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Why Models Essential for Society's Survival Get Buried

The Toronto Star (12/01, "Anti-Poverty success airbrushed out" by Carol Goar) recounts a scandalous tale: "Sitting tantalizingly in a warehouse in Winnipeg are 2,000 boxes of information about one of the most fascinating social policy experiments in Canadian history.

"Evelyn Forget, a professor of health sciences at the University of Manitoba, fought for five years to get access to those boxes, owned by Archives Canada. She finally succeeded in 2009, but the bulging files – statistics, completed questionnaires, interview transcripts, all on paper – overwhelmed her. 'Until it is computerized, analyzing the data in a systematic way would be incredibly expensive,' she says.

"Nevertheless, she has been able to piece together part of the story, using the census, public health insurance records and the recollections of researchers and participants.

"The experiment began in 1974. It was designed to test the concept of a guaranteed annual income in a small, fairly typical community, Dauphin, a rural municipality of 13,000 midway between Winnipeg and Regina, was chosen at the behest of former Manitoba premier Ed Schreyer.

"The city's low-income residents were lifted and kept out of poverty, using a negative income tax. (Canada Revenue Agency topped up their income if it fell below the property line.) They could use the money as they chose.

"The initiative was called 'income.' It was billed as an 'important contribution to the review of Canada's social security system.' It cost Ottawa $12.8 million and Manitoba $4.2 million.

"It ended prematurely. In 1978, Ottawa pulled the plug when the economy slumped, unemployment and inflation climbed and public interest in welfare reform plummeted.

"The findings were never analyzed. No report was ever written.

"But the concept of a guaranteed annual income (GAI) refused to die. The Royal Commission on the Economic Union and Development Prospects for Canada (the same blue-chip panel that called for a free-trade agreement between Canada and the United States) recommended a 'universal income security program' in 1988. Former prime minister Jean Chrétien toyed with the idea in 2001 as a part of his governments 'war on poverty.' Conservative Senator Hugh Segal is still convinced it is the right way to go.

"In today's climate of austerity, no government is likely to embrace a radical poverty reduction strategy. But computerizing the box loads of archived information in Winnipeg – not a huge expense for a government or public institution – would give scholars and policy-makers insight into what works and what doesn't in poverty reduction programs.

"Here is what Forget's research has already shown:

• "During the GAI experiment, Dauphin had a dramatically lower rate of hospital admissions than similar communities in Manitoba.

• "Its high-school dropout rate fell and stayed down for a generation.

• "It had fewer accidents, serious injuries, arrests and convictions.

• "Consultations for mental illness declined.

• "And, contrary to policy-makers' fears, people in Dauphin did not stop working or reduce their hours to get 'free' money from

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Models *from page 1*

the government.

• "'In all of the indicators I could find the quality of life, people did better,' Forget says.

"But she can't do a proper cost-benefit analysis. 'Someone needs to estimate the savings associated with reduced bureaucracy, better education and health outcomes and probably lower costs associated with crime and special education,' she told *The Uniter,* a student newspaper at the University of Winnipeg.

"She doesn't know if there were design flaws or delivery problems that reduced the program's effectiveness.

"She can't say how relevant data collected in Dauphin is three decades later in an urbanized, ethnically mixed, post-industrial Canada. What she does know compels to dig deeper.

"The information is there. If it is digitalized, Forget has the tools to analyze it fairly efficiently. If it remains on paper, she fears she'll die of old age finishing the job."

To really put this vital research, she would have to recover the vital chapters of our history never repealed, still on our law books. One is the purpose for which the Bank of Canada established as a private corporation in 1935. Some 12,000 shareholders were bought at a profit to them in 1938. That not only allowed the Government of Canada to finance its part of WWII more advantageously than the United Kingdom, that bought out the central bank in the UK only after the war, but more advantageously than Washington was where only the Federal Reserve in New York is publicly owned. That advantage of Canada which gets back essentially all of what it borrows from the Bank of Canada as dividends, was able to receive and settle millions of refugees after the war, without which we could never have transformed our country from an essentially agricultural land devastated by the Great Depression to the vigorous industrial land that settled millions of mostly penniless refugees from Europe.

That period of postwar prosperity and growth came to an abrupt end under the Brian Mulroney's years as prime minister.

In the United States, the Federal Reserve set the goal of "zero inflation." Accordingly the Bank of Canada imported from the International Monetary Fund John Crow, whose background had been in cracking the whip to keep near bankrupt governments in Latin America and Asia in line. Canada was anything but near-bankrupt but had transformed its economy due largely to its nationalized bank In no way was it beholden to the IMF. Yet the Mulroney government acted as though it were.

Though the government had been sole shareholder of the Bank of Canada since 1938, and Section 14 of the act sets out the power of the Minister of Finance to dismiss the Governor of the Bank of Canadian the event of a disagreement with the Governor Bank, the Mulroney government conducted an elaborate campaign to introduce "zero inflation" and the independence of the Bank of Canada from the Government into the Constitution.

The Largest Bank Heist Ever

However, under Mulroney, the government acted as though the Mulroney initiative had become the law of the land. University economic departments were purged through early retirement of any staff members who did not conform to the new evangel. Economic texts were elaborately rewritten to by-pass the real powers of the Bank of Canada.

It was under Mulroney, to curry favor with Washington, that bone-crushing interest rates were brought in "to lick inflation." Prior to 1991, the Bank of Canada had two major weapons for combating perceived inflation. It could raise the overnight bank rate that banks charged for making loans to one another to meet their overnight reserve shortfalls. Or, it could raise the statutory reserves – at the time – say, from some 6% to 10% of the deposits that the banks took in which would cool an overheated economy with reduced dependence on raising interest rates. This alternative was weakened and eventually repealed. That left interest rates the sole tool for keeping prices down.

Even earlier the Bank for International Settlements (BIS) a pure technical institution had come to serve as the bunker where central bankers plotted the undoing of the Roosevelt banking legislation of 1935 that restricted the banks to banking, and forbade them the acquisition of the other "financial pillars" – notably at a time when credit cards had not yet surfaced, the three such "other pillars" were stock brokers, Insurance companies, and mortgage brokerages – our readers will note that without the banks taking over of these three other pillars, the present foreclosed housing mess could not have taken place.

The assessment of the creditworthiness of banks was shifted from their cash reserves to

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On Scientific Method

In its broadest sense, the COMER perspective is inimical to the societies into which we have inadvertently evolved. The consequences of Perroux's dominant revenue concept, to which Bill Krehm frequently refers, have made us the ideal slave of the Financial System. We actually "believe" the absurdity that it is the availability of money as provided by the Financial System that determines what actions our societies can or cannot take.

Only the summation of the productive energies of all of society's members and how well these integrate to best serve the needs and wants of all those members will determine what is and is not possible. To claim otherwise is merely to acknowledge how laughably primitive is the way we go about seeking "solutions" to the problems that plague us.

Francis Bacon was born shortly after the death-bed publication of Copernicus' treatise on a sun-centered solar system, and died shortly before the birth of Newton. He was a contemporary of Galileo, of Harvey and of Gilbert. In his *Novum Organum*, published a few years before his death in 1627, he showed a remarkable appreciation of the significance of his age as the beginning of something very different – what we now call the scientific revolution.

"There are and can be only two ways of searching into and discovering truth. The one flies from the senses and particulars to the most general axioms, and from these principles, the truth of which it takes as settled, proceeds to judgment and to the discovery of middle axioms. And this way is now in fashion. The other derives axioms from the senses and particulars, rising by a gradual and unbroken ascent, so that it arrives at the most general axioms last of all. This is the true way, but as yet untried. Therefore from a closer and purer league between these two faculties, the experimental and the rational (such as has never yet been made), much may be hoped."

In this paragraph Bacon contrasts a "new" way of thinking *(such as has never yet been made)* from the "old" way of thinking *(this way is now in fashion)*. Bacon goes on to describe in meticulous detail the nature of this old way of thinking. What is amazing is how well this description fits our own times. Most of us most often think in Bacon's "old" way. Scientific thinking, which has so successfully solved the problems that has made possible the emergence of our modern world, as in the past, continues to be a rarity.

As a professional scientist myself, I have come to understand this dichotomy. Many recognize that science is about measurement and running experiments. Few appreciate that such skills, although essential to the scientific endeavor, are secondary. Scientific thinking cannot flourish in the absence of two fundamental attributes. First is a willingness to "disbelieve." Scientific knowledge advances only when someone disbelieves what it is fashionable to believe. It is too easy to believe true that which all your compatriots believe is true, and that which your schooling has taught you is true. Scientific thinking demands disbelief.

A second attribute is to have as a central focus the goal of disproving that which is believed to be true. The primary goal of scientific research is to show that an idea cannot be proved wrong. No idea can be proved to be true. It can only be proved to be untrue. Scientific knowledge advances not because we prove something is true, but because we are able to prove that something is untrue.

Unfortunately, however, we are all comfortable in many of our beliefs. We naturally accept all evidence that supports such beliefs and reject as flawed all contrary evidence. We lack that vital scientific attribute to give to adverse data primary attention.

Scientific thinking is a requirement for efficient problem solving. Its absence explains much about our society's dismal record.

The evidence of the past few years has spoken clearly to anyone who has the capacity to "disbelieve" and the capacity to give primary consideration to adverse data; that is, to think scientifically. The economy that we have inherited clearly does not work well. It has failed miserably to support the ability of our society to unleash the productive energies of all of its members and support the integration of these to best serve the needs and wants of all those members.

As a society, we have spent the past few years in an exceptional effort to restore the same economy that has been revealed as seriously flawed, albeit with a few patches designed to reassure that our cherished beliefs, much evidence to the contrary, need not be abused. Francis Bacon would be much amused.

Wavell Cowan

Humanity's Thinking and Fate, Reshaped for Split-second Communication across Planets for Stock Quotes or Bombs

We have dealt with the subject repeatedly, but never have we seen so detailed summary as the one in *The New York Times* (2/01, "The New Speed of Money" by Graham Bowley). We quote: "Secaucus, NJ – A substantial part of all stock trading takes place in the United States in a warehouse in a nondescript business park just off the New Jersey Turnpike.

"Few humans are present in this vast technological sanctum, known as New York Four. Instead, the building, nearly the size of three football fields, is filled with long avenues of computer servers illuminated by energy-efficient blue phosphorescent light.

"Countless metal cages contain racks of computers that perform all kinds of trades for Wall Street banks, hedge funds, brokerage firms, and other institutions. And within just one of these cages – a tight space measuring 40 feet by 45 feet and festooned with blue and white wires – is an array of servers that together form the mechanized heart of one of the top four stock exchanges in the United States.

"The exchange is called Direct Edge, hardly a household name. But as the lights pulse on its servers, you can almost see the holdings in your 401(k) zip by.

"'This,' says Steven Bonanno, the chief technology officer of the exchange, looking on proudly, 'is where everyone does their magic.'"

A Gabbling of Computers

"In many of the world's markets, nearly all stock trading is now conducted by computers talking to other computers at high speeds. As the machines have taken over, trading has been migrating from raucous, populated trading floors like those of the New York Stock Exchange to dozens of separate, electronic exchanges. They rely on data centers like this one, many in the suburbs of northern New Jersey.

"While this 'Tron' landscape is dominated by the titans of Wall Street, it affects nearly everyone who owns shares of stock or mutual funds, or who has a stake in a pension fund or works for a public company. For better or for worse, part of your wealth, your livelihood, is throbbing through those wires.

"The advantages of this new technological order are clear. Trading costs have plummeted, and anyone can buy stocks from anywhere in seconds with the simple click of a mouse or a tap on a smartphone's screen.

"But some experts wonder whether the technology is getting dangerously out of control. Even apart from the huge amounts of energy the megacomputers consume, and the dangers of putting so much of the economy's plumbing in one place, they wonder whether the new world is a fairer one – and whether traders with access to the fastest machines win at the expense of ordinary investors.

"It also seems to be a much more hair-trigger market. The so-called flash-crash in the market last May – when stock prices plunged hundreds of points before recovering – showed how unpredictable the new systems could be. Fear of this volatile, blindingly fast market may be why ordinary investors have been withdrawing money from domestic stock mutual funds – \$90 billion worth since May, according to figures from the Investment Company Institute.

"No one knows whether this is a better world, and that includes the regulators, who are struggling to keep up with the pace of renovation in the great technological arms race that the stock market has become.

"William O'Brien, a former lawyers for Goldman Sachs, crosses the Hudson River each day from New York to reach his Jersey City destination – a shiny blue building opposite a Courtyard by Marriott.

"Mr. O'Brien, 40, works there as chief executive of Direct Edge, the young electronic stock exchange that is part of New Jersey's burgeoning financial eco-system. Seven miles away, in Seaucus, is the New York Four warehouse that houses Direct Edge's servers. Another cluster of data centers, serving various companies, is five miles north, in Weehawken, at the Western mouth of the Lincoln Tunnel. And yet another is planted 20 miles south on the New Jersey Turnpike, at Exit 13, in Carteret, NJ.

"As Mr. O'Brien says, 'New Jersey is the new heart of Wall Street.'

"Direct Edge's office demonstrates that it doesn't take many people to become a major outfit in today's electronic market. The firm, whose motto is 'Everybody needs some edge,' has only 90 employees, most of them on this building's sixth floor. There are lines of cubicles for programmers and a small operations room where two men watch a wall of screens, checking that market-order traffic moves smoothly and, of course, quickly. Direct Design receives up to 10,000 orders a second.

"Mr. O'Brien's personal story reflects the recent history of stock-exchange upheaval. A fit, blue-eyed Wall Street veteran, who wears the monogram 'W. O'B' on his purple shirt cuff, Mr. O'Brien is the son of a seat holder and trader on the floor of the New York Stock Exchange in the 1970s, when the Big Board was by far the biggest game around.

"But in the 1980s, NASDAQ, a new electronic competitor, challenged that dominance. And a bigger upheaval came in the late 1990s and early 2000s, after the Securities and Exchange Commission enacted a series of regulations to foster competition and drive down commission costs for ordinary investors.

"Those changes forced the New York Stock Exchange and NASDAQ to post orders electronically and execute them immediately, at the best price available in the United States – suddenly giving an advantage to start-up operators to start-up operations that were faster and cheaper. Mr. O'Brien went to work for one of them, called Brut. The NYSE fought back, buying up smaller rivals: NASDAQ, for example, acquired Brut. And to give itself greater firepower, the NYSE, which had been member-owned, became a public, for-profit company.

"Brokerage firms and traders came to fear that a-NYSE duopoly was asserting itself, one that would charge them heavily for the right to trade, so they created their own exchanges.

"One was Direct Edge, which formally became an exchange six months ago. Another, the BATS Exchange, is located in another unlikely capital of stock market trading, Kansas City, MO.

"Direct Edge now trails the NYSE and NASDAQ in size; it views with BATS for third place, Direct Edge is backed by a powerful roster of financial players: Goldman Sachs, Knight Capital, Citadel Securities and the International Securities Exchange; its largest shareholder. JPMorgan also holds a stake. Direct Edge still occupies the same building as its original founder, Knight Capital, in Jersey City.

"The exchange now accounts for about 10 percent of stock market trading in the United States, according to the exchange and the TABB Group, a specialist on the markets. Of the 5.5 billion shares traded daily in the United States, about 833 million are bought and sold on Mr. O'Brien's platforms.

"As it has grown, Direct Edge and other new venues have sucked volumes away from the Big Board and NASDAQ. The NYSE accounted for more than 70 percent of trading in NYSE-listed stocks just five years ago. Now, the Big Board handles only 36% of those trades itself. The remaining market share is divided among about 12 other exchanges, several electronic trading plat forms and vast so-called unlit markets including those as dark pools.

"The Big Board is embracing the new warp-speed world. Although it maintains a Wall Street trading floor, even that is mostly electronic. The exchange also has its own, separate electronic arm, Arca, and opened a new data-center last year for its computers in Mahwah, NJ.

"From his office in New Jersey, Mr. O'Brien looks back across the water to Manhattan and his former office on the 50th floor of the NASDAQ building at One Liberty Plaza, and he reflects wistfully on the huge changes that have taken place.

"'To walk out of there to go across the river to Jersey City,' he says, 'That was a big leap of faith.'

"His colleague, Bryan Harkins, the exchange's chief operating officer, sounds confident about the impact of the past decade's changes. The new world is fairer, he says, because it is more competitive. 'We helped break the grip of the New York Stock Exchange,' he says.

"In this high-tech stock market, Direct Edge and the other exchanges are sprinting for advantage. All the exchanges have pushed down their latencies – the fancy word for the less-than-a-blink-of-an-eye that it takes them to complete a trade. Almost each week, it seems, one exchange or another claims a new record. NASDAQ, for example says its time for an average order 'round trip' is 98 microseconds – a mind-numbing speed equal to 98 millionths of a second.

RENEW TODAY!
(SEE PAGE 2)

"The exchanges have gone warp-speed because traders have demanded it. Even mainstream banks and old-fashioned mutual funds have embraced the change.

"'Broker-dealers hedge funds, traditional asset managers have been forced to play keep-up to stay in the game,' Adam Honore, research director of the Alte Group, wrote in a recent report.

"Even the savings of many long-term mutual fund investors are swept up in this maelstrom, when fund managers make changes in their holdings. But the exchanges are catering mostly to a different market breed – to high frequency traders who have turned speed into a new art form. They use algorithms to zip in and out of markets, often changing orders and strategies within seconds. They make a living by being the first to react to events, dashing past slower investors – a category that includes most investors – to take advantage of mispricing between stocks, for example, or differences in prices quoted across exchanges.

"One new strategy is to use powerful computers to speed-read news reports – even Twitter messages – automatically, then to let their machines interpret and trade on them."

Peeping Tom Traders

"By using such techniques, traders may make only the tiniest fraction of a cent on each trade. But multiplied many times a second over an entire day, these fractions add up to real money.

According to Kevin McPartland of the TABB Group, high-frequency trading not accounts for 56% of total stock market trading. A measure of their importance is that rather than charging them, some exchange not pay high frequency traders to bring orders to their machines.

"High-frequency traders are 'the reason for the massive infrastructure,' Mr. McPartland says. 'Everyone realizes you have to attract the high-speed traders.'

"As everyone goes warp speed, a number of high-tech construction projects are under way.

"One such project is a 428,000-square-foot data center in the western suburbs of Chicago opened by the CME Group, which owns the Chicago Mercantile Exchange. It houses the exchanges Globex electronic futures and options trading platform and space for traders to install computers next to the exchanges' machines, a practice known as co-location – at a cost of about $25,000 a month per rack of computers.

"The exchange is making its investment because derivatives as well as stocks are being swept up in the high-frequency revolution. The Commodity Futures Trading Commission estimates that high frequency traders now account for about one third of all volume on domestic futures exchanges.

"In August, Spread Networks of Ridgeland, Miss., completed an 825-mile fiber-optic network connecting the South Loop of Chicago to Cartaret, NJ, cutting a swath across Central Pennsylvania and reducing the round-trip trading time between Chicago and New York by three milliseconds, to 13.33 milliseconds.

"Then there are the international projects. Fractions of a second are regularly being shaved off of the busy Frankfurt-to-London route. And in October, a company called Hibernia Atlantic announced plans for a new fiber-optic link beneath the Atlantic from Halifax, Nova Scotia, to Somerset, England that will be able to send shares from London to New York and back in 60 milli-seconds.

"Bjarni Thorvardarson, chief executive of Hibernia Atlantic, says the link, due to open in 2012, is primarily intended to meet the needs of high-frequency algorithmic traders and will cost hundreds of millions of dollars.

"'It's very important for these algorithmic traders to have the most advanced technology,' he says….

"The data center in Weehawken is a modern building that looks more like a shopping mall than a center for equity trading. But one recent afternoon, the hammering and drilling for the latest phase of expansion seemed to conjure up the wealth being dug out of the stock market….

"The 'flash crash,' the harrowing plunge in share prices that shook the stock market during the afternoon of May 6 last year, crystallized the fears of some in the industry that technology was getting ahead of the regulators. In their investigations into the plunge, the SEC and Commodity Futures Trading Commission found that the drop was precipitated not by a rogue high-frequency firm, but by the sale of a single $4.1 billion block of E-Mint Standard & Poor's 500 futures contracts on the

Chicago Mercantile Exchange by a mutual fund company.

"The Fund company, Waddell & Reed Financial of Overland Park, Can., conducted its sale through a computer algorithm provided by Barclay's Capital, one of the many off-the-shelf programs available to investors these days. The algorithm automatically dripped the billions of dollars of sell order into the futures markets for 90 minutes and as other traders jumped in to sell their holdings."

And then *The New York Times* seems to believe that sets matters right with the remark. But there was no attempt to disrupt the market, the regulators found. However, it shows the hazards of providing the infrastructures for split second gambling across continents and oceans in a world where the official faith in a self-balancing market, has already brought to the economy to its knees.

Obviously, Mr. William O'Brien had his own scheme of diverting the *Times* from its usual excellent reporting by providing some fresh information on recent progress the world of algorithmic trading in the high heavens and the deep seas, in return for the *Times* keeping politely inarticulate on the interception of internet stock orders to earn a commission without ever having acquired the stock.

W.K.

Why Must Society's Suppressed Problems Elbow Their Way to a Partial Recognition?

The Wall Street Journal (03/01, "Forget Pep Talks; Governors Warn of Tough Times" by James R. Hagerty and Ben Casselman) is groping in the shadows what had been had been fully recognized, and suppressed decades ago: "New governors in 28 US states are starting to take office with somber warnings to constituents of more tough times amid revenue shortfalls and a weak job market.

"With sagging economies, soaring budget deficits, soaring budget deficits and the loss of federal stimulus moneys, incoming governors face the deepest fiscal crisis in decades and expectations that they will remain true to campaign pledges to slash spending and taxes."

However, what still remains unmentioned is that what has been suppressed is not borrowing, but fully prepaid investment of society in its human capital that was briefly recognized as the best investment that a government can make. This consists not only of the education and training. but the opportunity of the highly educated labor force to employment worthy of their training, the health of their families, suitable care of the environment, and adequate infrastructures to serve a rapidly urbanizing world.

But that – though briefly recognized – has been suppressed. The very name of the economist who had reached these conclusions from the wrong forecasts of the many hundreds of economists sent by Washington to study the damage suffered by the once great trading nations, Japan and Germany. Some sixteen years later, one of these economists – Theodore Schultz of the University of Chicago published a paper concluding how wide of the mark, the forecasts of his colleagues and himself had been. This he attributed to their having concentrated on the physical wartime destruction, and overlooked the crucial importance of the detail that the highly trained human resources had had come through the ordeal relatively intact.

And from that in a stroke of genius he concluded that the investment of a country in its human capital – that would of course include proper care of the environment, adequate infrastructures for the rapidly urbanizing world, are the most productive investments governments can make. This is becoming ever clearer today when countries rich in mineral and other natural resources, like Brazil, or Africa, are unable to take advantage of these economically because of their inadequate investment in human capital.

And that is the dilemma that haunts the world today. Made worse, by the fact that political power has been left in the hands of the speculative financial system that has suppressed the teachings of Schultz and others in the first place. This, too, had been predicted by generations by economists and sociologists: that when power mover moves from once class to another, the new class that has acquired economic ascendancy, must not leave political control in the hands of the class that has been replaced in economically. Do that and inevitably the new economic set up will be sabotaged. That is the key to the ever deepening economic crises that simply refuse to go away.

However, let us return to *The Wall Street Journal:* "'I don't think a grand ceremony – would be appropriate,' Andrew M. Cuomo said Saturday after being sworn in as New York's governor. The Democrat promised to put a lid on property taxes and shrink the state's government.

"He said budget troubles were only part of the problem in a state that also faced a 'trust deficit. 'Too often government responds to the whispers of lobbyists before the cries of the people,' Mr. Cuomo said.

"Michigan's new Republican governor, Rick Snyder, issued a call to residents during his inauguration speech: stop infighting and believe the once-proud state can stage a successful turn-around. The former venture capitalist argued during the campaign that Michigan must cut taxes and trim spending.

"In his address Saturday, Mr. Snyder implored Michigan's people to move beyond past woes, including high unemployment and home-foreclosure rates.

"'This election was the point where we understood that the old ways don't work,' Mr. Snyder said adding that the state could build on assets such as its natural resources, universities, manufacturing base and people.

"In New Mexico, Republican Susana Martinez pledged to create jobs, cut back on wasteful spending and crack down on patronage. 'Government won't ask New Mexicans to do what government is not willing to do,' said Ms. Martinez, the first Hispanic woman to serve as governor of a US state. 'We won't take more of your money from you or grow the deficit because we are not willing to make the same tough decisions you have had to make.'"

Fine words skirting around the real essence of the matter, but avoiding to recognize human capital not as debt but prepaid capital investment that is the "most profitable investment that a country can make."

But without that, clearly recognized and committed to, the US and the world at large must go on evading, tumbling and bumbling right to the ultimate disaster of atomic war.

William Krehm

Why It Is Necessary to Take Back Control Over Money Creation — And Why You Should Care!

Lack of sufficient funds is the fundamental problem facing all community efforts to reduce poverty and, in general, raise living standards for all.

At the meeting held on December 2, 2010, to organize a Kingston Workers'/ Peoples' Assembly I mentioned that in 2009 Canadians paid $160 million a day on public debt interest. The portion of that carried by the people of Ontario was $64 million a day – every day, all year long which amounts to about $5 per day for every man, woman and child, or $20 a day for a family of four. Some people find it hard to believe these numbers. They can't see where we are spending $64 million a day in Ontario, but the figures are correct and easily verified.[1] It means that this money is not available for other uses. It means that our taxes are higher than necessary.

How big is $64 million? The *kingstonlife* magazine (January/February 2011) reports on p. 34 that "For two years the city has allowed $2.5 million from the province to sit unused." That's $2.5 million per year of government grants for affordable housing. That is a lot of money, but on a per capita basis it only represents what the population of Kingston pays on public debt interest in less than a week.

Our governments use these huge costs to justify cutbacks and wage freezes. Prime Minister Harper wants to reduce the federal deficit in order to reduce the debt servicing charges, but doing that will take money out of the economy and make the recession worse.[2] We need to increase the deficit, *not* with private interest-bearing dollars but dollars borrowed from our public bank, the Bank of Canada, at zero cost to the federal government. This money would be injected into the economy through investments in infrastructure, hospitals, schools, universities, recreation facilities, social support programs, the environment, industrial research and more. The wages received by those working in these areas would be spent in the community; local businesses and farmers would be strengthened; but most importantly, the influence of large corporations, banks and other wealthy financiers on government policy decisions would be reduced.

The knee-jerk reaction to the suggestion that government borrow from its own Bank is that it would cause run-away inflation. Since for over 30 years our government has *not* borrowed significantly from its own bank, but primarily from private sources at interest we might assume that there has been little inflation. We know, of course, that is not true. Just think for a moment what a house cost 30 years ago and what a similar one costs today.

"While borrowing too much money can lead to inflation, once the decision to borrow has been made it is no more inflationary for the government to borrow from the Bank of Canada than it is for it to borrow from private financial markets. *In fact, it is less inflationary by exactly the amount of the interest that the government saves by using its own bank.*"[3]

The Right Honourable William Lyon Mackenzie King, Prime Minister of Canada, said in a radio address, August 2, 1935, while campaigning to become Prime Minister, "Once a nation parts with control of its currency and credit, it matters not who makes that nation's laws. Usury, once in control, will wreck any nation. Until the control of the issue of currency and credit is restored to government and recognized as its most conspicuous and sacred responsibility, all talk of the sovereignty of Parliament and of democracy is idle and futile."

The Bank was nationalized by King in 1938 and used to the advantage of Canadians for 35 years, but during that time controls over monetary policy were gradually reduced. By 1974 monetarism and the ultra free market ideology were adopted in Canada, the government reduced its use of the Bank of Canada to finance public debt, relying almost entirely on the private sector, and *de facto control of currency and credit was taken over by the chartered banks.* As a result, when interest rates were pushed very high in 1979/80/81 and 1989/90, the federal debt soared over 3,000% from $18 billion in 1974 to $588 billion in 1997, with a corresponding increase in provincial and municipal debt and massive debt charges. In 2009 Federal interest bearing debt stood at $710 billion, and total interest bearing debt for all levels of government reached about one and half trillion.

Seventy-five years ago Saul Alinsky, a

Proposal to the CCPA National Research Fund

January 22, 2011
To COMER members:

The Kingston Chapter of COMER has adopted a resolution to send to the CCPA National Research Fund as follows:

"In 2009 we Canadians paid $160 million per day in interest charges to service our public debt (Canadian Economic Observer: Historical Statistical Supplement 2009/2010). We propose that it is time to study how we accrued this debt. It is urgent that we find ways to alleviate our public debt before our social programs and our economy are harmed by it.

"In particular, we are interested in the role the Bank of Canada has had in financing public debt since its formation in 1934. Could it play an active role in debt reduction? We invite the CCPA (and other equally concerned citizens) to research these questions."

Richard Priestman

Reference

Canadian Economic Observer: Historical Statistical Supplement 2009/2010 National accounts, www.statcan.gc.ca/pub/11-210-x/2009000/tablelist-listetableaux1-eng.htm, Table 1.3-1, Government revenue and expenditure – Total government.

Table 1.3-1 shows that interest on the public debt in 2009/2010 amounted to $58,669 million ($160.7 million per day).

The above motion was declared as an independent initiative of Kingston COMER, but that it be shared with our affiliates, and circulated for wider support. If you would like to show support for this resolution please let us know and we will add your name to it.

Community Organizer in Chicago said, "the problem with poor people is they don't have any money." We could get rid of poverty "over night" if we instituted a "guaranteed annual income" as promoted in Canada 40 years ago and spoken to more recently by Senator Hugh Segal.

"The existence of large scale poverty in Canada's generally affluent society is not a matter of dispute. The Economic Council of Canada has documented this phenomenon and helped to stimulate public debate about the reasons for it. The fact that approximately one-fifth of the people of Canada are designated poor is impressive evidence of the collective failure of existing programs to come to grips with the problem of poverty. The Guaranteed Annual Income approach has been advanced as a new solution to these problems.

"The feasibility of 'full employment' as a national objective is increasingly a matter of dispute. One school of guaranteed income advocates, led by Robert Theobald, asserts that technological advances will soon reduce the necessary labour force to 10% or less of the population. In that event some form of guaranteed income program becomes absolutely necessary to distribute the product of our economic system."

Social Policy Statement on Guaranteed Annual Income, 1971, Canadian Association of Social Workers

"The key issue in the discussion of the guaranteed annual income is neither economic nor political, but moral."[4] The money *could* be raised, but attitudes toward work and wealth question whether it *should* be. Some will ask, why should people who won't work have a right to a guaranteed income. Technical development has meant that fewer workers are needed to produce the goods society needs. This being the case are the surplus workers to be sent to the scrap heap while a few continue to fill their weeks with *work*, or can we share the nation's wealth and leisure time so that all benefit?

Those who oppose the concept of sharing the nation's wealth argue that wealth belongs to those who through their hard work and ingenuity created it, but forget about the generations who have gone before them and contributed to society's knowledge and expertise on which their wealth is based! William Krehm calls this the "social heritage" and states, "This 'social heritage' must not be appropriated entirely by those who patent an invention or a gene and employ it as though it were not based to a significant extent on this "social heritage."[5]

Could government borrowing from the

The Ambiguity of the Volcker Rule

The Wall Street Journal (15/01, "Broad Tack Expected in Implementing 'Volcker Rule'" by Aaron Lucchetti and Victoria McGrane) reports: "Washington – Top US financial regulators charged with recommendations on how to implement the 'Volcker rule' appear to be leaning against suggesting specific assets or trades, and instead might focus on the amount of risk being carried by a firm or trading desk, according to people briefed on the negotiations. "Included in the sweeping financial overhaul passed last summer, named for former Federal Reserve Chairman Paul Volcker, seeks to prevent banks from putting capital at risk by prohibiting proprietary trading and banning certain relationships with hedge funds and private-equity funds. It left much of the details on how to do that with regulators.

"After months of sometimes tense works, financial regulators reached a tentative deal in recent days on recommendations about how the Volcker rule should be implemented, said one industry official briefed on the situation. The study is expected as early as Tuesday, when the regulators who comprise the administration's Financial Oversight Stability Over sight Council meet.

"Regulators have kept details of the nearly 80-page draft close, and its content is subject to change until the council votes to approve it.

"What is becoming clearer is that the document likely won't propose that regulators look at each and every trade, people briefed on the matter said. Instead, it will discuss reviews of large trades and the amount of risks firms are taking on a broader basis. Regulators would then decide whether trading desks are taking on too much risk. This approach would be seen as a win for the financial industry, and could irk Democrats who pushed the provision into law last year.

"Another concept could be aired: giving Wall Street firms some say in defining what they do to meet client's needs, an area of activity exempt from the rule. Federal regulators would adjust or reject the firms' approach and hold them accountable for sticking to their plans, these people say. As a result, a trade that sets off Volcker detectors at one firm might pass muster at another.

"One of the hardest problems facing regulators is measuring the risk a firm is taking on. Among the factors likely to be discussed in the study are the size of the position, how long it will be held for and something called the Sharpe Ratio, people briefed on the discussions said. The Sharpe Ratio is a risk measure developed by Nobel laureate William F. Sharpe that shows the trade-off between risk and return.

"While the report is likely to include some minor bright points in the eyes of Wall Street, analysts still expect the Volcker hit to be significant. JPMorgan, for example, predicted that the rule change will shave 14% off estimated earnings for Goldman Sachs Group Inc. and Morgan Stanley in 2012, have seen high-profile traders depart or plan to start new firms in anticipation of the new restrictions as 'pure proprietary' trading desks are shut down.

"Critics of the Volcker rule warn its restrictions will put US banks at a disadvantage compared with its foreign competitors. JPMorgan's report said European banks will be 'the clear winners' since regulators there appear opposed to implementing Volcker-like rules.

"The study is likely to contain harsh language in the way if describes and analyzes proprietary trading, including a discussion of why it is risky and should be regulated, said people briefed on regulators' thinking."

We might add that "proprietary banking" is in essence one of the powerful legislative tools bought in by President F.D. Roosevelt in his *Glass-Steagall Act* brought in 1935 that forbade banks from acquiring other "financial pillars" – in those remote days before credit cards had come in these other non-banking pillars consisted essentially of stock brokerages, insurance and mortgage companies. The reason for the legislation was to prevent banks from acquiring access to the capital of such "other pillars" they would simply use their capital to extend gambles and finance.

W.K.

Bank of Canada to finance public debt be done? Yes, but only by electing people to parliament who support the concept of financing public debt with public money for investment in public infrastructure and public services. Unfortunately, none of the parties in parliament will discuss these ideas publicly. None has shown a willingness to provide leadership on this issue.

So, how do we elect these people?

We ask every candidate if he or she will make a public commitment to support and promote use of the Bank of Canada to finance public debt, making it very clear to the candidates that we will only vote for those who do make this commitment. If none of the party representatives agree to make such a commitment then we find someone to run as an independent candidate, and rally the community to support that person. Some will argue that an independent candidate has no power and can do nothing. But what good is it to have party representatives in Parliament who do not use their position to change the fundamental flaw in our financial system?

Richard Priestman

1. Canadian Economic Observer: Historical Statistical Supplement 2009/2010 National accounts, Table 1.3-1 Government revenue and expenditure – Total government. Table 1.3-1 shows that interest on the public debt in 2009 amounted to $58,669 millions or $160.7 millions per day.

2. Jim Stanford: "Economic 'recovery' fuelled by household debt is shaky," *CCPA Monitor*, July/August 2010, p. 20-21: "…the efforts by Canadian governments to slash their deficits in coming years would make a bad situation far worse, if in fact private debt slows, stops or (God help us) reverses."

3. Don Findlay: "There Is a Way to Reduce Taxes Without Increasing the Deficit, Causing Inflation, or Destroying Canada's Social Programs!" 1997.

4. Rev. Gerald W. Paul, Iona College, University of Windsor, *Communiqué*, July 6, 1973, p. 1, and Philip Wogaman, "The moral Issues of the Guaranteed Annual Income."

5. Krehm, William (March, 2004). "Meltdown – Money, Debt and the Wealth of Nations," Volume 4, p. 35.

The World Is Not Necessarily Going to Pot — Two Contrasting Reports Prove There Is Still Hope

Our first bit of evidence is from *The Wall Street Journal* (01/04, "All the President's Men" by Julia M. Klein writing from Philadelphia. I quote: "With temperatures in the mid-20s, the mid-December dedication of the President's House was an occasion for celebration (that the site, after eight years of controversy and delays, was finished), thoughtful rumination (about the entanglement of liberty and slavery in Federalist America) and incipient frostbite.

"Abutting the Liberty Bell Center in the heart of Independence National Historic Park, the $11.9 million project combines architecture and archeology, memorial and exhibition. 'The President's House: Freedom and Slavery in the Making of a New Nation' touches on the uses and abuses of federal power, the spread of slavery, Philadelphia's 18th-century free-black community – and, most tellingly, the occupants of the house itself.

"The original President's House was the seat of US executive power from 1790 to 1800 – the home of President George Washington and his successor, John Adams. Built in the late 1760s at what is now the corner of Sixth and Market Streets and mostly demolished in the 1830s, the gracious Georgian mansion was at various times the residence of British Gen William Howe, the traitor Benedict Arnold (who hatched his treason here) and Revolutionary War financier Robert Morris.

"But not only dignitaries called this place home. During Washington's presidency, nine 'enslaved people' (in the exhibition's vernacular) also lived and worked here, just a block from Independence Hall.

"Washington periodically rotated his slaves back to his Mount Vernon, VA, plantation to circumvent Pennsylvania's *Gradual Abolition Act* of 1790, which would have freed them after six months of residency. Two of the nine eventually escaped and were never recaptured, despite Washington's signing of the 1793 *Fugitive Slave Act*.…

"That the place was all but forgotten for so long – and its site used for a public restroom – is amazing. In the January 2002 issue of the *Pennsylvania Magazine of History and Biography*, the historian Edward Lawler Jr. pinpointed the house's precise location and features, and lit an intellectual conflagration by declaring that 'the last thing the visitor will walk across…before entering the Liberty Bell Center will be the slave quarters that George Washington added to the President's House.

"Grass-roots organizations – including the Avenging the Ancestors Coalition, Generations Unlimited, and the Ad Hoc Historians – agitated for recognition of the site, and especially of its significance for African-Americans.

"After initial resistance, the National Park Service and the city of Philadelphia embraced the memorial project. Rhetorical battles were waged over design and interpretation, including how to balance the mansion's presidential history with its connections to slavery. (That battle seems to have been fought to a draw.)

"An archeological dig in 2007 uncovered the house's 18th-century foundations – the remains of the kitchen and corridors where slaves toiled and of a bay window addition that may have inspired the design of the Oval Office.…

"The exhibition mentions the Whiskey Rebellion, the *Alien and Sedition Acts* of 1798, the migration of Haitian slave owners to Philadelphia, the yellow fever outbreaks of the 1790s, and the formation of Philadelphia's first two black churches. It suggests that contact with Philadelphia's free black community, as well as white abolitionists, heightened the restlessness of Washington's slaves.

"But restoring those nine people to history is the project's signal accomplishment. In the moving finale of his dedication address, Philadelphia's Mayor Michael A. Nutter recited their names, etched on a granite wall on the structure's east side.…

"Videos sum up the little that is known of their lives, describing the escapes of Oney Judge, maid to Martha Curtis Washington, and Hercules, George Washington's gifted chef. Learning she was about to be given to Martha's grandchild, Judge fled, in 1976 to New Hampshire, where she married and had three children. Washington apparently never stopped pursuing her. Under his steward's name, he placed an advertisement for a 'light Mulatto' and offered a reward of $10 or more for her capture.

"Hercules, shipped back to Mount Vernon to make bricks, snuck away from the Virginia Plantation in 1797, on Washington's 65th birthday. He left behind at least three children and virtually no documentary trail.

"Washington was, we now know, conflicted about slavery. As the exhibition relates, his will freed the 123 slaves he owned with emancipation to occur after his wife's death. She liberated them herself in 1801. But she did not emancipate her own 153 'dower' slaves, from the estate of her first husband; she left them instead to her grandchildren.

"That created a conundrum on the plantation: mixed marriages between enslaved and free spouses. A video asks just how this would have played out in human terms – and whether Washington and his wife ever discussed the differing fates of their workers. These are provocative questions – portals to yet more dark, intricate corridors of history.

Society in These Troubled Times does Show Real Humane Concern

The Toronto Star (15/01, "Rescue from Mogadishu" by Michelle Shephard) reports an initiative of deep and effective concern that has the victims of murderous bigotry in Africa to a haven in polar regions: "Harstad, Norway – Ismao Khalif Abdulle stared at the map of Norway for much of the two-hour

The US Fed's Dubious Bonanza

The New York Times (11/2011, "Fed's Crisis Investments Are Showing Big Returns" by Sewell Chan) is not above kidding itself and a credulous public. We quote: "Central banking in the aftermath of a financial crisis is a lucrative business it turns out.

"The Federal Reserve will deliver a record $78.4 billion to the Treasury from its investments last year, a 65 percent increase from the $47.4 billion it transferred in 2009, according to preliminary estimates released Monday.

"'It's interest that the Treasury didn't have to pay to the Chinese,' the Fed's chairman, Ben S. Bernanke said, half-jokingly, during a Congressional hearing on Friday, at which he offered a rough preview of the figures.

"The transfer to the federal coffers is a by-product of the ballooning Fed balance sheet, which now stands at nearly $2.5 trillion – nearly triple what it was at the end of 2007, when turmoil from the bursting of the housing bubble began to disrupt financial markets.

"The Fed has been amassing assets in an effort to stimulate growth by holding down long-term rates, which the Fed influences more directly, have been essentially zero for corporations and households and have lifted securities markets, though unemployment remains stubbornly high.

"Last March, the Fed completed the purchase of $1.25 trillion in mortgage-backed securities, and in November, it began buying $600 billion in Treasury bonds.

"Interest income from its investment portfolio has produced record profits for the Fed for two consecutive years. But over time, when economic conditions improve, the portfolio could become a risk, because the investments could lose value when interest rates eventually rise.

"'From the taxpayers' view, I think it is a mistake to make much of this number either way,' said John H. Cochrane, an economist who has been critical of the central bank. 'The Fed is acting like a huge hedge fund on our behalf. It is borrowing at very low short-term rates and investing in long-term government bonds. It made a profit on those investments last year, but it is bearing a lot of risk.'

"Mr. Cochrane, a University of Chicago finance professor, said the Fed was intentionally bearing those risks to support housing and other markets.

"'But inevitably, with a big portfolio of long-term bonds, mortgages and risky securities, the day will come when the Fed loses money on those investments, at least on a mark-to-market basis,' Mr. Cochrane added, referring to the accounting the Fed uses to fairly value its balance its balance sheet.

"In testimony before the Senate Budget Committee on Friday, Mr. Bernanke acknowledged the risk. He gave an estimate of the Fed's profit for 2010 and said that it was 'much higher than normal.'

"Should it be the case that short-term interest rates rise, which of course could happen if the economy recovers and we need to normalize monetary policy, then those profitable programs, from the perspective of the federal deficit. 'Remittances could go down,' Mr. Bernanke said Friday."

Moreover, with the very large practically deregulated banks freed from the restrictions on acquiring other "financial platforms" that had been denied them under President F.D. Roosevelt, they were in a position to throw up a rickety skyscraper of financial make-believe with elevators that ran always upward, never downward, at ever-dizzier speed. It was denied them even to slow down, for by pushing their gamble to the uttermost that would bring on a collapse. Our readers will have noted that the three dimensions of speculative banking that the banks of the postwar were engaged in – stock brokerages, insurance and mortgage financing were at the head of the speculative binge that brought on the collapse of the housing market. They should have noted as well, that the leading character entrusted with bringing in the over-advertised was a leading official with responsible careers both with Treasury and the New York Federal Reserve.

And yet one of the most productive lessons that came out of World War II, warned the world of the assured disaster of such a set up. No sooner had the surrender of Japan and Germany taken place than Washington sent many hundreds of economists to those two countries to study the damage suffered during the war to predict how long it would take before they could resume their roles as great trading nations. Sixteen years later one of these, Theodore Schultz wrote an essay in which he asserted that he and his colleagues had been so wide of the mark in their forecast, mostly because they had concentrated on the physical destruction, and given little heed to the detail that the key human resources had come out of the struggle basically intact. And then in what can only described as a stroke of genius. he concluded that he and his colleagues had failed so badly in their assignment, because they had concentrated on the physical destruction in the war, but paid little heed to the detail that the human capital had come through war almost intact. For a few years Schultz was celebrated and decorated, and then all mention of him completely suppressed. And, left there, the prospects of society are hopeless. For that human capital comes prepaid. It must be seen, of course, to include not only the learning already paid for, but the good health, good environment, and adequate infrastructures for the rapid urbanization that is taking place. The children of healthy parents tend to be healthier, those of educated parents easier to educate.

Without the concept of human capital, indeed, there can be no serious accountancy. For by treating the greatest investment – completely prepaid – as debt, nothing that could be mistaken for serious accountancy is possible. Left unused to balance a budget that is simply beyond balancing, you leave the world doomed to operate in deep darkness without anything that could be mistaken for accountancy.

W. Krehm

flight from Oslo to this city 200 kilometers north of the Arctic circle, trying to imagine what a day with only a couple of hours of winter twilight would be like.

"'It's okay,' he shrugged eventually. 'The sun in Mogadishu used to drive me crazy.'

"The skinny teenager, who had seen snow only on TV and thought an African evening that dipped to 18°C was chilly, was traveling to his new home in the land of polar nights and midnight sun, ready to deal with whatever culture shock awaited him.

"But even with his laid-back nature and the most open of minds, the 18-year-old refugee could not believe his eyes when he was greeted at the airport last week by a smiling 6-foot-8 Somali.

"Mohammed Osman, known as just 'Osman' or by his Norwegian nickname meaning 'Little Friend' was part of Ismail's welcoming crew. Like Ismail, he had been given refuge in this picturesque town of 23,500.

"Osman was just one of many unexpected surprises for the teenager, who had gone from seeing the worst of humanity to experiencing the best. One year ago, Ismail was sitting in a Mogadishu government compound fighting back tears about how he became a victim of Al Shabab, a Somali-based insurgency that has declared itself Al Quaeda's proxy in the Horn of Africa.

"After refusing to join the group, he and three other boys were taken to a stadium where Shabab members cut off their right hands and left feet in a barbaric public amputation in the name of sharia law.

"The boys' limbs were later hung in the town's square as a lesson to others.

"In Somalia, a country mired in an unending war, Ismail's story was only one of many. But it was also one that touched many.

"Toronto's Somali Diaspora started a group called Project Ismail and lobbied to get Ismail to Canada. Abdul Hassan, a Somali-born Canadian living in Nairobi, enlisted an underground network of supporters to spirit Ismail out of Somalia and into Kenya.

"A month after his rescue, the United Nations declared Ismail a refugee in need of protection, and the teenager applied for sponsorship outside Africa. His first choice was Canada, which is believed to have the largest Diaspora outside of Africa (and is the country where his beloved rescuer, Hassan, has citizenship). Other choices included Norway and Finland, where he has half-siblings from his now-deceased father's first marriage.

"In just a matter of weeks, Norway accepted his application on an emergency basis, and Ismail's stunning odyssey ended here last week in the rugged far northern reaches of the country.

"Hassan, whom Ismail calls his 'second father,' accompanied the boy on flights from Nairobi to Oslo, and then finally – along with a *Star* reporter – to Harstad.

"Overcome by emotion, the slight teenager could not believe his fortune.

"'They could not break my spirit,' Ismail said of the Shabab. 'If they break your spirit you cannot go anywhere. They only took my hand and foot.'

"Then, flashing a grin, he added, 'There was a day when I could not even hold a cup of water, and look at me. I am in Norway!'

"Seeing another Somali in Harstad was only Ismail's first surprise. Just hours after arriving and on his first trip to the grocery store (Corn Flakes, Coke, a bag of candy, buns and a bag of oranges) Ismail was stunned to find more boys from Somalia. In all, he would discover, there are as many as a dozen Somali residents among the nearly 150 refugees living in this town."

A Very Concerted Effort

"Ola Steinvoll, a barrel-chested, big-hearted Norwegian who runs the refugee program here, says Harstad works hard to integrate the asylum-seekers, providing intense language and life skills training and then a university-level education.

"Within his first few days, Ismail had been given a bank card for a modest account and a medical checkup, had registered with police and had filled out the paperwork for his social insurance number and new identification (where his name is spelled Ismail, as opposed to an earlier spelling of Ismael).

"The prospect to get him proper prosthetic limbs also began. Incredibly, the small town has not one but two companies that customize prosthetics.

"Ismail was also provided with a temporary apartment – which he proudly swept every morning, although the floor was spotless. Eventually he'll settle in with Somali roommates elsewhere. The formal refugee program here is just two years old, and most credit 54-year-old Steinvoll, along with other staff for its success.

"'For refugees here he is not the big boss, he is a father, he is our friend,' says Ahmed Ayoub, a 33-year-old Yemeni who was among the first to arrive when the program started. 'He is smiling all the time. If you are sick, he will come to you. If you need something, he will give it to you.'

"By the second day here, Ismail has learned his first Norwegian word, *bestefar* which means 'grandfather' and is what he calls Steinvoll.

"For Steinvoll, a married father of two boys now in university and a former healthcare system worker, the experience of helping refugees settle has been life-altering. 'Earlier I was prejudging people,' he said. 'I thought Canadians are like this, Americans are like this, Somalis are this, they are lazy, Arabs are criminals.'

"'After four weeks in this job I realized this is totally wrong. Now when I am out speaking about my job I say that.' 'Abdul Hassan' is actually an alias because the Canadian father of three still lives in Nairobi, where al Shabab has a presence.

"I find some guys in the audience and I say, refugees are like me and you and are totally different, and they need to be treated as individuals, with respect.

"Osman was one of the first refugees here. After two years, he is already fluent in Norwegian and English. Recently, his wife and four children joined him, also accepted as refugees. Osman is eager to help Ismail and already knew his story, because he had read the local news report in the summer of 2000, when Ismail and the other boys had their limbs amputated.

"Osman had also escaped the Shabab, which is designated a terrorist group in Canada and the US.

"The 30-year-old is a trained nurse but worked for the Coca-Cola plant in Mogadishu making syrup, which was a more lucrative job and one he needed as an only child, having to support his parents, wife and young children.

"But the Shabab wanted him. 'I was told I had to be prepared like a good soldier because I was so strong,' he recalls. I was told it was the military and I said, 'No. no, I won't take a gun.'

"They accused him of working for a 'Jewish company,' and came looking for him. Instead they found his parents and executed them both….

Models *from page 2*

their capital reserves. Though banks do raise their capital in cash, little is left in that form.

In short the guaranteed annual income frustrated experiment in only one aspect, but a highly important one was left – a treasury of costly lessons learned and then violently removed from public access and memory.

William Krehm

"Abdul Hassan had read about Ismail's plight in a January 2010 *Star* article and vowed to help him. When he met Ismail four months later in Mogadishu, he was captivated by the teenager.

"Along with members of Toronto's Somali Diaspora who started Project Ismail, Hassan managed to get Ismail from Mogadishu to Nairobi. The *Star* agreed not to disclose the exact route of the escape as that could jeopardize the lives or jobs of his rescuers.

"Sponsorship requests often take months to process – in the case of Canada's busy Nairobi bureau, sometimes years. Hassan said he was happy to adopt Ismail during that time and shelter him in his Nairobi apartment with his children."

What a superb reporting job *The Toronto Star* has done! Our congratulations.

W.K.

Lessons Out of China

We have long been vocally aware that our society is shaped largely by our technology. To this we must add, and by the technology of the Heavenly Lord which we irreverently dismiss as Chance.

It was a recent essay of Nicholas D. Kristof in *The New York Times* (09/01, "China Rises, and Checkmates' from Beijing: "If there's a human face on Rising China, it belongs not to some Politburo chief, not to an internet tycoon, but to a quiet, mild-mannered teenage girl named Hou Yifan.

"Ms. Hou (whose name is pronounced Ho Ee-fan) is an astonishing phenomenon: at 16, she is the new women's world chess champion, the youngest person, male or female, ever to win a world championship. And she reflects the way China – by investing heavily in education and human capital, particularly in young women – is increasingly having an outsize impact on every aspect of the world.

"Napoleon is famously said to have declared: 'When China wakes, it will shake the world.' That is becoming true even in spheres that China historically has had little connection with, like chess, basketball, rare earth minerals, cyber warfare, space exploration and nuclear research.

"This is a process that Miss Hou exemplifies. Only about 1 percent of Chinese play chess, and China has never been a chess power. But since 1991, China has produced four women's world chess champions, and Ms. Hou is the one with by far the most promise.

"At this point, I have to put my sensitive male ego aside. You see, Ms. Hou gamely agreed to play me after I interviewed her. She had just flown into Beijing after winning the world championship, and she was exhausted – and she shredded me in 21 moves.

"Most dispiriting, when I was teetering at the abyss near the end of the game, her coach nudged her and suggested mischievously that we should switch sides. Ms. Hou would inherit my impossible position – and the gleam in her coach's eye suggested that she could still win.

"I protested that I could survive being beaten on the chess board by a school-girl. But to be toyed with, like a mouse by a cat – that would be too much. Ms. Hou nodded compassionately and checkmated me a few moves later.

"At 14 she became the youngest female grandmaster ever. She's still so young that it's unclear just how remarkable she will become.

"Women in general haven't been nearly as good at chess as men, and the world's top women are mostly ranked well below the top men – but Ms. Hou could be an exception. She is the only female chess player today considered to have a shot at becoming one of the top players in the world, male or female.

"Cynics sometimes suggest that China's rise as a world power is largely a matter of government manipulation of currency rates and trade rules, and there's no doubt that there's plenty of rigging and cheating going on in every sphere. But China has also done an extraordinarily good job of investing in its people and in spreading opportunity across the country. Moreover, perhaps as a legacy of Confucianism, its citizen have shown a passion for education and self-improvement – along with remarkable capacity for discipline and hard work, what the Chinese call 'chi ku,' or 'eating bitterness.'

"China used to be one of the most sexist societies in the world – with female infanticide, foot binding and concubinage – but it turned a corner and now is remarkably good at giving opportunities to girls as well as to boys. When Ms. Hou's parents noticed her interest in a chess board at a store, they promptly bought her a chess set – and then hire a chess tutor for her.

"Ye Juangchuan, the chief coach of the national men and women's teams, told me that he played Ms. Hou when she was 9 years old – and was stunned. 'I saw that this kid was special,' he told me, and he invited her to move to Beijing to play with the national teams. Three years later she was the youngest girl ever to compete in the world championships.

"It will be many, many decades before China can challenge the United States as the overall 'No. 1' in the world, for we have a huge lead and China still must show that it can transition to a more open and democratic society. But already in discrete areas – its automobile market, carbon emissions and now women's chess – China is emerging as No. 1 here and there, and that progress will continue.

"There's a lesson for us as well. China's national commitment to education, opportunity and 'eating bitterness' – those are the qualities that we in the West might emulate as well. As you know after you've been checkmated by Hou Yifan."

However, there is no end of further lessons to be learned. Those lessons can be seen as coming from a divine creator who ultimately – out of the modesty that we must recognize as an inevitable trait of a Divine Creator – or as due to the frequent – alas not inevitable – wisdom of human societies. For who can doubt that without the single-child restriction of the previous Communist regimes, Chinese parents are unlikely to have concerned themselves with development of talents of their sole offspring regardless of its sex.

Where were the wise men to foretell the eventual benign effect that was made of this harsh restriction of a bloodthirsty dictatorial regime?

It also emphasizes from yet another source the importance of recognizing human capital not as a debt, but the most productive prepaid investment that a society can make.

Would we have to contract China's Ms. Hou to convince our Western governments of the key importance of human capital as an investment rather than as a debt?

William Krehm

The Interaction of Market and Non-Market Forces

In rereading my book, *Price in a Mixed Economy: Our Record of Disaster,* published in 1975, I was astounded by the extent of the contributions of many powerful analysts much of whose contributions had eluded my aging memory. Their powers of pioneering were particularly great in France and to them COMER is greatly indebted – not only for the early recognition of our efforts, but for their notable contributions to the development of our program.

The public sector and the various social revalorizations could be represented as multidimensional spaces projecting onto the market through their common dimensions. Each of these spaces has its own peculiar geometry that functions spanning it must obey. Some of these geometries could be regarded as non-Euclidean. The process of capital accumulation does not seem destined to go on gaining momentum indefinitely. At a certain point, the 'work ethic' would seem to decay and accumulation downgraded as the major aim in life: society starts developing doubts about the virtues of exponential development, and even turns to J.S. Mill's notion of the "stationary state." The use of a curved space in the given model might remind economists that such changes in comportment are not to be explained by market logic.

I will set up the model in three distinct zones. To the lowest of these I relegate influences upon price originating outside the market. One of these would be the Social Lien reflecting the relative growth of the public sector. Another would be Social Revalorization that translates the degree of esteem accorded a social group into economic terms. A final category belonging here I will label Random Influences, comprising such things as wars and natural catastrophes.

My topmost zone is the encounter area of supply and demand, the price determinants of pure market theory. By conventional reasoning the factors arising in the lowest zone should influence price only by working through the supply-demand relationship in our topmost zone: for it is only so that they can be assimilated into the symmetries of equilibrium models. Actually this is far from the case. As often as not they act upon price without passing through the supply-demand circuits. Instead they have an impact on prices and wages directly in an intermediate zone. This intermediate zone for the most part escapes the attention of conventional theory. We could call it the "mixer zone" or the "induction zone."

Happenings in this zone are determined by social forces and institutions that have become crucial. Though these have been analyzed in part or as a whole by many writers, the best summary comes from Jacques Valier.[1] Valier shows that the complex of existing institutions translates all "inflationary" tensions – no matter how or where they may originate – into a sustained upward price ramp. For brevity I will refer to this institutional complex as the "Valier Complex."

For this to have effect, an unfailing reserve of permissive demand is needed that will allow entrepreneurs to raise their prices to cover themselves against wage increases or other rising costs. Such permissive demand is assured not only by the wage increases in question, but by policy commitments to near-full employment and by social legislation. That makes it possible for trade unions to concentrate their attention on wage increases. Such higher wages won in prospering industries tend to become suffused throughout the economy. Minimum wage legislation and the very scope of collective agreements contribute to this. The duration of labor contracts over several years lessens the likelihood of downward adjustment of wages during the recessions.

The oligopolistic organization of key industries prevents them from expanding their production blindly to the point where marginal revenue equals marginal costs. They thus command reserves of unexploited market power that often enables them to pass higher wages into price. Productivity increases, moreover, are more likely to result in quality improvement and expanded capacity than in reduced prices.

Such market structures transmit "inflationary tensions" throughout the economy, but tend to block deflationary adjustments. In its net effect the Valier Complex can be likened to an electronic rectifying tube that will pass impulses only in a single direction and thus converts alternating current into direct current.

Valier draws a sharp distinction between "creeping inflation" and "inflation proper." The former he sees as a persistent price climb related to changing market structure, the latter as a cumulative runaway phenomenon. He refuses to view "creeping inflation" as an accidental or pathological phenomenon.[2] "Creeping inflation" he sees likely to appear in developed countries: in underdeveloped lands it is his "inflation proper" that is more customary. I prefer the term "structural price rise" instead of his "creeping inflation," for in the word *inflation* ("blowing up") we have the suggestion that such price movement is both pathological and curable. It is important to avoid having elements of diagnosis creep into our nomenclature.

The gap in Valier's model is that the tensions that he sees feeding into his transmitting mechanism are essentially random impulses. He fails to step outside the market to seek *non-random* sources of such tensions in our changing non-market structures.[3] I attempt to fill the gap by introducing into my lowest zone the Social Lien and Social Revalorization as well as Random Influences.

Random Non-Market Influences in the lowest zone will give rise to lines of influence running directly to Supply and Demand into the topmost zone, the Market Zone. Usually such Random Influences (wars, natural catastrophes) have a negative effect upon Supply, and hence I have a broken line from Random Influences to Supply. (In this graph broken lines denote a negative influence, solid lines a positive one.) On occasion, of course, this effect on Supply could be positive, as when a local oversupply results from customary markets having been shut off by war. I ignore this to avoid overloading the diagram. Similarly I will take the effect of Random Influences on Demand to be positive.

The two major classes of non-random influences originating in the Non-Market Zone will exert much of their effect without first passing through the Supply-Demand confrontation on the top levels. This I show by grouping the interacting factors of the "mixer zone" as two closed circuits, and having the Social-Lien and Social-Revalorization influences coming from the lowest zone feed into these directly. The closed circuit shows that the factors involved tend to be mutually inductive: they act one upon the other directly as multipliers without having to work via the Supply-Demand encounter in the top zone – though, of course, they may very well do that as well.

Let us examine some of the relationships in this model. An upward price gradient powered by the Social Lien must in time induce a parallel trend in interest rates.

This is shown by an unbroken line from the Social Lien in the bottom zone to the box Interest Rate Gradient on the positive price circuit in the middle zone. This in turn not only feeds back positively to increase public expenditure (higher service charges on the public debt); together with the price increase this can knock out entire areas of the private sector, and make it necessary for the state to take over its functions. Hence there is another box on the positive price circuit: "Abandonment of economic areas by private sector." This feeds back into the Social Lien on the lowest level with a positive line.

Higher interest rates may, of course, depress investment, demand and prices. This is shown by broken lines running from the Interest Rate Gradient box on the positive circuit to Demand and Supply in the topmost zone. Yet if expectations of a continuing price rise and further climb of interest rates are there, entrepreneurs could start borrowing and investing more in anticipation of still higher interest rates and prices. The signals here are thus ambiguous. To indicate this I match the broken line running from our Interest Rate Gradient box to Supply and to Demand with a positive unbroken line in each case. In this our model, reflecting reality, discloses a broad degree of indetermination. Which of the opposed influences will prevail will be decided by many factors contributing to create a prevailing comportment of the economic groups involved.

Returning to the lowest level, Social Revalorization bringing higher wages to certain groups of workers, may trigger "counter-revalorization" among other groups. Teachers, for example, may take to comparing their pay with that of garbage collectors, and that might lead to higher salaries for them as well. I show this by a box in the positive price circuit: "Counter-adjustments to Social Revalorization." If such salaries are paid by the government, this will feed back positively to the lowest level and swell the Social Lien.

The entire positive price circuit of the middle level will feed back into the Social Lien on the lowest level – the counter-shift effect. On the positive price circuit there is a box: "Mistaken Deflationary Stabilization Policy." This can lead to higher prices by adding to unit costs through more unused capacity (Harrod Effect), and by adding to the Social Lien through the greater call for social services and narrowing the tax base. A positive feedback thus runs from this box to the Social Lien on the lowest level. However, because such Deflationary Stabilization Policy may also dampen Demand, there is a broken line leading from this box to Demand (and another to Supply) at the top level.

A positive feedback from "Mistaken Deflationary Policy" also goes to Social Revalorization on the lowest level: the social unrest likely to result from unemployment is bound to heighten political pressures from underprivileged groups.

It is impossible to predict which of these contrary influences of 'Mistaken Deflationary Policy' will prevail. But in view of the strong unidirectional field set up by the Valier Complex, as well as by the numerous positive feedbacks to the non-market zone, the deflationary policy would have to bring on quite catastrophic liquidation for a negative resultant effect on price to assert itself. Even so, this would not eliminate the accelerated increase of the Social Lien and the Social Revalorizations on price; it would merely eclipse their effects temporarily.

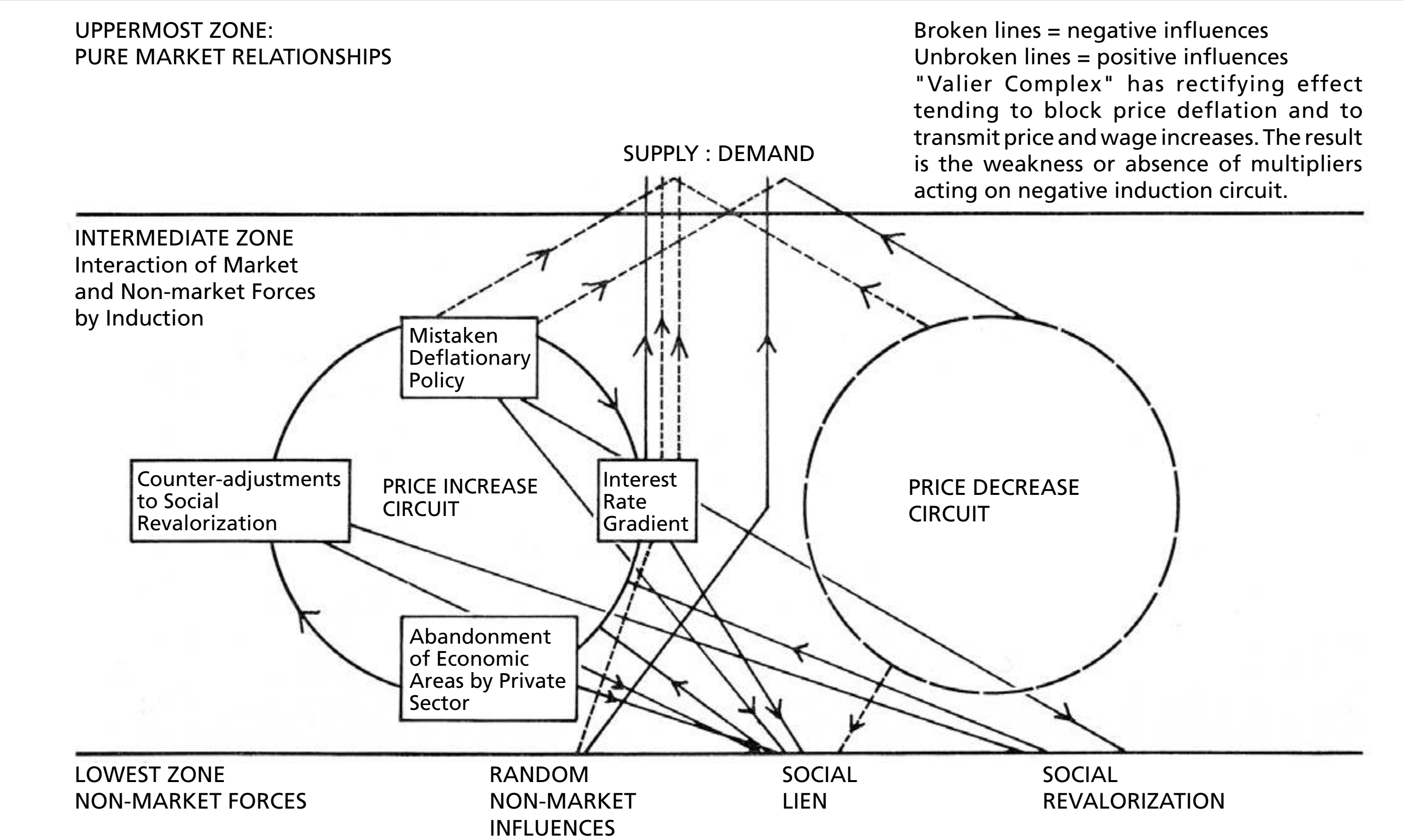
I could go on adding feedback lines to the graph, but that would only create a forbidding complexity. The highly dishevelled appearance that it has already attained makes one thing very clear: there is a high degree of indeterminacy in price levels in our mixed economy. The responses in most areas are of an ambiguous nature because of the induction effects in our middle zone. This confutes the simplistic notion that prices today are determined primarily by the balance of supply and demand.

William Krehm

1. Valier, Jacques (1968). *L'inflation rampante dans les pays de capitalisme evolue.* Paris: Cujas.

2. Valier, pp. 13 and 17.

3. Valier, p. 33.



Reducing the Human Mind to an Organ for Evasion

The Globe and Mail (12/01, "Getting a handle on happiness" by Bill Cherry) takes us for a bumpy ride: "As Canada's gross domestic product numbers start to face, Finance Minister Jim Flaherty could easily – and legitimately – boast that Canadians are at least the happiest in the G7.

"But Canada has shown little interest in such measures, even as other G7 nations jump on board a global movement to think seriously about being happy.

"Acknowledging that critics find the idea a bit 'wooly' and 'airy-fairy,' British Prime Minister David Cameron last week announced his government's new measurement on measuring happiness, saying it will show that Britain's future success is about more than economic growth.

"In Ottawa this week, a group of experts – including a director of the UK Office for National Statistics – are debating whether Canada should think happy thoughts.

"One idea under discussion arises from a recent analysis by the Centre for the Study of Living Standards, which is co-hosting this week's conference, concluding that a rise in income can have less impact on happiness than improved mental health and community attachment.

"Mel Cappe uses the example of garbage. The former Clerk of the Privy Council notes that a country that produces a lot stuff – including garbage – could be praised for having a high GDP.

"Yet that measure fails to take into account the citizenry's unhappiness with all the garbage.

"That's why Mr. Cappe, who now heads the Institute for Research on Public policy and is a panelist at Wednesday's debate, supports the idea of complementing GDP numbers with a measure of happiness. The idea still needs a lot of work, he said, but the British government's endorsement adds momentum.

"'The fact that Cameron said what he said is really a sea change,' Mr. Cappe said."

The Skepticism

"Former TD Bank chief economist Don Drummond, another member of the panel, plans to throw a bit of cold water on what he labels the 'happiness movement.'

"He disputes the underlying assumption that governments are blindly pursuing hikes to the GDP as the be all and end all of success.

"Ultimately, he said, politics depends on happy voters, and politicians are always polling and looking for ways to make voters happy. He also points out that there are limits to what governments can spare on health care and other social programs before the lack of public funds creates its own unhappiness.

"'I'm still a little quizzical,' he said.

"The mix of national approaches to measuring happiness hasn't stopped others from producing global rankings. The London-based New Economic Foundation publishes a Happy Planet Index.

"Canada ranks fifth for life satisfaction, trailing only Costa Rica, Denmark, Norway and Ireland.

"The kingdom of Bhutan in the Himalayan mountains was among the first to take such measurements seriously. A 2008 survey found 97 percent of its citizens were happy. French President Nicolas Sarkozy adopted a happiness-based program last year after commissioning the advice of two Nobel economists, calling it a 'great revolution.'

"The rich, writes Joe Friesen, really are getting richer, and that may not make for a happy society.

"The super rich are, in one respect, not that different from ordinary Canadians: they work for their money. It's just that they're rewarded at a rate most people dream of.

"The top 0.01 percent of Canadian income earners, the 2,400 people who earn at least $185 million, aren't just basking in investment income and business profits. Nearly 75 percent of their income comes from wages, just like the average Canadians, according to a study from the Canadian Centre for Policy Alternatives. The top 1 percent, the 246,000 Canadians who earn more than $169,000, receive about 67 percent of their income as wages.

"That's a change from the 1940s, when the rich took 45 percent of their income from wages, 25 percent from business profits and the rest from investments, dividends and interest. 'Those at the top actually work more for their money than any generation of the rich going back to the 1920s,' said economist Armine Yalnizian, the study's author.

"Ms. Yalnizian said the major trend she identifies is that the wealthiest Canadians are increasing their share of income at a historic pace, with income concentrated in a way that hasn't been seen since the 1920s. In the past decade, almost a third of income growth, has gone to the richest 1 percent, she added.

"The big picture shows that after the Second World War, Canadian society distributed income in an increasingly level fashion. From 1946 to 1977, she writes, the income share of the richest 1 percent fell from 14 percent to 7.7 percent. That trend was reversed over the past 30 years, as the top 1 percent regained its 14-percent share of Canadian income. Over that time, the richest 0.1 percent almost tripled their income share and the richest 0.01 percent increased their share fivefold.

"Median incomes, meanwhile, have been stagnant, according to Ms. Yalnizian. 'You've always had these people who've got their fingers on something the rest of us don't. But why are they suddenly worth many multiples of what they were back then?' Ms. Yalnizian said.

"'The answer,' she said, 'is not economics. It's in our culture. As a society, we sanction it, by and large, for better and for worse.'

"Economist Michael Veall, who teaches at McMaster University, said a few theories try to explain the income shift. One view is that corporate governors have allowed CEO salaries to jump because they were climbing elsewhere. Another is that CEOs, known for being superb communicators, are more effective, and thus more valuable, in the digital age because e-mail and the mass media facilitate contact with employees and the public.

"Ms. Yalnizian said in the long run the trend towards income concentration seems, in her view, politically and economically unsustainable.

"'You can't growing an underclass that plays by all the rules, gets a better education, works more and doesn't get ahead,' she said."

That certainly disposes of some of the official evasions, but hardly gets us to the

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Celebrated News Sources of a Unified World are Now being Blocked as a Technique of Espionage

The Wall Street Journal (8-9/01, "A Walled Wide Web for Nervous Autocrats" by Evgeny Morozov) reports: "At the end of 2010, the 'open-source' software movement whose activists tend to be fringe academics and ponytailed computer geeks, found an unusual ally: the Russian government. Vladimir Putin signed a 20-page executive order requiring all institutions in Russia to replace proprietary software, developed by companies like Microsoft and Adobe, with free open-source alternatives by 2015.

"The move will save billions of licensing fees, but Mr. Putin's motives are not strictly economic. In all likelihood, his real fear is that Russia's growing dependence on proprietary software, especially programs sold by foreign vendors, has immense implications for the country's national security. Free open-source software, by its nature, is unlikely to feature secret back doors that lead directly to Langley, VA.

"Nor is Russia alone in its distrust of commercial software from abroad. Just two weeks after Mr. Putin's executive order, Iran's minister of information technology, citing security concerns, announced plans for a national open-source operating system, China has also expressed a growing interest. When state-owned China Mobile recently joined the Linux Foundation, the non-profit entity behind the most famous open-source project, one of the company's executives announced – ominously to the ears of some – that the company 'was looking forward to contributing to Linus on a global scale.'

"Information technology has been rightly celebrated for flattening traditional boundaries and borders, but there can be no doubt that its future will be decisively shaped by geopolitics. Over the past few years, policymakers around the world have had constant reminders of their growing dependence on – and vulnerability to – the new technology: the uncovering of the mysterious China-based GhostNet network, which spied on diplomatic missions around the globe; the purported crippling of Iran's nuclear capability by the Stuxnet virus; and, of course, the whole WikiLeaks affair. Governments are taking a closer look at who is providing their hardware, software and services – and they are increasingly deciding that it is dangerous not to develop independent national capabilities of their own.

"Open-source software can allay some of these security concerns. Though such systems are more democratic than closed ones, they are also easier to manipulate, especially for governments with vast resources at their command. But open-sources solutions can't deal with every perceived threat. As Google learned, the Chinese government continues to see Western search engines as a challenge to its carefully managed presentation of controversial subjects. Similarly, email can be read by the host government of the company offering the service, and the transmission of sensitive data can be intercepted via secret back doors and sent to WikiLeaks or its numerous local equivalents.

"For these reasons, more governments are likely to start designing internet services as a strategic industry, with foreign firms precluded from competing in politically strategic niches. The Turkish government has emerged as the leading proponent of such 'information independence,' floating the idea of both a national search engine and a national email system. China and Iran have debated similar proposals.

"Judging by last year's standoff between the Blackberry maker Research in Motion and the governments of India, Saudi Arabia and the United Arab Emirates, questions of access also will play a growing role in shaping technology. If a government suspects that the US National Security Agency has arranged to be able to retrieve private emails sent with Blackberrys secure encryption technology, it starts to wonder why it doesn't have similar streams of intelligence data from services like Gmail and Skype. As a minimum, more governments will demand that data servers base their operations in their own jurisdictions, inconveniencing global internet companies that have based their business plans on the assumption that they could run their Indian operations from Iowa.

"The real Internet trade wars will begin once Russian and Chinese technology giants, with their poorly veiled government connections and piles of cash, come looking for American and European acquisitions. How will officials in Washington and European react when China's Tencent 25 (with a market capitalization of $42 billion, almost twice that of Yahoo) makes a bid for AOL or Skype?

"Painful decisions will need to be made soon. The Russian company Digital Sky Technologies, owned by a Kremlin-friendly oligarch, has a nearly 10% stake in Facebook and 5% stakes in such hot Web properties as Zynga and Groupon. What will happen once Russian or Chinese firms seek to purchase a stake in companies like Google (a contractor to the National Geospatial Intelligence Agency) or Amazon, which caters to nearly 20 US government agencies through its Web hosting services? The unpleasant effects of this rising nationalism are already evident in the case of hardware exports. When Sprint Nextel began considering bids from China's Huawei and ZTE Technologies in 2010 for a projected $5 billion upgrade of its network, a group of American senators wrote to the company's chief executive expressing their concern that Huawei might be subject to 'significant influence by the Chinese military' and that communications in the US could be 'disrupted, interrupted, tampered with, or purposely misrouted.' Sprint Nestel turned down the bids. The European Union recently announced plans to create an authority similar to the US Committee on Foreign Investment to specifically vet approaches from China's technology giants.

"Even if they are spurned by the US and Europe, China's tech giants are likely to resurface elsewhere. For several years China has been using its huge cash reserves to hand out loans – mostly to governments in Africa, but also to neighbors like Cambodia – with the condition that those governments only do business with China's telecom companies. With or without secret access to that data, the fact that China controls so much of the communications infrastructure in the developing world gives it political leverage.

"At the same time, Yota, a partly state-owned Russian telecom provider, has been trying to build a base in Latin America, launching its 4G service in Nicaragua and soon, in Peru. Other Russian companies are busy building (or buying up) the telecom infrastructure in the former Soviet republics, perhaps in a bid to do for the internet what Russia's gas giant Gazprom has done for energy: build up physical infrastructure and then use it as a tool of political leverage.

"What does all this mean for the future of America's technological industry? If China's expansion into Africa and Russia's into Latin America and the former Soviet Union are any indication, Silicon Valley's ability to expand globally will be severely limited, if only because Beijing and Moscow have no qualms about blending politics and business. The global triumph of American technology has been predicated on the implicit separation between the business interests of Silicon Valley and the political interests of Washington.

"In the past, foreign governments have rushed to install the latest version of Microsoft Office or Google's Chrome browser because it was hard to imagine that Washington would tinker with technology to advance its strategic interests.

"But just a few weeks before Mr. Putin publicly endorsed open-source software, FBI Director Robert Mueller toured Silicon Valley's leading companies to ask their CEOs to build back doors into their software, making it easier for American law enforcement and intelligence gathering agencies to eavesdrop on online conversations. The possibility of such arrangements to force foreign governments to reconsider their dependence on American technology. Whatever the outcome of Washington's engagement with the Internet, Silicon Valley will be the one to bear the costs.

"For ordinary users, there is one silver lining. The embrace of open-source technology by governments may result in more intuitive software applications, written by a more diverse set of developers. The possible downside is that the era of globally oriented services like Skype may soon come to an end, as they are replaced by almost certainly less use-friendly domestic alternatives that would provide secret back-door access. As governments seek to assert control, companies will be providing fewer and fewer guarantees about both data security and access by third parties – such as governments.

"The irony in these developments is hard to miss. Information technology has been one of the leading drivers of globalization, and may now be in the process may become one of its major victims."

The globalized control of how the world reckons its balance sheet had come to be controlled largely by US influence when it ruled out the recognition of human capital investment which is not marketed and had been identified as the prepaid investment as the best investment a government can make. And that was eliminated by the determination of the US speculative banks and the government that they came to control, and imposed on the world as a whole. Now that same government is seen as imposing a powerful back-door official Washington propaganda, function that if accepted would prevent incipient countries to be fed Washington's interest rather than valid analysis of where the world economy might be headed. By its own doing, Washington is undermining its control of economic thinking in the rest of the world. That would give the Good Lord above the clouds to regain a say as to where the real interests of the rest of the world may lie.

William Krehm

Lost in the Brambles of Greed

The New York Times (16/01, "In the Health Care Fight, a Political Focus on Jobs, with No Simple Answers" by Robert Pear) presents the extent of the coherence that has taken over official thought. We quote: "Washington – As Republicans choreograph a House vote to repeal President Obama's health care overhaul this week, no charge has stung Democrats more than the argument that the new law will 'kill' jobs in an economy wobbling back to life.

"In the fight over whether the law will create or destroy jobs, both political parties cite evidence to support their claims. But many economists say the effect on jobs is likely to be modest – neither so negative as the Republicans assert nor so positive as Democrats contend.

"In any event, economists say the impact on jobs – a hot political issue now – is not a particularly good standard to use in evaluating a complex law that will affect one-sixth of the economy and almost every American. For many experts, a more significant test is whether the law will slow the growth of health costs and provide greater value to consumers, taxpayers and employers in return for the $2.5 trillion a year they spend on health care.

"'The effect of the law on jobs is likely to be modest,' said Katherine Baicker, an economic adviser to President George W. Bush who is now a professor of health economics at Harvard. 'The most important effects of the law will be on health costs and coverage and the efficiency of the health care system, not on jobs.'

"Economists tend to agree that the law could lead some employers to hire fewer low-wage workers, as the nonpartisan Congressional Budget Office has said. But, they add, if the law eventually slows the growth of health costs, it could leave the employers with more money to spend on expanding their business and even on hiring.

"Health care jobs have been growing for years, and many experts say the trend is likely to continue if, as the budget office has projected, more than 30 million people gain coverage.

"Republicans say the law will discourage hiring and employment; it will impose additional payroll costs and taxes on many businesses.

"The shaky economy and the health care law, passed on party-line votes in both houses of Congress, are separate political issues. But they could become a combustible mix in the 2012 presidential campaign if unemployment remains high and Republicans gain traction with their argument that the health care law is adding to the problem.

"White House officials, aware of the political risks, portray the law as an engine of economic growth that could create more than 300,000 jobs by reining in the cost of employees health benefits.

"Starting in 2014, employers with 50 or more employees will be required to pay penalties if they do not offer insurance – or if their coverage does not measure up to federal standards – and if at least one worker gets a federal subsidy to help buy insurance. Companies that provide skimpy health benefits or none at all could thus incur substantial costs.

"At least one fourth of workers are in small businesses that will be exempt from the penalties, the Congressional Research Service says, and the desire to keep that exemption could influence the behavior of some business owners.

"Tony Gagliardi, director of the Denver office of the National Federation of Independent Business, said many proprietors had told him: 'If I have 49 employees, I'm not going to hire the 50th one. The government has removed the incentive for me to create jobs over that threshold.' (Whether the threshold is at 50 or 51 employees is not entirely certain. 'There is an inconsistency in the law' that may need fixing, the Congressional Research Service has said.)

"The law's defenders say several factors will limit its impact on jobs. Employers will have several years to adjust many of its incentives and requirements. Most large companies already provide health benefits to employees. And many small employers can obtain tax credits to help delay insurance costs for several years.

"Economists say the new costs – including those for new health benefits and benefits – will, over time, generally be passed on to workers, through reductions in wages or other compensation.

"'However,' the Congressional Budget Office says, 'firms generally cannot reduce workers' wages below the minimum wage,' now $7.25 an hour, and this 'will probably cause some employers to respond by hiring fewer low-wage workers.'

"Alternatively, the budget office said, the law may create incentives for some employers to use more part-time workers, because they will not be counted in calculating the amount of penalties.

"Representative Vicky Hartzler of Missouri, a freshman Republican who ousted a 17-term Democrat, said small businesses in her district were 'not hiring and not expanding because of the health care law.

"But Gary Burtless, a labor economist at the Brookings Institute, said he was 'skeptical of the idea that the new law will be a wholesale job-killer.'

"'If it appears that there will be a lot of extra costs for providing health insurance to your least skilled employees, Mr. Burtless said, 'my hunch is that employers will find some route, direct or indirect, to avoid paying those costs,' Mr. Burtless said.

"The law's impact on jobs, depends in part whether it will slow the growth of health costs, a question on which expert opinion is divided.

"'If the growth of health costs is reduced, employers could use the savings to generate a significant number of jobs,' said Frank B. McArdie, manager of the Washington office of Aon Hewitt, a benefits consulting firm. 'If costs go up because of health care reform, employers will have to hire or keep a smaller number of employees, or change the mix of full-time and part-time workers.'

"'The jury is still out,' on provisions of the law intended to squeeze health costs, Mr. McArdie added.

"When Massachusetts required people to carry health insurance, it saw an increase in coverage and in the demand for medical care, especially primary care. Administration official expect a similar response to the federal law.

"The increase in health care jobs has long seemed unstoppable, even when the overall employment picture is bleak. From the start of the depression in December 2007 until December, 2010, the nation as a whole lost 7.2 million jobs, but the health care industry gained 800,000, according to the Federal Bureau of Labor Statistics."

However, what ails the world economy is something far more basic, so much so that disregarding it is putting the human race at serious risk. No sooner had Japan and Germany surrendered, than Washington sent hundreds of economists to those defeated Axis leaders to study the war-time damage and from it forecast how soon it would be before those once great traders could resume such roles. Some sixteen years later one of these economists, Theodore Schultz of the University of Chicago wrote an essay stating why he and his colleagues had been so wrong. The main reason for their bad forecasts, he concluded, was their having concentrated on the physical destruction, while little importance had been given to the fact that the gifted, highly trained human resources had come through the war relatively intact.

And then in a stroke of genius, he concluded that human capital today, is by far the most important investment a country can make. For a few years Schultz was celebrated, decorated, for his great discovery, and then plunged into oblivion. I fear that COMER alone even remembers his great conclusion which would have prevented and even now could solve the deepening world crisis. For what is involved is the most elementary accountancy. If you disregard for our ever-more-populous cities adequate infrastructure is not an expenditure, but investment – the most productive investment that a government can make, and entirely prepaid, the present world crisis would not exist.

Note well, the children of educated parents tend to be more easily educated, healthier. Note, too, that there are any number of countries like Brazil and much of Africa, with immense still unexploited mineral wealth, but without the human capital to exploit it adequately.

No need then for the endless mini-calculations that remind one of putting together a patchwork quilt, when what we must do is to reinvest to the best effect the human capital which is here prepaid in abundance. As it is we are flying mean and blind.

Years ago I approached essentially the same problem in terms of elementary logic applied to the very current concept of inflation. If I put a loaded pistol to my head and press the trigger, I fall dead. But propositions are not reversible. If I fall dead, it cannot be assumed that I have suicided. It could have been heart-failure. Nevertheless, this most elementary rule of logic is ignored and any rise in the price level is called 'inflation' and treated with higher interest rates. And in our universities, with a few honorable exceptions, those members who question this logical illiteracy, risk dismissal.

In the 1960s I devoted myself to an analysis of the very different possible reasons for rises in the price level. It might be a lack of supply to satisfy demand, and that is real inflation. But it could be something quite different which I chose to call the *social lien.* That refers to the rapidly increasing portion of the national and international output that is satisfied by direct investments of governments. This would include such items as human capital in health, education, and social welfare, adequate infrastructure at all levels of government.

That was published in the leading French economic journal of the day *Revue économique* (May, 1970), and was reviewed twice favorably by the economic journal of Cambridge University and some other eight prestigious economic journals.

I have tested this in the housing and stock markets and its verification made possible the financing of much of COMER's publications and activities.

On the editorial board of *Revue économique* was the leading French social historian and two statisticians who had tried verifying the prices rise as a result of scarcity of available supply over demand and found that there was no such relationship in fact. At that point the postman delivered my essay that analyzed the phenomenon from many different angles. A review of that review in a Toronto paper resulted an invitation from John Hotson of Waterloo University to come and explain my thesis, and led to the foundation of COMER.

That essay led to collaboration to our mutual advantage with extraordinary economists like François Perroux. He was most helpful with insights such as his "dominant revenue" that notes that those in the political saddle identify the well-being of their group as an adequate index of the welfare of society as a whole. The lesson from that is do not leave in the saddle, anyone whose interests are those of the social class overthrown. A lesson the President Obama could have found helpful as a warning against allowing Mr. Geithner associated both with the New York banks and the Washington Treasury as mentor of his supposedly new regime.

W. Krehm

Hocus-Pocus at the Law Schools

The New York Times (9/01, "Is Law School a Losing Game?" by David Segal) reports: "If there is ever a class in how to remain calm while trapped beneath $250.000 in loans, Michael Wallerstein ought to teach it.

"Here he is sitting one-afternoon at a restaurant on the Upper East Side of Manhattan, a tall, sandy-haired 27-year-old – a kind of surfer-dude serenity. His secret, if that's the right word, is to pretty much ignore all the calls and letters that he receives every day from the dozen or so creditors now hounding him for cash.

"'And I don't open the e-mail alerts with my credit score,' he adds. 'I can't look at my credit-score any more.'

"Mr. Wallerstein, who can't afford to pay down interest and thus watches the outstanding loan balance grow, is in roughly the same financial hell as people who bought more home than they could afford during the real estate boom. But creditors can't foreclose on him because he didn't spend the money on a house.

"He spent it on a law degree. And from every angle, this looks like a catastrophic investment. Well, every angle except one, the view from law schools. To judge from data that law schools collect, and which is published in the closely parsed *US News and World Report* annual rankings, the prospects of young doctors of jurisprudence are downright rosy.

"In reality, and based on every other source of information, Mr. Wallerstein and a generation of JDs face the grimmest job market in decades. Since 2008, some 15,000 attorney and legal-staff jobs at large firms have vanished, according to a Northwestern Law study. Associates have been laid off, partners nudged out the door and recruitment programs have been scaled back or eliminated.

"And with corporations scrutinizing their legal expenses as never before, more entry-level legal work is now outsourced to contract temporary employees, both in the US and in countries like India. It's common to hear lawyers fret about the sort of tectonic shift that crushed the domestic steel industry decades ago.

"But improbably enough, law schools have concluded that life for newly-minted grads is getting sweeter, at least by one crucial measure. In 1997, when *US News* first published a statistic called 'graduates known to be employed nine month after graduation' reported an average employment rate of 84%. In the most recent *US News* ratings 93 percent of grades were working – nearly a ten-point jump.

"In the Wonderland of these statistics, a remarkable number of law school grades are not just busy – they are raking it in. Many schools, even those that have failed to break into the *US News* top 40, state that the media starting salary of graduates in the private sector is $160,000. That seems highly unlikely, given that Harvard and Yale, at the top of the pile list the exact same figure.

"How do law schools depict a feast amid so much famine?

"'Enron-type accounting standards have become the norm,' says William Henderson of Indiana University, one of many exasperated law professors who are asking the American Bar Association to overhaul the way in which law schools assess themselves. 'Every time I look at this data, I feel dirty.'

"It is an open secret, Professor Henderson and other say, that schools finesse survey information in dozens of ways. And the surveys guidelines, which are established not by *US News* but by the American Bar Association for Law Emplacement, all but invite trimming.

"A law grad, for instance, counts as 'employed after nine months,' if he or she has a job that doesn't require a law degree. Waiting tables at Applebee's. You're employed. Stocking aisles at Home Depot, you're working, too.

"Number-fudging games are endemic, professors and deans say, because the fortunes of law schools rise and fall on rankings, with reputations and huge sums of money hanging in the balance.

"They are also cash cows.

"Tuition at even mediocre law schools can cost up to $43,000 a year…. There are no labs or expensive equipment to maintain. So much money flows into law schools that law professors are among the highest paid in academia, and law schools that are part of universities often subsidize the money-losing fields of higher education….

"There were fewer complaints about fudging and subsidizing when legal jobs were plentiful. But student loans have always been the financial equivalent of chronic illnesses because there is no legal way to shake them. So the glut of diplomas, the dearth of jobs and those candy-coated employment statistics have now yielded a crop of furious young lawyers who say they mortgaged their future under false pretences….

"'Avoid this overpriced sewer pit as if your life depended on it,' writes the anonymous author of the blog Third Tier Reality – a reference to the second-to-bottom tier of the US News rankings – in a typically scatological review. 'Unless, of course, you think that you will be better off with $110k-$190k in *non-dischargeable* debt for a degree that qualifies you to wait tables at the Battery Park Bar and Lounge.'

"But so far, the warnings have been unheeded. Job openings for lawyers have plunged, but law schools are not dialing back enrolment. About 43,000 JDs were handed out in 2009, 11 percent more than a decade earlier, and the number of law schools keeps rising – nine new ones in the last ten years, and five more seeking approval to open in the future.

"Apparently, there is no shortage of 22-year-olds who think that law school is the perfect place to wait out a lousy economy and the gasoline that fuels this system – federally backed student loans – is still widely available. But the legal market has always been obsessed with academic credentials, and today, few student except those with strong grade-point averages at top national and regional schools can expect a come-hither from a deep-pocketed firm. Nearly everyone else is in for a struggle. Which is why many law school professors privately are appalled by what they describe as a huge and continuing transfer of wealth, from students short on cash to richly salaried academics….

"'I think the student loans that kids leave law school with are more scandalous than payday loans,' says Andrew Morris, a law professor at the University of Alabama….

"Like everything else about the law, however, the full picture here is complicated. Independent surveys find that most law students would enroll even if they knew that only a tiny number of them would wind up with six-figure salaries. Nearly all of them, it seems, are convinced that they're going to win the ring toss at this carnival and bring home the stuffed bear.

"True, say Professor Henderson and his allies. But he contends that law schools – which, let's not forget, require students to take courses on disclosure and ethics – have a special moral obligation to tell the truth about themselves. 'What we have here is powder keg, and if law schools don't solve this problem, there will be a day when the Federal Trade Commission, or some plaintiff's lawyer, shows up and says, "This looks like illegal deception."'"

Seen from an even higher vantage point, the real dilemma is still more appalling: if you start out by ignoring the most important lesson that came out of World War II – when Washington lost not a moment in sending many hundreds economists into defeated Japan and Germany to study the extent of the destruction and predict how long it would take for those once great trading nations to resume such roles again. Some sixteen years later one of these, Theodore Schultz published an essay in which he explained why he and his colleagues had come up with quite the wrong answer. It was because we had concentrated on the physical destruction and paid little heed to the detail that the human capital – the highly educated, talented, and dedicated human resources had come through the war relatively intact.

And then in a stroke of genius, he reached the conclusion that human capital, which must include not only the ever higher education of the human resources, health, but also proper care of the environment, and adequate infrastructure for the immense urbanization underway. Were this done, there would be no deficits. Great Britain is still deriving ever greater returns from whatever Stratford-upon-Avon may have spent on one Billy Shakespeare, or what Lincolnshire laid out for the education of Isaac Newton.

Though Ted Schultz was celebrated and even decorated, he and his great discovery were soon buried in an unmarked grave, as speculative banking took over. The lessons of the Great Depression were similarly treated.

Such human capital is not a debt, but a social asset. If it is treated as a debt, we simply lack anything that could mistaken for accountancy in the dark. The final great desperate gamble is atomic war, for which the weaponry is proceeding well-enough funded.

William Krehm

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crucial point.

That is so risky to even allude to, that the mere mention of it can endanger of the livelihood of an economist from employment in most of our universities today.

What has not been forgotten but buried are the crucial lessons learned both from the Great Depression of the 1930s and from the Second World War. By the time President F.D. Roosevelt had been inaugurated 38% of the banks in the US had already shut their doors, and one of the new President's acts was to proclaim a bank moratorium that lasted a month. During that time the new President with scant economic learning behind him, consulted just about anybody with an idea of what must be done. From this emerged the restrictions on banking embodies in *Glass-Steagall* finally adopted as law in mid-1935. This barred banks from acquiring interests in the non-banking financial platforms, which at the time consisted essentially of brokerages, insurance, and mortgage companies.

The reason for the restriction is that once the banks acquired control of these, they would use the financial reserves needed for their own businesses to pursue their own speculations, and what would result is an ever riskier skyscraper of speculation with elevators that could only go upward at ever greater speed – never, ever downward, for the whole contrivance not to collapse. A further safeguard was the statutory reserve that required the banks to deposit a portion of their earnings with the central bank on which they earned no interest. Since this reduced the amount of liquid assets banks could gamble with, it provided an alternative to higher interest rates in cooling off a speculative boom. That was increasingly ignored during the 1980s and formally done away with in 1993.

However, the most radical rethinking of economic theory that we are missing today resulted from an initiative of the US government. No sooner was the armistice signed with Japan and Germany than Washington sent hundreds upon hundreds of economists to those two once great trading powers to study the destruction and from it predict how long it would take before they could once again resume such roles. Some sixteen years later one of these, Theodore Schultz of the University of Chicago, published a paper showing how wide of the mark their predictions – including his own, had been. This he attributed to their having concentrated on the physical destruction, and paid little heed to the detail that the human resources had come out of the war virtually intact.

And then in a stroke of sheer genius, he concluded that investment in human capital best investment a government can make. Included in that of course, were not only education, but health, proper care of the environment and adequate infrastructures for the ever rapid urbanization that is under way. Such human capital came prepaid and is not to be confused with debt and spending. The children of educated, healthy parents tend to be healthier and more readily educated.

That, however, collided head on with the budget balancing by slashing educational, health and budgets for preserving the environment.

Surely it is enough to note the plight of countries like Brazil and almost every African state, that almost invariably have vast national resources, but lack the human capital to develop them.

The leading French economic publication of the day *Revue économique* in its May 1970 issue, published a 41-page essay of mine arguing the logical propositions cannot blindly be turned around and assumed valid. If I shoot myself in the head, I fall dead. From that I cannot assume that if someone drops dead he has suicided. It could have been a heart failure. Nevertheless rising prices are today assumed by economists to be deflation.

My paper pointed it could result from mistaken prepaid human capital investment – proven by Ted Schultz to be the most productive investment a government can make is throughout the world not distinguished from "inflation." This warrants the banks being bailed out by governments from their speculative disasters at the expense of the very human capital, proven to be the best investment a government can make. Expenditures for education, health, the environment, adequate infrastructures for many million-headed municipalities.

The price effects of such human capital investments I termed the "social lien" that was singled out for a good choice of title by the two favorable reviews in the economic publication of Cambridge University in Britain are treated as indulgences rather than as the key investments that they are.

Despite that our ever more tightly globalized world goes on being driven by pseudo-mathematics that were rejected by the Babylonians 4,000 years ago.

As a result world is being run and squeezed with nothing that could be identified with accountancy even with lights out.

Bill Krehm