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## **FREEDOM 2010**

### **The Good Guys Get to Win**

I don't know what it is like in your neighborhood, but Vancouver, where I live, is plagued by a number of critters. There are urban bears, urban coyotes, urban raccoons, urban skunks and urban socialists. Of course, the latter have done the most harm.

Under various compelling arguments the state has imposed its authority in a manner unseen in four hundred years. Since the early 1900s the main pitch has been that economic central planning has been needed for the public good. Eastern Europe got Marx. The Western World got Keynes. However, as marked by the fall of the Berlin Wall in 1989, folks who had suffered from too much central planning began throw it off. Political reform swept the world and in the 1990s many hard-line socialists slipped into the environmental movement. Within this, man-caused global warming has been a powerful ploy in imposing authority and in academe – harvesting grant money.

Any impartial review of history would conclude that the notion that an economy is national and can be managed by manipulating interest rates has been some form of madness. More specifically, financial history itself is a "due diligence" on every wild scheme ever floated – that's in the markets as well as by financial adventurers in public policy.

Modern markets and central banking developed in the late 1600s. There has been only one financial history and the basic pattern has been a long expansion, a speculative asset inflation culminating in a blow-off. This has been followed by a long contraction. Then it repeats.

I gave a paper in May called "*Great Depressions Are So Methodical*". It reviewed that the action in the curve and credit spreads has been the same on the way up each mania, the same on the transition from boom to the initial panic, and then the same on the lengthy contraction. In a yet to be published paper I've shown that governments essentially do the same things during the boom, which has been swanning around taking credit for the apparent prosperity. Then they take measures to prevent the initial crisis, and then turn to scapegoats and protectionism.

The concept of throwing credit at a credit contraction and hoping it will go away has been floated on every severe crisis since the 1618 crash. The esteemed Walter Bagehot argued it elegantly when he was editor of *The Economist* in 1873. That year's collapse of a great bubble marked the beginning of long contraction that in 1884 prompted the first usage of the term "Great Depression". The long-running contrast between academics and the markets has been one of the best generators of irony in history. The contraction lasted from 1873 to 1895, but as late as 1939, top economists such as Rostow, were still analyzing it as the "Great Depression".

Recently, leading experts have declared that certain manipulations have prevented "Great Depression 2.0" from happening. From their own literature such economists should know that it would be the third one. History counts that the one that started in 1929 was number five in the series.

It is worth emphasizing that the Fed was given the unique privilege of a "flexible" currency in order to prevent bad things from happening. Of course, the 1929 Crash was impossible so an even better agency was needed.

Two important acts were passed that were designed to prevent another run-a-way bubble.

One of the promoter-politicians boasted that the SEC would put a "*cop at the corner of Wall and Broad Streets*". The SEC did not prevent another bubble and it did not shut down the biggest Ponzi Scheme when advised of it some years before Madoff failed.

Glass-Steagall was taken off the books to belatedly bless the existing move by commercial banks into Wall Street. But then at the culmination of a financial mania it has been essential to have all institutions involved, which is another example of policymakers repeating their own history. As Lord Overstone observed "*No warning can save a people determined to suddenly grow rich*".

It seems that the combination of the late great boom and its visions of Goldilocks has been accompanied by the equivalent bubble in authoritarian politics. Both are vulnerable to powerful post-bubble forces. For example, the rallying cry of the American Revolution was about taxes and the heavy hand of government. The preceding long expansion and concluding bubble blew out in 1772. Similar revulsion for the authoritarian White House is developing. As this contraction continues Democrat bullies will become even more isolated from the electorate.

Researchers should not dwell on the notion that throwing credit around is a good thing, or explaining why it wasn't successful in 1929, or boasting that this time it has worked. Before building any theory on financial markets it is essential to review just how a mania turns to bust.

Typically, the boom runs some 12 to 16 months against an inverted yield curve. What's more, rising interest rates is an indicator that the boom is on. The worry should begin when short-dated rates, such as treasury bills, start to decline. Short rates fall through most of the initial liquidity crisis. For example, the key administered rate declined from 6% in 1929 to 1.5% in 1930, or 450 basis points. Much later, scholars insisted that the Fed wasn't aggressive enough in cutting rates. In the post-1873 bust the Bank of England dropped the rate from 9% to 2.5% and 650 bps was not enough to prevent that Great Depression. Just like their concepts on credit – the notion that lowering interest rates will re-ignite a boom is right out of thin air.

If they had cut them to zero would it have made any difference? It's doubtful because high interest rates accompany a boom and low ones accompany contractions. Throughout its history the senior central bank has followed the big changes in market rates of interest.

On our market debacle, the curve was expected to reverse to steepening by June 2007, which was the critical sixteenth month. It reversed in that fateful May, and as the saying goes – the rest is history. This proved again that the Fed has virtually no influence on the curve or on spreads and these have been some of the best indicators of a developing contraction.

Credit deteriorated for some time before it triggered last fall's classic crash. After a bounce, the crash extended into March when a natural rebound began.

After the panic, the rebound could run for some five to six months and September was the sixth month. On the equivalent in 1930, Barron's noted that "*the urge to speculate is as speculative as ever*" and concluded that it would be difficult to "*quench the fires of enthusiasm*". On that rebound, the Dow retraced 50 percent of the loss.

This time, the Dow has recovered 44 percent of the loss and the Nasdaq 56 percent – both with wonderful enthusiasm, which is now measurable. Sentiment got to 92 Percent Bulls in September and this compares to 88 Percent Bulls at the peak of the market in October 2007.

For those who dwell in GDP-Land, that peak is very important. At normal peaks, the cycle for stock certificates leads the peak in business activity by some 12 months. For example, the Dot-Com peak was in March 2000 and the NBER determined that it officially started in March of 2001.

The only times the peaks have been coincidental has been at the climax of a great financial mania.

For those who appreciate official numbers, in 1873 the crash began in mid September and the NBER determined that the recession started that October. In 1929, as everyone knows, the crash began in mid-September and the NBER date was set as that fateful August.

This time around, the stock market high was set in the latter part of October 2007 and the NBER date was that fateful December – close enough to fit the model of the transition from a Great Bubble to a Great Depression. Within which, an important step is the establishment claiming that the worst is over. There have been a number of those in September. Going back a few generations, on September 12, 1930, then Secretary of Labor, James J. Davis, announced "*we are on the upswing*". The Harvard Economic Society made similar announcements throughout most of 1930.

Other than missing the collapse of speculation, the establishment has made a serious blunder in the worst financial storm since the 1930s. Those who should have been more logical stated that it was not another depression – because unemployment was not at 25 percent. That horrible figure wasn't reached until 1933. In 1930 when the Secretary of Labor was on the "upswing", unemployment was around 9 percent, as it is lately.

It is prudent to make logical comparisons, and the main intellectual problems with economic interventionists are essentially the same for interventionists in climate control.

The quickest one to deal with is the simple failure in logic. A primitive syllogism is the description of the popular compulsion to conclude that because two things occur at the same time, they are causally linked.

Yeah – roosters crowing in the morning cause the sun to rise.

Yeah – credit does expand with increasing business activity, but there is no causal link. And to claim that an artificial increase in credit – think stimulation – will cause an economic expansion is something only a very egotistical rooster would fall for.

Unfortunately, much the same holds in the man-caused global warming movement.

You can visualize this one. Some post-hippie Greenpeacer is tired of knocking on doors to save the whales and notices that physicists have assembled a climate history. Then still angry about "dark satanic mills" he looks at the increase in temps since the 1800s and declares that industrial progress causes global warming. Eventually real earth scientists began to notice the promotion and said "*So what – it's been warming for 12,000 years*". The promotion then became "Climate Change" and the sweep of accusation quickly included cars and – shudder – oil companies.

Beyond the primitive syllogism, the parable includes the other main blunder by ambitious central planners, which is best described by an old saying in physics: "*If you keep your data base short enough, it will fit your theory*".

This is the case in economics where interventionists consider that the Fed is the perfect policy system. To maintain the image they have to accuse those running it in 1929 of being "too tight". The old *ad hominem* attack.

Most academics, such as Bernanke can't get out of the early part of the 1900s, and they overlook the fact that the Fed was trying to reflate. In July 1932, Barron's concluded that:

***"The Federal Reserve policy of cheapening credit through the purchase of government bonds has been unable to make a dent in the conservatism of borrower or bank lender, in short, every anti-deflationary effort has yet to provide positive results. The depression is sucking more and more bonds into its vortex."***

I have found the best way to counter the debate about the blunders made by Fed personnel in the post-1929 debacle is to ask the interventionist to explain the similar transition in 1873, when the existing treasury system and fiat currency was touted as proof against anything going wrong.

Much the same holds for the five bubble transitions from 1720 to 1929, or for that matter the prototype failure that began in 1618. That one prompted an early example of some intellectual imagining that throwing credit at a contraction would make it go away. The big scheme that failed involved heavy commitment by the government and veteran merchants described the venture as a sepulcher ***"Attractive without, dead bones within."***

Policymakers threw credit at the markets in 2007 and even more aggressively in 2008 and yet a classic crash happened. This made them really aggressive through this year and we have enjoyed a classic rebound in the markets and in business activity. This has done little to change the usual sequence of transitional events.

In the last few weeks, credit markets have taken a modest step towards adversity that could be signaling caution to highly speculative stock and corporate bond markets. The employment of leverage in the carry trade is again immense and it is worth keeping in mind that the Fed has no influence upon the curve or spreads. The speculative excesses of the August and September will have to be corrected and if the decline becomes severe it will likely take business activity with it. New lows will devastate both practicing and academic interventionists. Recall that in December 2007, Gregory Mankiw boasted that government policy advisors included the ***"dream team"*** of economists. Nothing could go wrong.

It did with the most significant crash since the 1930s.

This is also the case with the intense speculation in climate change. It is changing to down, with a temperature drop of about three-quarters of the previous rise that so agitated the alarmers. An important contributor to recent high temperatures has been that the sun was at its most active in over a thousand years (Zurich Institute for Astronomy, 2004).

This, as the saying goes, is in the market, and for some years solar activity has been diminishing. On the usual 11-year period, Solar Cycle 23 was likely to bottom in late 2006 or early 2007 and it did decline to then – and kept right on going. This is now the deepest solar minimum since 1913, and to some researchers – predictable. For most alarmers, and at the risk of a pun, it has been right over their heads.

It is coincidental that the bottom fell out of the Sun at almost the same time as credit markets turned south. It is very timely.

Now we get to science at its best and conventional hysteria at its worst.

Two astronomers at Tucson, Livingstone and Penn, with data beginning in 1992, concluded that the magnetic strength and area of sunspots were "**greatly diminished**". What's more, this is on a "**linear trend independent of the solar cycle**".

Obviously serious stuff, and as it was working out, four years ago they published a draft paper on declining sunspots and immediately a couple of propagandists got on the bandwagon by claiming it would add to global warming.

When the left is on a tear – watch out – they get nasty. Despite that one of the features of science has always been skepticism, academics have lost tenure for questioning anything about the message, and meteorologists have been fired for asking the wrong questions.

Even "experts" from other disciplines, or even no discipline have used bullying for persuasion. Dr. David Suzuki is a Zoologist and Canada's equivalent to Al Gore. In whipping up a crowd in 2008, he exhorted them to "**find a legal way of throwing our leaders into jail**" because not acting upon climate change was an "**intergenerational crime**".

In June, Nobel economist Paul Krugman, condemned deniers "**I was watching a form of treason – treason against the planet.**"

One of the dangers in non-science propaganda is reliance upon authority or consensus. The UN's IPCC still insists that "**the science is settled**", as does Al Gore who will not meet with or debate anyone on the skeptical side. With cooling temps Mother Nature is winning the debate.

Indeed, attempts to stifle skepticism have been massive and remind of the Vatican's stifling of Galileo. His message was science, his nemesis was Jesuit astronomers fixed upon authority. In their case the main one was 1 Chronicles 16:30 that instructed "**The world is firmly established, it cannot be moved.**"

In following that authority, they had to contrive very elaborate models to explain motions in the solar system. As data accumulated on planetary motion Vatican astronomers were fully employed keeping their preposterous "models" up to date. They had a lot of turf to defend and Galileo threatened their status and comfort.

Real science was put on hold and this is the case now, as climate experts put global warming into their "models" and global warming comes out.

Eventually, the path of science resumed and other than Luddite riots that accompanied the start of industrialization, there has been no significant anti-science movement until today's climate control freaks.

If you don't mind I'll cover some personal points. I completed a single degree in Geophysics in 1962 and after one winter in the bush I sought indoor employment with no heavy lifting. And found it with Canada's largest bond underwriter. As a trainee I knew nothing, but did have the nerve to ask the VP of underwriting about inflation getting above 2 percent and its affect upon the coupon and principle. The answer was that inflation only occurred in lesser countries in Europe or South America. Governments in Canada and the U.S. had too much integrity to succumb to depreciation.

Pension funds were full of bonds just as the greatest bond bear market was getting underway.

Flash forward to 2008 when pension funds had become convinced that depreciation was the way of the land. They could count on sound money being banished forever and they loaded up on commodities. Pension funds were forced to abandon probity and term matching because policymaking had become corrupt, with no redemption in sight.

In the early 1960s, the subject of recurring ice ages and interglacials was strongly debated. Some lectured that an ice age needed huge amounts of precipitation in the form of snow and this required ocean circulation through an open Bering Strait. Others lectured that Milankovitch temperature periodicity based upon changes in the Earth's orbit made the most sense.

There was very little temperature history so no definite conclusions could be made. In the late 1960s data started to accumulate and has continued – it confirms periodicity. Variation in solar output of energy has long been implied by sunspots and then by satellite measure. The Sun's behaviour is periodic and is on a noticeable downtrend that is inconvenient to warming hysteria.

Time doesn't permit full detailing of the scientific errors, misconceptions, data distortions and omissions essential to the promotion. But it can be researched at a number of reputable sites. **Friends of Science** is one that I support.

As with the adoption of Keynesian economics, that the nonsense of man-caused warming has been at the forefront is that the promotion transfers huge amount of money and power to the state.

Reid Bryson has been considered as the father of scientific climatology and he observed: *"If you want to be an eminent scientist, you have to have a lot of grad students and a lot of grants. You can't get grants unless you say, 'Oh, global warming, yes, yes, carbon dioxide.' "*

Hillary Clinton used the financial disaster to advance alarmism by advising *"Never let a crisis go to waste."*

The late 1700s and early 1800s was also a time of intense political ambition and inflation. On the associated corruption, Goethe dryly observed *"Most men only care for science so far as they get a living by it, but they will worship error when it affords them a subsistence."*

The trading floor of the old and notorious Vancouver Stock Exchange is long gone, but its definition of a promotion is ageless.

*"In the beginning, the promoter has the vision and the public has the money.*

*At the end of the promotion, the promoter has the money and the public has the vision."*

In 1900 all levels of government were taking around 5 percent of GDP. Now the ambition is to take it all over.

Interventionist economics only serves the state and its limitation has always been the silly notion about a national economy. Interventionist climate control mainly serves control freaks and their ambition is global. Their schedule of alarmist meetings is intended to create a one-world-government. It will be authoritarian, and the Copenhagen Climate Summit in December has within its agenda wording about one-world-government.

It could be the movement's Waterloo. Why?

Globally, the rate they are going through them there will soon be a shortage of lies. Why soon? They are already out of half-truths.

By way of concluding this address, another saying from the old VSE is instructive:

*"So long as the price is going up, the public will ardently believe the most preposterous story."* Then when it breaks the suspension of belief fails and is replaced by shock, remorse and chagrin.

This has been the case with interventionist economics since 2007, and the remarkable plunge in solar activity and very timely decline in temps is severely impairing alarmist promotions. It is beginning to force some scientists with a regard for their reputation to climb off the bandwagon.

The Sixteenth Century was mentioned in my opening comments. This was one of three Tyrannical Centuries within which the authoritarian movement used a number of superstitions and icons to extend power. Fortunately in England, this blew out with the rate of inflation in the early 1600s and what followed has been called the "Protestant Reformation".

This description is too narrow and it could be called the "Great Reformation", whereby once the spell of authoritarianism had lost momentum, all social institutions were critically examined by the public. Those that assisted repression were dumped or diminished in influence. In science, superstitions employed by the state such as Astrology and Alchemy evolved into Astronomy and Chemistry.

Today's superstition about managing the economy is really another form of alchemy, that along with the promotion of climate change, will be soon assigned to the "dustbin of history".