rating firm fees and evaluate the companies' accuracy. Senator Franken declined to comment for this column, but he has said in the past that the plan will aid competition by encouraging upstart firms to bid for the work 'to allow for fairness and economy.'"

But surely all this is salted peanuts alongside the great suppression of our history, the ignorant abuse of the most basic mathematical operations, a positive criminal innocence-through-suppression of what can be insured or "certified," and what is fraud. It would be like passing off Al Capone, given a bath and a manicure, as the Holy Ghost.

The New York Times (16/05, "A Credit Union That Played With Fire" by Gretchen Morgenson) leads us to the next shocker: "When Wall Street is accused – as it has been so often these days – of selling risky products to unwitting customers, it usually argues that investors in such exotic stuff are sophisticated adults capable of assessing any hidden dangers.

"So it goes with collateralized debt obligations, or CDOs, which are bonds, loans and other assets that the Street pools together and sells as packages of securities. Purveyors of CDOs maintain that buyers who lost billions in these mortgage-related instruments were, of course, sophisticated.

"But as a recent report from the inspector general of the National Credit Union Administration shows, it is neither credible nor factual that only savvy investors bought CDOs."

A Credit Union that Played with Fire

"The report analyzes the April 2008 collapse of the Eastern Financial Florida Credit Union. Based in Minamar, Fla., this state-chartered institution was created in 1937 to serve the Miami employees of what later became Eastern Airlines. The institution added other Florida employee groups and was serving 208,000 members when it filed last year.

"Eastern Financial had $1.6 billion in assets at the end of 2008. The company was placed in conservatorship on April 24, 2009. It was taken over by the Space Coast Credit Union of Melbourne, Fla. The failure will cost the National Credit Union Share Insurance Fund, the federal agency that guarantees credit union deposits, an estimated $40 million.

"Because it was based in Florida, the doomed credit union had its share of bad real estate loans on its books. But the inspector general's autopsy report said that the major cause of the Eastern Financial collapse was its decision to dive head-first into toxic CDOs just as the mortgage mania was faltering.

"Between March 2007 and June 22, 2007, the credit union committed nearly $100 million to buy 16 of these instruments; most contained dicey home equity loans.

"The timing of these purchases is intriguing. The spring of 2007 was when Wall Street's mortgage machinery was sputtering; New Century Financial, a big sub-prime lender, filed for bankruptcy that April. Brokerage firms that had provided funding to lenders like First Century and Countrywide began pulling in their credit lines. At the same time it became a matter of some urgency for these firms to jettison mortgage-related securities in their pipelines.

"Who sold Eastern Financial its toxic securities? Alas, the inspector general identifies neither the CDOs the credit union bought nor the firms that peddled them.

"But the report did note that the instruments Eastern Financial bought were private placements 'which provided less readily available market data to perform analysis and provide better understanding of underlying assets and grading systems, tranches, etc.' In other words, the most obscure CDOs imaginable."

Can a Bank Sell Bogus Investments to Credit Unions and Remain Innocent?

"'This situation illustrates yet again why over-the-counter securities and derivatives are not suitable for federally insured banks and other "soft" institutional clients,' said Christopher Whalen, editor of the *Institutional Risk Analyst.* 'Wall Street securities dealers who knowingly cause losses to federally insured depositors should go to jail.'

"Credit unions are nonprofit entities and typically do not engage in the risky investing that bank executives did during the credit bubble. Federal credit unions are also limited in the types of securities they can buy. While they can purchase mortgage-backed securities, they are barred from buying the CDOs.

"State-chartered credit unions have more leeway to invest in exotic instruments if their home states allow it. Florida, California and Michigan are three such states. But according to the National Credit Union Administration, less than 1 percent of all credit union representatives fall into the exotic category.

"Those state-chartered institutions that can buy CDOs and other riskier investments must set aside reserves of mark-to-market losses in such securities when they decline in value. This is intended to deter credit union executives from venturing down the risk spectrum.

"The Florida credit union met that requirement, but clearly the deterrence didn't work. Eastern Financial's failure may be an outlier, but it makes for a terrific case study."

"Indeed, the inspector general's analysis is depressingly familiar. Eastern Financial's management and board 'relied too heavily on rating agencies' grading of CDO investments,' it concluded, and failed to evaluate and understand their complexity.

"Almost immediately after the credit union bought the CDOs, they fell in value. By September 2007, the credit union had recorded $63.4 million in losses on the products, almost two-thirds of the original investment. By the time of its failure, the credit union had charged off on all 18 CDO investments, resulting in total losses of nearly $150 million.

"Richard Field, managing director of TYI, which develops transparency, trading and risk management information systems, says the Eastern Financial collapse is yet another example of why investors in complex mortgage securities need to be able to complete loan-level data of what is in these pools.

"'But the Eastern Financial insolvency also illustrates why regulators should make Wall Street adhere to concepts of suitability for institutions as well as individuals,' Mr. Whalen said.

"'The dealers who sold the CDOs to this credit union should be sanctioned,' he said. 'It might even be possible to pursue the dealer who sold the CDOs under current law. At a minimum the Securities and Exchange Commission should impose retail investor suitability standards onto banks and public sector agencies to end the predation by large Wall Street derivative dealers.'

"Will the National Credit Union Administration pursue any of the credit union's executives of the firms that sold it the toxic securities?

"'We always consider potential claims of third-party liability in cases of this magnitude,' said John J. McKechnie III, director of public and congressional affairs and congressional affairs at the administration.

"Indeed, the inspector-general's analysis is depressingly familiar. Eastern Financial's management 'relied too heavily on rating agencies' grading of CDO investments,' it concluded, 'and failed to evaluate and understand their complexity.'"

What Went Awry?

But surely having come out of a decade of soul-shattering depression in the 1930s both the US and Canada and much of the rest of the world were in a position to apply the lessons learned in the age of President F.D. Roosevelt.

Or even a bit earlier.

In the last issue of *ER*, we recounted the incredible achievement of a high-school drop-out in Vancouver, G.G. McGeer, who sized up the causes of the Great Depression of the 1930s – far sooner, in fact, than John Maynard Keynes managed to do so at Cambridge. He convinced the Liberal Prime Minister, Mackenzie King, to nationalize the Bank of Canada by buying out the 12,000 shareholders at a fair profit. In our last issue, we published as lead article his explanation to the trade-unions whom he represented why the Royal commission brought in from Britain 1933 was not even worth addressing.

That Commission had been made up not only bankers, but of labor leaders suborned by being raised to peers of the realm. And, accordingly, they limited their remedies to getting back onto the gold standard. That, however, was not only an irrelevant, but a wholly impossible goal, for it was the reliability of governments as borrowers rather than gold that supported the money they issued. No other is available or even conceivable.

Having become first mayor of Vancouver and then member of Parliament, McGeer leaned on the Prime Minister sufficiently to have him nationalize the Bank of Canada. That led to Canada financing her part in WW II at considerably lower relative costs than either the US where the Federal Reserve is still a very mixed bag between private and public ownership.

Accordingly, after the war, Canada was able to bring over millions of penniless immigrants, provide them with jobs, education for their children, and promising futures. This could be done by utilizing our nationalized central bank for financing government investment in physical capital and eventually in human capital investment.

However, many factors are involved, once a government undertakes to take over its money creation. During the Great Depression of the 1930s several of these made their contribution towards a better understanding of what got the world into the Depression, and how – several quite distinct approaches contributed to solve it by making possible a variety of life styles.

By the time Roosevelt was inaugurated 38% of the country's banks had already closed their doors, and more were on the verge of doing so. One of the first things Roosevelt did was to declare a bank moratorium, during which all banks closed their doors. And during that bank-less interval, Roosevelt consulted anyone – not excluding "gold bugs" who tried out setting and resetting the price of gold each day. On the other hand many mighty industrialists like Henry Ford had little use for banks. Special schemes provided scrip that could only be used locally. Huge hydro power developments by the federal government were high on the list. However, Washington could not go full way and nationalize the Fed. It remains a hybrid affair with the central Fed owned by the Federal government, but the shares of the branches are still in the hands of private bankers.

Reviving the Belief in a Flat World while Preparing to Send Manned Spaceships to Mars

White with the ash of stricken memories crippling their thinking, official economics has returned to the flat-earth beliefs of yore.

We shall provide a few samples of the problem. Economists who manage to retain their teaching posts in most American, Canadian and other universities throughout the world, believe and teach that a proposition remains valid when turned around.

That, however, is illiterate nonsense. If I pull the trigger of a loaded pistol held to my head, I fall dead. But I cannot flip this over like a pastry cook does a pancake, and assume it still valid. If I fall dead, I cannot conclude that I have killed myself, it might have been heart-failure.

The economic consequences of this gaff are shattering. If prices go up it might mean that there is real inflation, i.e., too much demand for available supply to satisfy. However, it could be something quite different: the cost of physical or human capital investment by the government. In its May, 1970, issue of *La Revue économique,* the leading French economic journal of that day, carried a 70-page paper of mine describing a class of rising prices not having to do with the market balance of supply and demand. The essay was reviewed twice most favorably in the economic publication of Cambridge University in Britain, and the reviewer in one case congratulated my choice of the term "social lien" to describe this previously unrecognized factor. It received favorable reviews in at least a half dozen other economic journals throughout the world.

In any serious science when an exception is found to what had been taken for a universally valid relationship, that is immediately reflected in a change of nomenclature to warn future researchers of the newly discovered limitations to the once-believed universal tie. For example, the huge leap in amount of physical infrastructure to support the increase in the world's population, modern technology and rapid urbanization have led to the explosion of the populations of Toronto or Athens almost tenfold or more.

In the first week of our algebra lessons in the first year of our high school courses, when I entered high school some 85 years ago, we learned that if a problem had two variables, then you need two different equations to solve it. One won't do. If there are three independent variables you need three, and if there are ten thousand in this high-tech age with its exploding population globulation and unnecessary problems created our deregulated speculative banks trying to solve them with just two variables, supply and demand. It can't be done, but it serves the interest of deregulated banks that have taken over the entire show.

But today with modern technologies, world population explosion, globalization, and so much else, the number of variables that we need to solve those equations runs in to hundreds and thousands if not millions. But economists, some out of honest ignorance, and others in order to hold their jobs with our deregulated gambling banks that control our governments. And most of our universities are still trying to solve them entirely with two simple variables, supply and demand.

The late great French economist François Perroux, formulated a theory to explain how our economy got into this pickle. He held that in every society the class in the saddle, advances its revenue as a fitting index of the welfare of society as a whole.

This had been the large feudal landowners in country and town, whose interest was in screwing up rents to the utmost behind tariff walls. The, when Watt's steam engines replaced human muscle-power in the factories, the "dominant revenue" became the industrialists who started preaching the evangel of free trade to keep wages low in Britain, and spreading the free trade evangel abroad, the better to profit from their initial monopoly of steam powered factories.

Under F.D. Roosevelt, banks had been strictly confined to financing trade. They were forbidden to acquire investments for their own account in any of the other "financial pillars" – in those distant days these consisted of stock brokerages, insurance and mortgages. The reason was simple. Once, the banks had access to the cash reserves that these other "financial pillars" required for their own businesses, they used them for further speculative acquisitions. That was the purpose of the *Glass-Steagall* law adopted in 1935. Ignored, and finally altogether repealed in the late 1980s, the banks took over every conceivable "other financial pillar." Applied storey by storey to the reserves of other "financial pillars," a financial skyscraper arose, ever more rapidly, with elevators, forever accelerating, going only up, never down. For both the constant rise and the acceleration had been incorporated into the speculative pricing of the exercise, and a pause in the upward acceleration, to say nothing of a descent, would crash the whole fictitious credit structure.

The dynamics of the exercise permitted neither slow-down nor return.

Almost a thousand years ago, a Crusading order, the Knights Templar, had brought back from Muslim lands accrual accountancy or double-entry bookkeeping that required every business transaction to be entered not once but twice. The first entry covered the investment in cash or credit that had been put into the investment, and that was "amortized" ("to extinction" in Latin), i.e., debited, as it was paid off according to preset schedule. On the other side, the current value of the investment was entered and "depreciated" (from the Latin "priced") to respect the Muslim insistence that interest may only be charged if the lender risked his capital just as the borrowing entrepreneur. Otherwise the penalty could be lasting hell-fire.

Brought to Europe, this made possible the exploratory trips to China and India that led to the discovery of the Americas. It also made possible the financing of the wars that resulted in the consolidation of Europe from tiny feudal principalities into modern nations.

But deregulation took over as speculative banking arose. Not long after World War II, "standard accounting methods" came to replace accrual accountancy and the references on official documents spoke of "standard accounting methods." In practice this turned out to be more often than not keeping the capital spent on a project on the government's books as a debt being amortized, while the worth of the resulting investment was written off in a single year. In Canada this reached a pinnacle under the government of Brian Mulroney who, under the influence of Washington, was inspired to put into the Constitution zero inflation and a balanced budget. His own caucus in the Commons turned him down on the point.

When after the financial crisis brought on by this sort of accountancy in Mexico under the North American Free Trade Agreement, President Clinton brought in accrual accountancy for physical government investment, but under the misleading name of "Savings." "Savings," however, implies cash or near-cash forms, and what was involved here was recording a physical investment of government until it had been properly depreciated.

There remains the even more important feat of swindling that has to do with society's investment in human capital. It was in fact the most important lesson that came out of World War II. At the end of hostilities Washington sent to Japan and Germany hundreds upon hundreds of economists to study the war destruction to predict how long it would take for these two mighty traders to regain such status again. Some sixteen years later one of these, Theodore Schultz wrote a book in which he explained how wide of the mark he and his colleagues had been. That was because they had concentrated on the physical destruction during the war, while overlooking the detail that the human capital – the skilled workers, engineers and scientists had come through the struggle virtually intact. From this Schultz concluded that human capital was the most productive a government can make. And that includes, of course, investment in health and the environment as well.

For that stroke of genius Schultz was feted, even decorated by a Bank of Sweden Nobel Prize. And then after a few years his memory and his great conclusion were so thoroughly suppressed, that no one other than COMER mentions the name, even in academic circles.

Once the unique government investment in human capital is again recognized instead of being misrepresented as just spending on our government books, there need no longer be any serious unemployment. Not only is investment prepaid in human capital, but its alleged "spending" is a further investment. The children of healthier, educated, parents, are more readily educated, and tend to be healthier and better adjusted. Britain is still drawing revenue from whatever Stratford-upon-Avon spent on teaching a certain Billy Shakespeare the glories of the English tongue and the folly of men.

W. Krehm

The Moral Responsibilities that Come with Globalization

The *Toronto Star* (07/06, "A Sorority of Healing in a village of victims" by Rosie Dimanno) recounts a shattering tale: "Goma, Dr Congo – The mutual nurturing in womenfolk has created a haven out of horror. Ward rooms are shared by the dozen. Food is cooked communally. Laundry of raggedy clothes hangs on the line. One woman's child is every woman's child, whether for scolding or cuddling.

"Theirs is the stigmatized sorority of rape. Behind these courtyard walls at Heal Africa, they've found a sanctuary and *femaled* a village of the otherwise damned.

"Erased as wives and daughters for a crime done *to* them, they've been cast out from their homes, expelled from their hamlets, reviled by husbands and fathers and brothers, ostracized by neighbors.

"Some are sent packing with their kids, who are even less to blame for their misfortunes of war. Others give birth to babies that are the seed of an enemy assailant, an armed fighter who pounced, took what he wanted, and left.

"In truth that's how wars have always been fought in the margins, on the backs of terrified women. But in the Congo these past 15 years, with the country engulfed in combat between multiple factions, rape as a weapon of war has exploded. It's an ethic decleansing, the soiling of female humanity.

"'I was on my way to the market to buy sorghum,' recalls Sifa Ushindi, who is 30 but has the haggard look of someone much older. 'There were three of them. They took me back to my own house and made my husband watch while they each raped me.'

"'That was a day of infamy in the village of Numbi, just outside the Hutu rebel stronghold of Massisi. The fighters came in waves, not only to loot and plunder but to defile. To Ushindi's knowledge, six other women were raped that day by fighters.

"'When they left, my husband wouldn't even look at me. I cried. I begged him. I said, 'What could I have done different? He said I brought the soldiers to go with them, he didn't want me any more because I was dirty.' With her parents both dead, Ushindi turned to her oldest brother for refuge. 'He said I was not welcome there either.'

"It was through the assistance of a local 'listening house' – a network of counselling shelters that functions also as an underground railroad for disenfranchised rape victims – that Ushindi made her way to the central Heal Africa establishment in the North Kivu capital.

"Heal Africa has 28 safe houses in the province and in the past seven years has trained about 470 village women as counsellors. Ushindi's husband kept their three children. Isaac was born here 18 months ago.

"When the child begins to fret, Ushindi picks him up, coos into his ear. 'When I look at him, I do not see the face of a rapist, the child of a rapist father. What happened is not my baby's fault.'

"She clutches him tightly.

"'He's all I have. After he was born, there was a problem with my womb. I can have no more children. And I will never have another husband.'

"When the subject of abortion is raised, if she'd ever considered ridding herself of the fetus, Ushindi gasps. Not only is the procedure illegal in the Congo – except when the mother's physical health is endangered – but she, like the majority of Congolese, is Catholic, not the pick-and-choose kind either.

"'That would be killing. There is already so much killing in my country. An abortion would make me just another killer, like the soldiers.'

"Many do, however, seek butcher abortions or turn to older village women who know the tribal ways of inducing miscarriage. Some give birth and abandon the infants or worse.

"What Ushindi can't envision is telling Isaac about how he was conceived. 'He will grow up believing his father died because so many of our men have been killed.'

"That, of course, will require leaving the sanctuary before Isaac comes to understand his surroundings. To that end Ushindi is being skills-trained, along with the other residents. They learn to sew, primarily or make simple crafts.

"The women aspire to nothing more than a bit of independence in a country that has no social safety net. Many of these women will hire out as day labour on farms or vend bananas and lemons and roast corn on the streets.

"None will be forced to leave until they're ready. Some likely will never do so.

"While there are psychologists and social workers on staff, these women draw their strength from one another. The main building has private rooms on three floors, mostly occupied by new arrivals in the assessment phase, their trauma raw."

Challenging that Humans are Civilized

"In the back are the ward room quarters, noisy with children, their mothers huddling on a concrete stoop to chatter. Most seem stone-faced and sluggish in their movements. But they do laugh, sometimes; they have shared their stories, but apparently moved past the need to revisit their individual ordeals. Collectively, their stories challenge the belief that humans are a civilized species.

"For some of the victims, raping was not brutal enough. One tells of having a gun but rammed into her vagina. Several were gang-raped. A few were kept as sex slaves in the militia camp.

"They arrived here often pregnant and even more frequently diseased. Many are suffering – and being treated for – fistula, a rip in the vaginal wall, commonly caused by violent penetration in which is torn from the area separating the rectum and vagina. As a result these women can't control their urine and sometime their bowels.

"In so many ways has sexual violence become the scourge of the Congo – women overwhelmingly the victims but, of late, men also have been coming forward to admit they've been raped by rebel fighters.

"What motivates these 'soldiers' to perpetrate such harm?

"There is a casual disregard for the humanity of the victim, There is rage at authorities, whether this government or – in the case of fleeing Hutus associated with the Tutsi genocide in neighboring Rwanda – against Tutsi usurpers of power, condemning them to endless soldiering in these volatile eastern provinces.

"There is also, culturally underlining the violations, a sense that all women are the property of men, that they're entitled to take their pound of soft flesh.

"With actual fighting sporadic amidst (largely transgressed) peace agreements, rape is now the dominant feature of the ongoing conflict in eastern Congo. There were an estimated 9,000 rapes last year, with no functioning legal system to arrest and try suspects.

"An exhaustive four-year report commission by Oxfam and carried out by Harvard University experts, released in April, found that 56% of sexual assaults were committed by armed men in homes in the presence of the victims' families.

"About 16% were reported in the field and 15% in forests. Incidents of sexual slavery were reported by 12% of the women surveyed, with some held for years as hostages.

"Rapes leaped proportionately during military operations, such as last year's offensive against rebel factions by the Congolese army, which was supported by UN troops, the study observed.

"More than half the women waited for at least a year before seeking help – too late to obtain effective treatment for the prevention of HIV treatment.

"Worrisomely, in a country that feels increasingly inured to the commonplace of violence, the report found that civilian rape has burgeoned as well, with 38% of rapes committed by non-combatants in 2008 compared with less than 1% in 2004.

"'These findings imply a normalization of rape among the civilian population, suggesting the erosion of all constructive and social mechanisms that ought to protect civilians from sexual violence,' the report concluded.

"The overwhelming scale of such brutalities almost diminishes the individual impact of rape. Each accounts for a life forever fouled. 'I had a life before,' says Ushindi. 'It was a hard life but there was also happiness in it. Those rapists, those animals, took it from me.'

"She brushes a fly from her son's face.

"'All I have is Isaac.' Her eyes suddenly burn with something that might be fury.

"'I love Isaac. I do."

It is shattering how the complete fabric of human society can be ripped beyond recognition. It should be handled with care against whatever assailants.

W.K.

And Where Is President Obama in This Highly Politicized Fair?

There are only two words for it: "amazingly detached."

From Washington, Konrad Yakabuski in *The Globe and Mail* echoes the astounded commentary of much of the American press: ("Spewing oil doesn't have Obama gushing") and adds the commentary: "'The President's even-keel response to the emergency has come off looking robotic – and could threaten his political future,' he adds.

"Whatever happened to the fierce urgency of now?

"Since becoming President, Barack Obama has been a study in self-control. No irritant can get a rise out of him. Not the underwear bomber. Not Goldman Sachs. Not even BP.

"Perhaps the President should reread the Martin Luther King speech from which he borrowed the second-best line of his campaign (the first being: Yes, We Can). Reminding Americans of 'the fierce urgency of now,' Dr. King added, 'This is no time to engage in the luxury of cooling off.'

"Americans have been horrified by the oil gushing into the Gulf of Mexico, a scene they have been able to watch night and day thanks to the 'spillcam' whose live footage BP was eventually forced – by Massachusetts Congressman Ed Markey, not Mr. Obama mind you – to make public….

"Since the April 20 explosion on the Deepwater Horizon oil rig, Mr. Obama has shown only the occasional flourish of emotion. But mostly, in the 40 days since this horror began, he has simply delivered businesslike updates of his administration's increasingly questionable handling of what has become the worst oil spill in the US history and possibly the country's biggest environmental disaster.

"On Friday, Mr. Obama travelled to the Gulf for the second times since the accident to witness the devastation as oil the consistency of chocolate pudding seeped onto the shores and into the precious Louisiana marshes. His neat khakis and cleanly pressed shirt didn't quite cut it. Couldn't his handlers have at least dressed him in hip waders or something?

"'If Bill Clinton was president, he'd have been in a wetsuit trying to get down to see the spill,' Pennsylvania Governor Ed Rendell cracked.

"The last thing anyone wants is another inauthentic politician who swears he feels your pain. To his credit, Mr. Obama comes off more sincere than most, better briefed than his briefers, and clearly in command of his administration. But presidents must also be good communicators and Mr. Obama, to the surprise of almost everyone who witnessed his 2008 campaign performance, has struggled with his messaging.

"Sometimes the even-keeled approach just looks robotic.

"'The President is somebody who has navigated the racial divide in America by being a mediator. He's a diplomat at heart,' Rice University presidential historian Douglas Brinkley offered in an interview. 'It's certainly a noble instinct. But not everything is a mediation. Look, when a building's on fire, scream 'fire'….

"Interior Secretary Ken Salazar's rote response that the administration has kept its 'boot on the neck' of BP belies reality. It was only on Thursday that the government was able to estimate the actual spill flow – anywhere from 12,000 to 19,000 barrels of oil a day – after BP insisted for weeks that it hovered around 5,000 barrels.

"On Thursday afternoon, Coast Guard Admiral Thad Allen, the man Mr. Obama put in charge of the spill response effort, appeared on US networks affirming that BP's 'top kill' attempt to cap the leak was proceeding as planned. Only later was it disclosed that the BP had in fact, suspended the operation the night before. (It has since been resumed.)

"The White House displayed characteristic tone-deafness in allowing Mr. Obama to headline a trio of high-priced fundraisers in California on Tuesday, including one at the home of billionaire oil heir Gordon Getty. It was only after it took flack for that trip that the White House hastily organized another to the Gulf.

"Republicans have not let this opportunity pass. The party's senatorial committee has produced a video juxtaposing candidate Obama's criticism of the Bush administration's handling of the aftermath to Hurricane Katrina – in which Mr. Obama decries Mr. Bush's 'half-hearted leadership' and vows 'never again' – against this administration's own foibles.

"But it is the disavowal of the President by his own 'friends' that has been most devastating. Former Clinton aide James Carville's irate outbursts have been running in a loop on cable news: 'It looks like he's not involved in this, Man, you've got to go down there and take control of this. We're about to die down here.'

"Louisiana Democratic Senator Mary Landrieu was almost as caustic. 'The President has not been as visible as he should have been on this, and he's going to pay a political price for it, unfortunately,' she told Politico.

"To paraphrase Dr. King, it could be fatal to overlook the urgency of this moment."■

As World Crisis Deepens, Curiosity is Growing About Our Government's Accountancy

The New York Times (6/06, "Banks Say No, Too Bad Taxpayers Can't" by Gretchen Morgenson) pulls no punches: "From the earliest days of the credit crisis, the nation's big financial institutions have been less than forthcoming about ballooning losses buried inside their books." These in fact are now coming to be seen as competing with the books of Hans Christian Andersen.

"To some degree," remarks Ms. Morgenson, probably the sharpest pen in the *Times* business section, this is understandable: denial is a powerful thing, after all, and writing off troubled loans during a period of stress is, for bankers, the equivalent of getting a root canal.

"As profits abounded at many of these institutions, however, artful dodging becomes more disturbing. And when disguising problems wind up harming the taxpayer – the same folks who rode to the rescue of banks with billions of dollars – the denial is downright exasperating.

"Among the more glaring bookkeeping fictions on big banks' balance sheets today are the values they assign to all of the bounteous second mortgage loans, doled out during the mortgage bonanza. As any realist will attest, many of these loans are worth little, and yet there they sit, at fantasy levels, on banks' ledgers.

"Refusing to face reality on second liens ultimately hurts shareholders. But taxpayers are the ones holding the bag when institutions try to avoid losses by refusing to buy back problem loans they have sold to Fannie Mae and Freddie Mac, the mortgage finance grants that are wards of the state.

"Fannie and Freddie helped grease the nation's housing machinery before and during the boom years, scooping up loans from all corners of the country. The more of these that Fannie and Freddie bought, the easier it was for banks to write new mortgages.

"To protect themselves from getting piles of garbage loans shoveled their way when they buy mortgages, Fannie and Freddie require lenders or loan servicers to sign contracts requiring those firms to repurchase loans that don't meet certain standards relating to borrower incomes, job status or assets. Loans that were extended fraudulently, or deemed to have been predatory, are also candidates for buybacks.

"Surprise, surprise, banks don't want to repurchase these loans. So when Fannie or Freddie identify problem mortgages and request repayment, a battle royal begins. Banks may argue, for example, that the repayment requests have flaws of their own.

"But for us as taxpayers, watching this battle from the sidelines, one growing concern is how aggressively Fannie and Freddie will pursue their requests. If banks refuse to buy back flawed loans, taxpayers will have to cover more of the losses.

"A lot of money is at stake here, and the figure is growing all the time. According to March 31 figures from Freddie, for instance, the amount of problem loans that it has asked other firms to buy back stood at $4.8 billion – up 26 percent from $3.8 billion just three months earlier.

"Freddie also said that as of the end of March, 34% of its buyback requests had been outstanding for 90 days or more. Three months earlier, was 30%. That increase indicates a greater reluctance among banks to respond to Freddie's demands.

"Fannie, for its part, doesn't disclose how much it's asking banks to buy back. Instead, it simply reports how much banks have agreed to buy back but have yet to pay during a specific period.

"During the first quarter of 2010, for example, Fannie said the unpaid principal balance of loans repurchased by its servicers came in at $1.8 billion, up from $1.1 billion during the first quarter of 2009. 'We expect the amount of our outstanding repurchase and reimbursement requests to remain high throughout 2010,' Fannie said in a filing."

Banks' Poor Lending Standards a Blow to Taxpayers

"It's surely good news that Fannie and Freddie are trying to hold these other firms responsible for shoddy lending standards. But if these firms resist paying up, that would be bad news indeed for tax-payers who would have to absorb Fannie and Freddie's losses on the loans.

"'Banks have been unwilling to mark all the bad loans they have and mortgage securities they hold to their true values because that would require a loss,' said Kurt Eggert, a professor at the Chapman University School of Law. 'But this is about banks trying to avoid losses and having taxpayers absorb them.'

"Freddie does not identify the lenders or loan servicers it is asking for buybacks. Some of the difficulties it encounters with loan buybacks are, it is said, the result of 'potential insolvency' – that is, financial woes at companies that made or service the loans.

"The top three lenders or loan servicers doing business with Freddie are JPMorgan Chase, Bank of America and Wells Fargo.

"In its own filings, JPMorgan said it bought back a total of 41.1 billion in loans in 2009. At the end of that year, the bank recorded $218 million in repurchased loans as non-performing assets on its balance sheet. In the first quarter of 2010, the bank repurchased loans with an unpaid principal balance.

"The bank does not break out how many of these repurchases involved Fannie or Freddie.

"Wells Fargo's financial filings show that it repurchased or otherwise settled loans worth $1.3 billion last year and bought back an additional $600 million in the first quarter of 2010. Its reserves for future repurchase requests stood at $1 billion at the end of last year.

"Mary Esher, a Wells Fargo spokeswoman, said the bank 'continues to have a productive relationship with the agencies as we work together to mutually resolve repurchase requests in a timely manner.

"'While the research involved in this process can be time-consuming,' she said, 'it is Wells Fargo's goal to completely repurchase requests as quickly as possible, and we have adjusted staffing levels appropriately to respond to current volumes.'

"Thomas A. Kelly, a spokesman for JPMorgan Chase, said the banks 'works consistently, loan by loan with Fannie and Freddy.'

"Bank of America did not reply to an e-mail message seeking comment.

"Michael Cosgrove, a Freddie spokesman, said the company is aggressive about enforcing its right to recover on questionable loans because it has a duty to be a good steward of taxpayer dollars. 'These reviews are more important than ever; there is no reason why taxpayers should pay for decisions that led to the sale of bad loans to Freddie Mac,' he said.

"But the banks have a keen interest in minimizing their exposure to loan buybacks, and you can be sure that they are asserting their rights to say no to these demands just as aggressively.

"'If the banks are not abiding by repurchase agreements, essentially they are saying the taxpayers should be on the hook, not them,' Mr. Eggert said. 'It's a bailout.'

"Throughout the credit crisis, the Obama Administration has bent over backward to accommodate the nation's large financial institutions, arguing that shoring up the banking system is in everyone's interest.

"To that end, the White House has given banks a lot of carrots in this crisis. But when it comes to buying back reckless loans, banks should now get the stick."

Not one, but several noted economists, historians, and philosophers have concurred in the view that if a different economic class comes in control of a country, it must change the group in charge of the political machine. Failing that, whether by military coup or by bloodless intrigue, the new regime will be hamstrung. President Obama inspired a good many of his fellow-Americans and people throughout the world when he came to power with his talent and as the member of a race of former slaves.

That legacy and the responsibility it entailed must have meant a great deal to him. It is tragic, that he should have picked for his leading economic adviser a man from one of the most power speculative banks on Wall St. This threatens not only the United States but the world. With the rapidly deepening world financial crisis this is no time to be running the US and much of the outside world stripped of the knowledge of how the US and much of the rest of the world got out of the Great Depression of the 1930s. As we make clear elsewhere in this issue, even the vocabulary that would permit us to identify how the world got into the current deepening mess has been wiped out. A situation that certainly did not exist in the 1930s.

W. Krehm

On the Perils of Memory Loss

The New York Times (02/02, "A Thief of Memory Stalks a Colombian Family" by Pam Belluck) reports: "Yarumal, Columbia – Tucked away on a steep street in this rough-hewn mountain town, an old woman found herself diapering her middle-age children.

"At frighteningly young ages, in their 40s four of Laura Cuartas's children began forgetting and falling apart, assaulted by what people here have long called La Bobera, the foolishness. It is a condition attributed in hushed rumors, to everything from touching a mysterious tree to the revenge of a wronged priest.

"It is Alzheimer's disease, and at 82, Mrs. Cuartas, gray raisin of a face grave, takes care of three of her children.

"One son, Dario, 55, babbles incoherently, shreds his socks and diapers, and squirms so vigorously he is sometimes tied to a chair with baggy blue shorts.

"A daughter, Maria Elsy, 61, a nurse who at 48 started forgetting patients' medications, and whose rages made her attack a sister who bathed her, is a human shell, fed by nose tube.

"Another son, Oderis, 50, denies that his memory is dying, that he remembers to buy only one thing at a time: milk, not milk and plantains. If he gets Alzheimer's, he says, he will poison himself.

"'To see your children like this,' Mrs. Cuartas said, 'It's horrible, horrible. I wouldn't wish it on a rabid dog. It is the most terrifying illness on the face of the earth.'

"For generations, the illness has tormented these thousands and thousands of others among a sprawling group of relatives: the world's largest family to experience Alzheimer's disease. Now, the Colombian clan is center stage in a potentially groundbreaking assault on Alzheimer's, a plan to see if giving treatment before dementia starts can lead to preventing Alzheimer's altogether.

"Most family members come from one Andes region, Antioquia. Geography and Basque ancestry, have isolated people here, who call themselves 'paisas,' countrymen. Over three centuries, many in this clan of 5,000 people have inherited a single genetic mutation guaranteeing that they will develop Alzheimer's.

"Large families, and intermarriages, have accelerated the spread. Mr. Cuartas's fourth debilitated child, in Medellin, Carlos Alberto Villegas, a former livestock trader and guitar serenader now often fed by baby bottle, married a distant cousin. His mother-in-law is an addled ghost: three of his wife's siblings, so far, are developing dementia.

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"With Alzheimer's in both parents' families, Mr. Villegas's three children, could face extraordinary risk. One, Natalia, 22, asks, 'How long have I got, till I'm 35? There's no way out.'

"Memories begin failing in one's 40s, occasionally as early as 32. By 47, on average, full-blown Alzheimer's develops.

"Their form of Alzheimer's, early-onset, was once considered too different to provide clues about far more common late-onset Alzheimer's, which has unknown causes and primarily attacks people over 65.

"But it turns out that both forms produce nearly identical brain changes and symptoms. Now, scientists will test as yet unproven treatments on Colombians genetically destined for Alzheimer's but not yet showing symptoms. They will give a to-be-determined drug or vaccine and see if it prevents memory loss or brain atrophy. If their disease can be halted, that could generate treatments to protect millions worldwide from common Alzheimer's."

Devising an Early Attack

"Alzheimer's has repeatedly resisted attempts to treat it. Current drugs, for people who are already impaired, show little benefit. Now scientists want to attack earlier. New findings show 'the brain is badly damaged by the time they have dementia,' said Dr. John C. Morris, an Alzheimer's researcher at Washington University in St. Louis. 'Perhaps the reason our therapies have been ineffective or mostly ineffective is that we're administering them too late.'

"With Alzheimer's afflicting 5.3 million Americans and 30 million people worldwide, numbers that some predict will double or triple by 2050. 'We can't wait to try to do prevention until we are absolutely sure what causes the disease,' said Neil Buckholtz, chief of dementias of aging at the National Institute on Aging. 'This public health emergency,' he said is 'just going to get out of control if we don't do something.'

"But preventive research is difficult. Participants should be people guaranteed, or highly likely, to develop dementia, and with common Alzheimer's identifying such people is challenging because the disease's cause is unknown. Also, because people would not be sick when treated, potential negative side effects are especially worrisome.

"Colombia provides the best chance. Mutation carriers always develop Alzheimer's and researchers know roughly when. They can give treatment about five years before expected memory loss, then see if brain changes or symptoms occur later or not at all.

"Since Colombians with Alzheimer's are young, without many old-age ailments, they have 'cleaner brains that can give a better picture of whether drugs work,' Dr. Buckholtz said.

"And the extended family's single location, large size and similar lifestyles provide enough comparable participants for solid scientific data.

"'This is the only place in the world where we can find a family like this, where it is possible to do prevention therapy more easily,' said Dr. Francisco Lopera, a Medellin neurologist who identified the family's illness 28 years ago and discovered its cause, an altered protein on the presenilin one gene on chromosome 14: the Paiasa mutation.

"Scientists consider Colombians not only valuable subjects but also deserving ones. 'We'd be giving people at the highest imminent risk of Alzheimer's access to treatment they wouldn't otherwise have,' said a project leader, Dr. Eric M. Reiman, director of Banner Alzheimer's Institution in Phoenix.

"Scientists are recruiting participants, hoping to start testing next year. Family members without symptoms, roughly 38 to 45 years old, will be gene-tested, given treatment or placebos, and monitored with memory tests, brain scans and other measures. A companion American trial will involve 60- to 80-year-olds of a different gene, which does not cause, but increases risk of common late-onset Alzheimer's.

"The treatment likely to be chosen by independent experts, could have failed with already demented patients or be something new. It will attack a protein, beta-amyloid, considered a culprit by many scientists because it creates plaques, deposits between the nerve cells.

"The treatment could be a drug that destroys or prevents plaques, or a vaccine that encourages or contains production of anti-amyloid antibodies.

"The project was not always an easy sell. For years 'I've been sort of shopping this around,' said Dr. S. Kosik, a University of California, Santa Barbara, neuro-scientist, who has long studied the family. 'People would get interested, then realize there are huge logistical hurdles. Medellin was a murder-capital of the world. Nobody wanted to even hear about going to Colombia.'

"Challenges included a relatively uneducated population with misconceptions about Alzheimer's, that it was transmitted through sex with already mad women, or blood of a sufferer's self-inflicted scratches. Relatives who handle care-giving here, sometimes take desperate measures, like locking the 'affecteds' in rooms to prevent wandering.

"Marriage options were often limited, and many did not realize that intermarriage would increase the chances of passing Alzheimer's to children. When Laura Cuarta's son Carlos Alberto Villegas married a cousin, Blanca Nelly Betancur, people knew La Bobera was on both sides, and some called the family 'the clan of the bobos.' But while Mr. Villegas told his bride-to-be that his 'father had become foolish,' she said back then that 'Carlos was healthy.'

Others talk of drastic reactions if they learn they are mutation-carriers.

"'I'd kill myself,' said Mr. Villegas's brother-in-law, Alberto Betancur, 40, a bus-driver with four-children. 'I'd throw myself under a train.'

"Such reactions, plus the lack of genetic counseling here, are why people gene-tested by Dr. Lopera, the Medellin neurologist, are not told if they will get Alzheimer's. Even he knows carriers only by computer code, not by name.

"American research participants sometimes learn their genetic status, and questions arose about testing drugs on Colombians who are unaware they are carriers. The answer was to give all participants something, so mutation-carriers are not revealed. Placebos will be given to non-carriers, treatment or placebos to carriers.

"'Two years ago,' said Dr. Pierre N. Tariot, a project leader who directs the Banner Alzheimer's Institute's memory disorders center, 'most scientists would have said that this is not feasible, considering it "science fiction."'

"Now, scientists are recruiting drug-industry sponsors for the $50 million trial, They currently have $8 million from donors. Some companies envision testing new treatments; others envision recovering investment in therapies that failed with already-demented people.

"'Prevent even one early-onset patient from getting the disease, that's a major victory,' said Dale Schenk, chief scientific officer for the Elan Corporation. 'It's not even debatable whether this should be done. It has to be done.'"

Memory is just that important to maintain the flourishing of humane development in human kind. Concern for the well-being of all divisions within and outside our own social group is the only means of assuring that we don't end up in the plight of the Alzheimer victims in Colombia. For there is a disturbing parallel. How then can we allow our governments without exceptions systematically to wipe out the critical records of our history, of how we got out of the Depression of the 1930s and achieved much in creating a better and more humane world? Our great universities – with few exceptions – have purged their staff and libraries of the achievements of economists, sociologists, and historians made possible to perpetuate the development of humanity to an ever higher level of humane achievement. We must campaign ceaselessly, untiringly, and equip ourselves for the task to allow us to retrieve the suppressed memories of all that most promising in world development learned by the humiliations of the Great Depression and the sacrifices of WWII. Otherwise we will not only share the fate of those deprived genetically of their memories, not around Medellin, Colombia, but in New York Paris, Rome and Berlin.

If humanity should perchance survive that, it could not be but as a degraded race haunted by the guilt of allowing themselves to be diddled out of their great inheritance of logic, of their history and background.

W. Krehm

Some Deep Philosophy from the Right

In its Review and Outlook section (09/06), *The Wall Street Journal* ("Feel the Rage") clues us into some of the deeper philosophy about the wisdom of a free market in a globalized, wildly mega-urbanizing world: "We don't expect miracles from Presidents. Even from those who pretend they can perform them, so we haven't been among those blaming Barack Obama for running a government that can't plug a well a mile under the sea. We've left that outrage to his one-time cheering section on the left, which has been begging Mr. Obama, imploring him, berating him, to locate and unleash his inner demagogue in reaction to the Gulf disaster.

"What a spectacle this has been, with the anchors, the various columnists and his *Newsweek* Boswells, furious and frustrated that the President hasn't demanded the heads of BP executives on pikes. All he's done so far is allow his Attorney General to loudly announce a *criminal* investigation of the spill – nothing demagogic about that – in mid-crisis and without any apparent criminal behavior on the public record.

"The liberals' fury at the President is almost as astounding as their outrage over the discovery that oil companies and their regulators might have grown too cozy. In economic literature, this behavior is known as 'regulatory capture,' and the current irony is that this a long-time *conservative* critique of the regulatory state.

"The Nobel economists George Stigler of the University of Chicago was one of the concept's main developers, and it is a seminal plank of the 'public choice' school of economics for which James Buchanan won the economic Nobel in 1986. Ronald Regan warned about this in different words in one of his farewell speeches.

"In the better economic textbooks, regulatory capture is described as a 'government failure,' as opposed to a market failure. It refers to the fact that individuals or companies with the highest interest or stake in a policy outcome will be able to focus their energies on politicians and bureaucracies to get the outcome they prefer.

"Perhaps if liberals read more conservative economists, they might understand that this is a common consequence of the regulatory solutions routinely offered in response to every accident or business failure.

"We should add that so far, based on the available evidence, we don't know if this spill really was a regulatory failure. But no matter, the same liberals who made oil drilling one of the most regulated activities on Earth are now busy deploring the energy bureaucracy and rearranging it so that (they promise) this will never happen again. Sound at all like the financial panic and the new regulatory remedy?

"How remarkable it is to see a President who has put such successive faith in the power of government being excoriated by his allies for a government failure. It's almost as astonishing as seeing Carol Browner, the White House green czar and long-time scourge of fossil fuels, being interrogated on NBC for excessive deference to Big Oil. Sometimes life really is fair.

"As for the President, he seems to be taking the liberal advice to rage against the ocean and BP. Yesterday, in addition to his 'kick-ass' vulgarity, he told NBC's

Today show that while hadn't talked to Tony Hayward during the crisis, he would have fired Mr. Hayward by now if the BP CEO worked for him. The President also hinted that BP should reduce its dividend. BP shares fell 5.7% yesterday.

"No doubt this will plug the leak."

We note that the *WSJ* mentions that James Buchanan won the Nobel Prize for economics in 1986 for his work on "the public choice" school of economics. It is, therefore, of relevance to check to see what the state of the world economy was at that time, whence it had come, and whither it was bound. And what the contribution of the ideas of the "public choice" school had been before and after that cited date.

Society has Buried the Lessons of the Depression of the 1930s

There was little public control of the economy in the 1920s. Wall St. got even shoe-shine boys investing in the stock markets and giving their customers market tips. The money Wall St. had raised had gone mostly into financing Latin American dictatorships, and when the financial boom collapsed it was not "regulatory capture" folk who jumped out of skyscraper windows, but brokers. Even Henry Ford, the legendary industrialist, held the banks responsible for the mess.

By the time F.D. Roosevelt was inaugurated 38% of the banks in the US had closed their doors. One of the first things he did, once inaugurated, was to declare a bank holiday which lasted a month. He consulted anybody with an idea of how to clean up the mess – no hint of "regulatory capture" there. With banking collapsed and firms bankrupt, Roosevelt could not be accused of taking the economy by previous design. He undertook giant hydro-electric projects to bring the collapsed economy going again.

Municipal credit schemes were encouraged to issue scrip valid only for trading locally – hardly a matter of competitive might between "public choice" and "regulatory capture." But the big innovation was the *Glass-Steagall* law that forbade banks from investing in "non-banking financial pillars" – significantly in that day consisting of stock brokerages, insurance and mortgage companies that played key roles in bringing on the speculative orgies of deregulated banks that brought on the current crisis.

The reason for *Glass-Steagall?* To prevent the banks from taking over these non-banking financial companies and using the cash reserves needed for their own business as basis for their speculative games with the deregulated banking multiplier. Allowed to, banks will use that cash to repeat the performance with the next acquisition, creating a skyscraper of credit with elevators rising only go up at ever-accelerating speed. Never down. For the moment the miracle stalled, the whole structure would turn to dust.

Man is not only the inventor of his technology, but in turn, though if may take a philosopher or a sociologist to grasp the deeper implications of this, his thinking also tends to be shaped by it even in his most intimate and social relationships. The technology of transcendental acceleration whereby each term of an infinite series is of a degree higher than the preceding one with a suitably adjusted coordinate is the mathematics of the atomic bomb. Obviously it has influenced our current financial structures. And since it is the speed rather than the durability that is the goal, the overriding result is, for those economically empowered, to cash in on the process before it blows up.

That is a far cry from the difference between "public choice" and "regulatory recapture." As is, the public's loss of any serious say in this crucial matter, since it has been deprived even in the economics departments of practically all our universities of the most elementary principles of logic, mathematics, the work of sociologists, of anything that would jeopardize the ride of the class in the saddle into infinity.

That is guaranteed in a couple of major ways. In any serious science, any alternative reaction to those already discovered is at once given a distinct name, to alert future researchers of the new research modifying the validity of what had previously been established. The contrary course has been followed in economics. In May 1970, the leading French journal on economic theory, *La Revue économique*, at the time carried a 70-page essay of mine establishing that when prices rise, this is not necessarily due to inflation, defined as higher prices due to insufficient supply throughout the economy to satisfy existing demand. It could be due to quite other causes-for example, there could be non-market factors at work – a greater investment in public infrastructures required by modern technology and urbanization, and also investment in human capital.

My paper was reviewed favorably in at least half a dozen journals on economic theory throughout the world, including twice by the economic journal of Cambridge University, one of the reviewers expressed admiration for the name given this non-market factor of price rise, the "social lien."

Fighting Bogus Inflation with Higher Interest Rates

However, today, "inflation" is used almost universally to describe any price rise. Obviously that justifies higher interest rates even in a depressed economy.

This despite what was undoubtedly the most important lesson to come out of the Second World War. Immediately after its end, Washington sent many hundreds of economists Japan and Germany to study the destruction and predict how long it would take for those two great trading nations to recover from their defeat and become formidable traders once again. Some sixteen years later one of these, Theodore Schultz, concluded that he and his colleagues had proved so wrong in their predictions because they had concentrated on the *physical* wartime destruction and attributed little importance to the fact that their superbly educated and talented human resources had come out of the war largely intact. From this Schultz, a professor – like George Stigler at the University of Chicago – concluded that human investment was the most productive that a government can make. For this, he was decorated with a Bank of Sweden Nobel price just as James Buchanan cited above.

For a few years he was celebrated, but then wiped out of economists' memories. Nevertheless, the Japanese lost little time in substantiating his conclusion. Tactfully, while seemingly assenting to the wishes of their US occupiers, they proceeded step by step they reshaped their economy from the exporter of textiles that had to import practically all the necessary materials, leaving minimal net profits in the country to an exporter of – step by step of heavy equipment and eventually motor cars.

Human capital, which is once again treated today as just "spending" that creates "inflation," has some very special traits. Not only is the spending for it actually prepaid, but itself has features of investment. The children of educated parents tend to be more readily educated, healthier and better adjusted to society than the average child of uneducated parents.

The other great lesson we owe to the late great economist François Perroux, amongst whose teeming insights, was that of the "dominant revenue." In every society, according to it, the class or sub-class in the saddle imposes its revenue as a reliable index of the welfare of society as a whole.

Closely connected with this is the realization that every significant redistribution of the national income must be accompanied by a change in all key personnel. For any key member under the previous rules for the distribution of the national income, will be likely to sabotage what must be a new order. In Mexico and many other Latin American countries, such drastic changes in the distribution of the national income were frequently accompanied with civil war, or the slaughter of the leaders of those who presided over the previous distribution of the national income. In Canada it is handled peacefully. But it is no less necessary. Obama undermined what reforms he may have intended making by choosing a high official of the previous regime as *cicerone.* Inevitably, that has led him back towards the old regime.

William Krehm

Can Governments Talk Seriously About Their Debt Without Serious Accountancy?

The New York Times (11/06, "Enthusiasm for Economy Sends Markets Surging" by Suzanna G. Kim) reports: "After weeks of violent swings, driven largely by concerns over the unfolding financial crisis in Europe, bargain hunters swooped in. The broad stock market leapt almost 3% in its biggest one-day gain in two weeks.

"For a day, at least, fears that the nation's fragile economic recovery might falter were cast aside. A stream of upbeat economic reports overseas prompted some investors to reverse their bearish bets with a rush of buy orders.

"But few investors or analysts seemed convinced that the market – down roughly 11% from its April highs – was finally out of the woods. Indeed, some suggested Thursday's gains might prove fleeting, given the nervousness pervading the markets.

"'Investors are spooked very easily by the smallest negative news stories now, and it won't take a lot for the Dow to be traded back to 10,000 as early as to-morrow,' said M. Jake Dollarhide, the chief executive of Longbow Asset Management.

"Even before the opening bell sounded, it looked like a good day for Wall Street. Thursday's rally began early, in Asian markets, and then spilled over into European trading. The US market gathered momentum into the close of New York trading, as some traders reversed short positions, or bets that stocks would decline in value.

"By the close, the Dow Jones industrial average was up 273.28 points, or 2.76% at 10,172.53. The broader Standard & Poor's 500-stock index rose 2.95%, or 31.15 points, to 1,086.84. While NASDAQ was up 2.77, or 59.86 points, to 2,218.71.

"The rally was broad and swift. Energy shares led the charge. BP, which has lost nearly half its value since the disastrous oil spill in the Gulf of Mexico, jumped 10%. Only a day before, BP had plunged nearly 16% after lawmakers called on the company to suspend its dividends and its advertising to pay for the costs of the cleanup.

"Driving the gains were several economic reports, mostly from overseas, that seemed to point to a sustainable global recovery. The European Central Bank slightly raised its forecast for economic growth in the euro zone this year, while the Japanese government reported that its economy grew 1.2% in the first quarter.

"A stronger-than-expected employment report in Australia and news that New Zealand was confident enough in its economic prospects to raise interest rates added to the sense of optimism, as did better-than-expected results on weekly jobless claims in the US.

"'China has been the economic juggernaut, and at least it's not falling apart,' said Michael Fitzpatrick, vice president for energy at MF Global.

"Others, however, insisted that the Chinese economy would ultimately slow down, posing a risk to growth worldwide.

"'Whether it's going to be a soft landing or hard landing – that to me is the fundamental risk,' said Stephen P. Wood, market strategist for Russell Investors. 'That's really the big, wild card.'

"Mr. Wood said a slowdown in China 'was inevitable.'

"Indeed, many on Wall Street say they believe the economic outlook remains murky at best.

"A report showing that weekly unemployment benefit rolls in the US fell by 255,000 to a seasonally adjusted 4.5 million, the lowest since December 2008, provided some relief to downbeat of late. But the report was not enough to persuade economists that unemployment would decline markedly soon."

The Tough, Ignored Reality Asserts Itself

"Scott J. Brown, chief economist of Raymond James, said jobs numbers from Thursday and last Friday indicated s 'long, hard slog ahead' ahead.

"The recovery should continue, but it may not be strong enough to push the unemployment rate down very much.'

"Mr. Wood said American economic data like Thursday's claims numbers were 'not bad, but not great.'

"'Jobless rate leads to consumer confidence, which leads to consumer spending,' Mr. Wood said. 'The key is consumption. The employment situation is the basis for consumer sentiment and behavior. And we're seeing stability and a modest improvement in that.'

"Mr. Wood acknowledged that risks from the oil spill and the European debt crisis could still affect US's growth. Which the Federal Reserve chairman Ben S. Bernanke, indicated would be 3.5% this year as long as the market held.

"Mr. Fitzpatrick said the news from China was more significant than the increase in jobless claims. 'But to say they're going to carry the entire world out of a recession is out of the question if their customers around the world are mired in a recession.' Mr. Fitzpatrick said.

"In Europe, the Euro stock market, a barometer of euro zone blue chips, settled 2% higher, while the FTSE 100 index 100 index added 0.92 percent in London."

There is something seriously missing in what can only be described as "tinkering" with random figures picked here and there in a complex world economy. And to commandeer the process to serve a group that has substituted political bias for analysis we must go back to what had proved itself the most valuable lesson to come out of the Second World War. At the end of the conflict Washington send hundreds of economists to Japan and Germany to study the wartime destruction and predict how long it would be until these nations could resume their role as formidable world traders.

Sixteen years later one of these, Theodore Schultz, wrote: "Economists were called upon to assess the effect of these wartime losses for recovery. Having had a small hand in this effort, I have had a special reason for looking back and wondering why the judgments we formed proved far from the mark. I am convinced, because we failed to take account of human capital and the important part that it plays in a modern economy.

"Not only is education capital, in every functional sense of the word, but it is the most dynamic of all categories of capital, endlessly unsettling and revolutionary in its effect. The typical capital accumulation of earlier generations – railways, factories, machines – served as a repository for society's inertia; its growth gave rise to spreading ranks of bondholders, rentiers, and passive stockholders. Over long period its increase seemed to blunt the economy's hunger for more capital – to hold back technical innovation, at times. That, indeed, was close to the heart of Marx's analysis. Capital placed in education has quite the opposite effect. It speeds the rhythms of change, shrinks write-off schedules, hastens obsolescence; it consigns to the scrap heap those solid tangible investments: factories and machines, which had been regarded as provident investments par excellence. In doing so, it has invalidated most of the traditional models of economics: Marxian, classical, as well as neoclassical."[1]

Need I, could I, add to this brilliant indictment of what the governments of the world at the present are hacking away at – education, health, scientific research, to clear the table for further feasts of deregulated, speculative capital?

That is the central and pivotal agenda that the G20 should be addressing. There is indication that they are oriented in quite the opposite direction.

The Austerity Summit

We quote on the point from *The Globe and Mail* of Toronto (08/06, "Europe's burden becomes the G20's problem" by Brian Milner, Janet McFarland, Toronto, And Kevin Carmichael, Montreal: "The highly anticipated gathering of G20 leaders in Toronto this months is fast becoming the Austerity Summit.

"As Europe's debt woes roil financial markets day after day – amid widening concerns that the crisis could send the still fragile global economy into a new tailspin – world leaders are shifting their focus to controlling ballooning deficits run up by governments to fight the recession.

"As a result such key issues as financial reform, climate change and poverty in the developing world could get shorter shrift when the leaders meet in Toronto on June 26-27. Further stimulus spending will not even be on the table.

"'It's the No. 1 issue of the G20,' Finance Minister Jim Flaherty said Monday. Mr. Flaherty was referring to the need for countries to find ways to deal with their spending and debt problems. 'What's going in Europe is not an academic exercise.'"

As though academia had not been *gleichgeschaltet* to the needs of our deregulated speculative banks.

"Governments across Europe are already adopting a new mantra of austerity and are pushing ahead with plans to either slash spending or raise taxes or both, in an effort to get their battered fiscal houses in order.

"There is a risk that pulling the plug on unprecedented measures launched in the wake of the global credit crunch in 2008 will send their economies reeling again. But that is outweighed by a stark loss of investor confidence – and the growing threat of costly credit downgrades – that has sent bonds and equities reeling and driven the euro to fresh lows against other major currencies.

"British Prime Minister David Cameron warned Britons Monday that they face heavy cuts in public spending and years of tough budgets, as the new coalition government wrestles with deteriorating public finances. 'The overall scale of the problem is even worse than we thought,' Mr. Cameron said in a speech north of London. 'How we deal with things will affect our economy, our society, indeed. And our whole way of life."

When you leave out proper accountancy and investment in public physical and human capital, it certainly will. To the point where the ultimate gamble – when all else has misfired – will be atomic war.

"German Chancellor Angela Merkel unveiled €82 billion worth of tax increases and reductions in spending and subsidies over the next four years and urged other leaders to follow her example.

"Ms. Merkel's cuts will effectively reduce growth in the German economy to zero, Carl Weinberg, chief economist with High Frequency Economics in Valhalla, NY, told clients on Monday.

"How much growth is Germany prepared to sacrifice over the next two years in the name of fiscal balance? Mr. Weinberg asked. 'Our calculations suggest a three-word answer – all of it.'

"The move came as euro-zone finance ministers put the final touches on a €440 billion fund designed to assist Spain, Portugal and other debt-ridden members of the common currency union.

"That financial safety net is a key weapon in the arsenal developed to defend the sagging euro, but so far international investors have been unimpressed. The euro has dropped below $1.20 (US) for the first time in four years.

"All economies, including Canada, must begin curbing stimulus spending and tackling their significant debts, Mr. Flaherty said in remarks to an International Corporate Governance Network conference in Toronto.

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That would apparently include our currency, since gold has long since been demonetized.

"The European finance ministers assessed the austerity plans announced by Spain and Portugal and glumly concluded that the proposed spending cuts will not be nearly enough.

"'More needs to be done and I can only encourage both countries to pursue structural reforms for instance in labor market and banking reforms,' said Olli Rehm, the European Union's economic and monetary affairs commissioner.

"The International Monetary Fund which will contribute an additional €250 billion to the euro-zone safety net, added its voice Monday to the growing chorus calling for major structural reforms and more centralized control of government finances, which the individual countries sharing the common currency have bitterly opposed.

"If vulnerable countries in Europe fail to resolve to reduce deficits, the resulting instability could hurt the economic recovery around the world. Mr. Flaherty said, 'I think it's clear there's a risk to growth arising out of the European situation.'"

Then why doesn't Canada use its central bank for what it was founded and is still the law of the land – to finance, practically interest-free, the human capital that is the most productive investment a government can make? We must renew our awareness of our history, the principles of elementary algebra taught in the first week of first-year classes, and remember that recognition of

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An Example that Our Official Economists Would Do Well to Follow

The Wall Street Journal (29/10, "Mining for Cold, Hard Facts" by Robert Lee Hotz) informs: "West Antarctica – At a camp here on the world's remotest continent, American researchers have constructed a towering drill that, like a biopsy needle, periodically plunges thousands of feet into ice to extract an exotic marrow of frozen gases and isotopes.

"Their work could settle a central question in the dispute over climate change, by documenting how greenhouse gases influenced temperatures in the past. Only then can researchers accurately analyze climate changes that may be under way today.

"Until now, that information was hidden in Antarctica's ancient ice.

"Scientists agree that temperatures are rising, and so are levels of carbon dioxide. But the immediate impact of human activity on natural climate cycles – from ice-sheet dynamics to wind and ocean currents – remains unclear. The Antarctica research could, for the first time, teach scientists how global warming developed when humankind had no hand in it.

"'One of the questions that everybody is interested in with greenhouse gases is, did the increase in greenhouse gas concentrations occur before or after the increase in temperatures in the past climate changes?' says glaciologist Kendrick Taylor, chief scientist of the $30 million US National Science Foundation project. 'Ice cores are the only way we can answer that question.'

"Ten times a day, scientists here recently winched up a 10-foot cylinder of compacted ice crystals containing the unsullied air and chemicals trapped by snowfall for the past 100,000 years."

No, that was no typo. The *WSJ* article reads "100,000 years."

"Each cylinder preserves bubbles of ancient layers of elements swept here by global winds. The ice records the annual rise and fall of greenhouse gases and temperatures every year before the last Ice Age, laminated by the cold in a thick parfait of time two miles thick.

"In March, a shipment of this rare ice completed an 8,000-mile journey to the National Ice Core Laboratory in Denver, where it was parceled out for analysis. Only Antarctica offers such a detailed calendar of climate change, the scientists say.

"Since November, revelations of errors in reports by the United Nations' Intergovernmental Panel of Climate Change have sapped public confidence in climate predictions. The scientists in Antarctica are excavating the ice to check on computer climate models at the heart of today's regulatory debates.

"Much of the present controversy over climate change centers on efforts to reconstruct past temperatures using what is known as 'proxy' data from tree rings, harvest records, sea beds and lake sediments. Unlike ice cores, which contain telltale gases and particles from ages ago, the proxy data offer only indirect or fragmentary evidence of climate trends.

"'Unfortunately many of our proxies have significant errors and are prone to be a slave to assumptions,' says climatologist John Christy of the University of Alabama in Huntsville, who has of often criticized the IPCC. His research, using temperature readings from NOAA and NASA satellites, has undermined arguments that the atmosphere is warming at an unusual rate.

"'The ice-core data from Antarctica is "terribly important,"' Dr. Christy says. 'We really need to know what the climate did before we can answer why it did what it did. If it happened before, it will happen again, and probably worse.'

"The camp here, 600 miles from the south Pole, is called WAIS Divide, named for its place atop a regional divide of the West Antarctic Ice Sheet. In January, 45 scientists, technicians and support staffers labored here at a cost of about $3 million for the season. They worked around the clock, inside an ice-house, probing a plateau of ice so thick that the continent sags beneath if weight.

"The first samples already reveal intriguing evidence of climate complexity. In ice layers attributed to the Middle Ages, when Europe was unusually warm, the team found surprising high levels of carbon black particles, or soot. Levels were found to be twice as high as during the more heavily populated and industrialized 20th century, says geochemist Russ Edwards at the Desert Research Institute in Reno, Nev.

"Overlooked in climate projections until recently, carbon black is a powerful warming agent. The spot, scientists speculate, came from giant wildfires that likely occurred in Australia and South America. So much soot could have raised temperatures.

"Preliminary tests also showed that soot levels dropped during the cooler centuries after the Middle Ages, a period known as the Little Ice Age.

"With more ice data, scientists hope to pin down the role of carbon dioxide in past global warming episodes. Rising levels of greenhouse gases like CO_2 in the atmosphere today are attributed to fossil-fuel emissions, land-use changes, cement production and agriculture. But no one is certain what made greenhouse gases fluctuate in the past.

"During Ice Age cycles of cooling and warming, temperatures often rose before levels of carbon dioxide changed – sometimes 800 years or so before – according to previous evidence of ice from Antarctica."

Effect Does Not Follow Cause

"'You don't expect the cause to follow the effect,' says atmospheric scientist Richard S. Lindzen at the Massachusetts Institute of Technology, a frequent IPCC critic. 'That's become an important issue.'

"Skeptics of carbon dioxide's role in global warming have made much of this discrepancy. They don't question the reliability of the data, but its interpretation, Dr. Lindzen says.

"Climate scientists offer explanations for the lag, from periodic variations in solar radiation due to the Earth's orbit and changing ocean currents, to problems with the dating of the data itself. But they lack enough information to prove them.

"The ice may hold the answer: 'This ice core is going to allow us to really look at the cause and effect relationship between CO_2 (carbon dioxide) and climate and temperature change,' says Julie Palais, head of the NSF's Antarctica glaciology program which is funding the project. 'That should give us the smoking gun.'

"To ensure accuracy, 27 independent laboratories will analyze the ice cores during the next three years. They expect to analyze 40 different trace chemicals related to climate, some in levels down to parts per quadrillion.

"At every stage the scientists must be able to prove that the ice cores haven't been contaminated. They must also make sure the samples stay at minus 20 degrees Celsius or so throughout their 8,000-mile journey to Colorado. Otherwise, the key gases will dissipate.

"'Its credibility is of crucial importance,' said Thomas Stocker at the University of Berne in Switzerland, a co-chairman of the United Nations working group that assesses data for the IPICC.

"Antarctica is a vast climate-science laboratory. For millennia, each new storm here captured the dust and chemicals brought by high-altitude winds from warmer latitudes and concentrated them at the bottom of the earth as the snow piled up and compressed into ice."

Antarctic Snow Pack a Chemical Periodic Table

"Gradually the snow pack became a periodic table of elements and temperatures 11,365 feet deep. 'Because it never melts, they are perfectly preserved,' says hydrologist Ray Banta from the Desert Research Institute, who is analyzing the ice.

"Dr. Taylor and his colleagues chose the remote drilling site in part because the snow and ice here accumulates about 10 times faster than [in] most places in Antarctica. That means the annual layers are thicker and easier to tell apart.

"Winter snowflakes are usually smaller and more densely packed, distinguished from the looser summer snow. By testing differences in acidity and electrical conductivity, researchers can also distinguish one year from the next.

"Ice cores excavated elsewhere before in Antarctica have tapped into even more ancient ice. But none of these ice cores offered such well-defined annual layers as those here at the WAIS Divide.

"Scientists here expect to harvest extremely detailed data for each of the past 40,000 years, plus another 60,000 years of data using both proven and experimental measuring techniques. Modern records of carbon dioxide levels go back a mere 50 years, and reliable temperature readings cover only the last 150 years or so.

"By measuring oxygen isotopes, the scientists can track the rise and fall of seasonal temperatures. Sulfates and ash reveal volcanic eruptions, which can help determine the age of the ice.

"Light isotopes of carbon in the ice can suggest the extent of vegetation elsewhere in the world. Calcium and a rare earth element called cerium hint at the extent of the world's deserts, while sodium is a measure of ocean storminess and sea spray. Soot and ammonium record wildfires. Methane is a clue to distant rainfall. Beryllium indicates changes in solar radiation.

"The snow also traps air. 'In between snowflakes, there are holes,' says Anais Orsi, a climate researcher from the Scripps Institution of Oceanography in La Jolla, Calif. 'As they get converted into ice, it seals in the air.'

"'Each ice core is about 10% of ancient air – a time capsule of the atmosphere unchanged from the year it formed. 'It is as if you opened a flask of air sampled 100,000 years ago,' says Dr. Stocker in Bern. 'It gives you direct, unbiased, unchanged access to its physical and chemical properties.'

"Spinning at 80 revolutions per minute, the $8 million drill chewed through ice with four hardened tool-steel cutters that bottoms out a mile below sea level.

"Every few hours, technicians from the University of Wisconsin put a narrow log of ice taken from the drill barrel into a frigid work room, where, bundled in red government issue parkas, researchers inspected it, measured it and cut it into 3-foot sections for easier handling.

"Their cheeks were blushed from frost; their eyes reddened by the glare of polar ultra-violet lights. Stiff wisps of hair whitened by frost framed their faces. As they handled the ice, they kept an extra pair of gloves warming in an oven, to don when their work gloves froze and fingers stiffened.

"They slept in unheated tents on a snowfield smooth as a starched shirt They were allocated one bucket of snow to melt for a shower once a week and three buckets of snow for laundry. In blizzard winds, crews slung guide ropes so that people could safely feel their way to the nearest outhouse.

"Working conditions are so harsh the researchers consider themselves lucky to run the drill 35 days a year. By the end of January they had drilled 1.5 miles into the ice. They packaged 4,500 feet of ice cores in individual three-foot tool, padded with snow. Then, they packed up the entire camp onto 68 wooden pallets for storage on the open ice cap until they can return next season. It may be another year or so before they can reach the bottom of the ice cap.

"The New York Air National Guard flew the year's shipment of ice to McMurdo Station, the main US supply base in Antarctica.

"There is was put into three refrigerated containers for shipment aboard a freighter across the tropics to Port Huenne, Calif., where it arrived March 8. Then the ice was driven across the desert to Denver.

"The refrigerated containers each have a back-up generator and a back-up compressor, which are triggered automatically if the temperature drops. A refrigeration technician accompanies the units. The temperature of the containers is also logged via satellite.

"'If it warms past minus 15 degrees C, it is worthless,' says Geoffery Hargreaves, curator of the National Ice Core Laboratory.

"There are four back-up systems to make sure everything stays safely frozen. In the worst case, technicians can flood the facility with liquid carbon dioxide.

"Sometimes this summer, technicians will start sawing the ice into small samples and shipping them to laboratories around the country, often via overnight mail. The samples will then be vaporized to free the air and elements within for analysis.

"At the peak of activity earlier this year, the crew guided the drill 100 feet deeper into the ice sheet every 24 hours, and another 365 years further into the past.

"'The drill is basically a time machine,' said planetary geologist Maria Banks from the Smithsonian's Center for Earth & Planetary Studies. As she spoke, she carefully wiped down a cylinder of ice that had fallen as snow 15,800 years ago."

With this staggering example of testing the deeper cause and effect in our physical environment, a tour de force that is aimed with a marksman's precision to ascertaining weather conditions long before there was even a human race, we must compare what has taken over our universities and government as acceptable economic doctrine, that still does its thinking on a mental-cycle with flat tires that passes for economic theory.

William Krehm

Accountancy *from page 18*

both physical and human capital, though deeply buried, is part of our history.

And without an intimate knowledge of our history and even what is still on our on law books, we will be cannon and bomb fodder in no time.

W. Krehm

1. Schultz, Theodore W. (1971). Investment in Human Capital. In Kiker, B.F. (Ed.), *Human Capital,* p. 51. Columbia: University of South Carolina Press.