2012 Year in Review

Free Markets, Rule of Law, and Other Urban Legends

by David Collum
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[Every year, friend-of-the-site David Collum writes a detailed "Year in Review" synopsis full of keen perspective and plenty of wit. This year's is no exception. Moreover, he has graciously selected PeakProsperity.com as the site where it will be published in full. It's quite longer than our usual posts, but worth the time to read in full. A downloadable pdf of the full article is available at the bottom of the post -- cheers, Adam]

Background

I was just trying to figure it all out.

~ Michael Burry, hedge fund manager

Every December, I write a Year in Review that has now found a home at Chris Martenson’s website PeakProsperity.com. What started as a simple summary intended for a couple dozen people morphed over time into a much more detailed account that accrued over 25,000 clicks last year. ‘Year in Review’ is a bit of a misnomer in that it is both a collage of what happened, plus a smattering of issues that are on my radar right now. As to why people care what an organic chemist thinks about investing, economics, monetary policy, and societal moods I can only offer a few thoughts.

For starters, in 33 years of investing with a decidedly undiversified portfolio, I had only one year in which my total wealth decreased in nominal dollars. For the 13 years beginning 01/01/00—the 13 toughest investing years of the new millennium!—I have been able to compound my personal wealth at an 11% annualized rate. This holds up well against the pros. I am also fairly good at distilling complexity down to

http://www.peakprosperity.com/print/80283
simplicity and seem to be a congenital contrarian. I also have been a devout follower of Austrian business cycle theory—i.e., free market economics—since the late 1990s.4 [53]

Each review begins with a highly personalized analysis of my efforts to get through another year of investing followed by a more holistic overview of what is now a 33-year quest for a ramen-soup-free retirement. These details may be instructive for those interested in my approach to investing. The bulk of the review, however, describes thoughts and observations—the year’s events told as a narrative. The links are copious, albeit not comprehensive. Some are flagged with enthusiasm. Everything can be found here.5 [54]

I have tried to avoid themes covered amply in my previous reviews. There is no silver bullet, however, against global crises, credit bubbles, and feckless central bankers. Debt permeates all levels of society, demanding comment every year. Precious metals and natural resources are a personal favorite. This year was particularly distorted by the elections; I offer my opinions as to why. Sections on Baptists, Bankers, The Federal Reserve, and Bootleggers describe the players in Jack Bogle’s Battle for the Soul of Capitalism.6 [55] Special attention is given to a financial crime diaspora fueled by globally overreaching monetary policies. Everything distills down to a relentlessly debated question: What is the role of government? I finish light with the year's book list that shaped my thinking. I acknowledge individuals who have made pondering capitalism a blast through direct exchanges over the years. They brought wisdom; I brought the chips and dip. You already know who you are. And then there are those characters whose behavior is so erratic, sociopathic, criminal, or just plain inexplicable—you guys are central to the plot. I leapfrog Rome and Titanic metaphors and go straight to the Lusitania.

One last caveat: I subscribe to the Aristotelian notion that one can entertain ideas without necessarily endorsing them, often causing me to color way outside the lines. With trillions of dollars circumnavigating the globe daily, nefarious activities are not only possible but near certainties. If you are prone to denounce conspiracy theories and conspiracy theorists to avoid unpleasant thoughts, you should stop reading now. I’m sure there’s another Black Something sale at Walmart. If you are a bull, you should also bail out or buckle up. This is the bear case. I will remain a permabear until some catharsis knocks me off my stance and they find a cure for my market- and politics-induced PTSD.

As this review was being completed, Lauren Lyster and Demetri Kofinas recently uploaded a companion interview on the Year in Review I did with Capital Accounts on RT_America (to be aired on December 21st and posted on Youtube.)7 [56] In this context I offer wisdom from the Master:

> If there is ever a medium to display your ignorance, television is it.

~ Jon Stewart

Footnote superscripts appear extensively throughout this review. The actual footnotes and associated hyperlinks can be found here [57].

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Investing

The elevated prices of financial assets have already eaten the future.

~ John Hussman, CEO of Hussman Funds

With rebalancing achieved only by directing my savings, I have changed almost nothing consequentially in my portfolio year over year. The total portfolio as of 12/15/12 is as follows:

Precious Metals et al.: 52%

Energy: 15%

Cash Equiv (short-term): 30%

Other: 3%

Most asset classes lurched off the starting line in January like Lance Armstrong. My portfolio eventually
settled down and spent most of the year snorkeling slightly up or slightly underwater. In a relatively rare instance, an overall return on investment (ROI) of 4% was beat handily by both the S&P 500 (13%) and Berkshire Hathaway (17%), although nearly the entire return of the S&P was p/e expansion. A majority of hedge funds struggled to beat the S&P this year as well. 

My precious metals are distributed in approximately three equal portions to the gold-silver holding company Central Fund of Canada (CEF), Fidelity’s precious metal fund (FSAGX), and physical metals (Figure 1). Gains in gold (17%) and silver (8%) were offset by a horrendously lagging performance for the second year in a row by the corresponding precious metal-based equities (-10%). The metal-equity divergence began in January 2011 and continues to baffle the hard-asset crowd (Figure 2). A plot of the ratio of the silver ETF (SLV) versus the world’s largest silver miner, Pan American Silver (PAAS), is striking (Figure 3). In May I emailed a dozen gurus for opinions about arbitraging (swapping) an SLV position for PAAS. Realizing that collectively these folks controlled billions of dollars, I felt I had to move on the idea pronto (my only portfolio change for the year). After a few weeks of an overwhelming sense of superiority, gyrations eventually left the arbitrage at about break-even. I’m guardedly optimistic about the precious-metal equities, but they have been widowmakers for two years.

Figure 1. Precious-metal-based indices (GLD in green, XAU in red, SLV in brown, and XAU in red) versus the S&P 500 (in blue) for 2012.

Figure 2. Relative performance of gold-based equities (XAU in red) vs. gold (GLD in blue).
A basket of Fidelity-based energy and materials funds afforded 2-16%. They are represented emblematically by the XLE spider (3%) and XNG Amex natural gas index (1%) in Figure 4. I am wildly bullish on natural gas for reasons discussed in detail two years ago. Unfortunately, Fidelity’s natural gas fund (FSNGX) foisted upon me by Cornell got crushed in 2009 and subsequent years relative to its peers. Making the right calls is hard enough without that kind of headwind. New management as of 2010 seems to be finally tracking the XNG. I keep adding to an already chunky position. Friends deeply embedded in the energy complex suggest that the fracking glut will take 2-3 years to burn off. (It is also claimed that the derivatives traders are whacking out the price discovery; what else is new?)

A global shift toward natural gas should reward patience.

Cash was in a U.S. Treasury-backed money-market bunker returning 0%. I had a $25K money market fund that failed to reach the IRS taxable threshold! I could care less what risky gangplank Bernanke wishes that I walk. Buying ten-year Treasurys returning <2%, with or without your finger quivering over the sell command, is a fool’s game: I’ll take the yield hit. The bond market will eventually become a killing field. Those who are pair trading—long bonds/short brains—will get their organs harvested. This seems like a near certainty.
The most disappointing part of the year was a personal savings equivalent of only 11% of my gross income compared with 29% last year and 20-30% in typical years. Unusual expenses in the form of a year of college education, a serious violin upgrade, and very large landscaping costs don’t excuse the fact that we chose lower savings over lower consumption. This troubles me deeply. Profound austerity is not a cause but an effect, something the Europeans may be just now figuring out.

To understand my lifetime returns, you must understand two unusual premises that have dominated my thoughts and actions. First, you must become wedded to an investment. Did I just say that? Yep. You’ve got to be a true believer to resist being shaken out of good investments or suckered into bad ones. Many say it’s never a bad time to take a profit. Total hooey. Those ten-baggers—the miracles of compounding—will never materialize if you bail after 20%. Just ask the Microsoft investors who exited in 1990 for a handsome profit.

My second premise is that you have to get it right only about once a decade. One of my favorite bloggers and an e-pal, Grant Williams, illustrated how daisy-chaining four secular bull markets—Gold, Nikkei, NASDAQ, and Gold—could have produced a virtual return of 640,000%—a 6400-bagger (Figure 5).1 Admittedly, this kind of luck is only found in Narnia. Statistically, somebody might have done this, although not likely in such a Texas Hold’em all-in fashion.

My variant of such a sequential trek via imbalanced portfolios changed in decadal rhythms as follows:

- 1980-88: exclusively bonds (100%)
- 1988-99: classic 60:40 equities:bonds
- 1999-2001: cash, precious metals, shorts (minor)

![Figure 5. Sequential investments in secular bull markets starting in 1970.](http://www.peakprosperity.com/print/80283)
2001-2012: cash, precious metals, energy, tobacco (minor)

My total wealth accumulated through a combination of savings and investment as shown in Figure 6. (I redacted the dollar amounts along the y-axis.) Avoiding 1987 and 2000 equity crashes and capturing the bull market in precious metals proved fortuitous. You can see that 2008 was the only down year. Berkshire has dropped five years since 1991. A 13-year accumulation rate beginning 01/01/00 of 11% annualized compares favorably to an annualized return on the S&P of -0.03% and on Berkshire of 7%.

![Figure 6. Total wealth accumulated (ex-housing) versus year of employment. Absolute dollar values have been omitted.](image_url)

I also monitor overall progress by what I call a salary multiple, which is defined as the total accumulated investable wealth (excluding my house) divided by annual salary (line 22 of the 1099 form excluding capital gains). Over 33 years my salary (actually total income) rose twelve-fold, which I can fairly accurately dissect into a fourfold gain resulting from inflation and a threefold gain (relative to starting salaries of newly minted assistant professors) due to increasing sources of income and merit-based pay raises. My accumulated wealth normalized to the moving benchmark of a rising income is plotted versus time in Figure 7. The fluctuations visible in Figure 7 not apparent in Figure 6 result from income variations.
Figure 7. Total wealth accumulated measured as a multiple of annual salary versus years of investing.

To clarify the origins of a 13-year return of 11% per year I offer Figure 8. By plunging into the precious-metal and energy sector early and avoiding all other forms of investments (S&P in particular), I was able to capture the entire hard-asset bull market. According to Money magazine’s calculator,\(^{12}\) \(^{\text{[63]}}\) I can spike the ball in the endzone and dance. They are wrong. My ultimate target—a valid target—is to accumulate 20 salary equivalents over the next 12 years (age 70). This will require an inflation-adjusted (real) annual growth of 4-5%. Some of that will come from savings. As you can tell by the Hussman quote and discussions below, however, such gains are not assured.

Figure 8. Plot of Central Fund of Canada (CEF; 1:1 gold:silver by value), XLE, and S&P.
Thinking About Capitalism

When the blind lead the blind get out of the way.

~ First grader

I realize that is what I do—I think about capitalism. It’s not deep stuff; more like taking a weed whacker to a hay field of information. This year, however, there was something askew—something corrupting the information flow. It was the presidential elections. This is a good starting point.

Election Year

No serious person would question the integrity of the Bureau of Labor Statistics. These numbers are put together by career employees.

~ Alan Krueger, White House Council of Economic Advisers

To a news and economic data junkie, presidential elections are profoundly distorting. The news feeds are inundated by election analyses that are mundane at best and nauseating on a bad day. It’s a variant of Gresham’s Law—bad information pushes out good. The pundits are either talking about the elections explicitly or couching potentially credible news stories in the context of the election. Terrorist attacks in Benghazi mutate into Obama’s Big Screw Up. The news feeds are further corrupted by billions of campaign dollars spent to deceive us. Frank Rich, award-winning New York Times journalist, estimates that George Bush had 120 “journalists” on payroll. They get overtime and hazard pay during elections. The shenanigans go deeper.

There have been numerous accusations of voter fraud. From my recollection, it was mostly the left accusing the right (the CEO of Diebold in particular). A window opened when the mischievous computer hackers, Anonymous, did a smash-and-grab on Stratfor’s server, obtaining over 5 million emails. Stratfor provides confidential intelligence services to large corporations and government agencies, including the U.S. Department of Homeland Security, U.S. Marines, and U.S. Defense Intelligence Agency. From 971 emails released to date (by Wikileaks), we find that Democrats stuffed the ballot boxes in Pennsylvania in 2008 that went unchallenged by McCain. Jesse Jackson shook down Obama for a six-digit payoff.13

Emails detailing the Bin Laden capture are worth a peek.

The most insidious election year distortion may be the tainting of economic data feeds that the marketplace relies on. Data coming from career statisticians in the federal government are always suspect. The inflation numbers, for example, are widely believed to be cooked beyond recognition using corrections recommended by the Boskin Commission.14 [65],15 [66] This year, however, the data massaging morphed into an all-out rub ‘n’ tug to ensure a happy ending for the Democrats.

The data from the Bureau of Labor Statistics (BLS) are especially susceptible to corruption. The Birth-Death Model, for example, estimates new jobs being created that nobody can detect.16 [67] Apparently, the absence of data demands that some get fabricated. These embryonic jobs have reached epidemic proportions—hundreds of thousands per month—oftentimes overwhelming the detectable jobs. Curiously, no administration ever fabricates undetectable job losses.

Another trick is a very simple iterative process for reporting statistics: Step 1—Announce inflated economic statistics as good news; Step 2—correct the inflated statistics at some later date to a very deflated number, hope nobody notices, and call it “old news anyway”; Step 3—Report new inflated
numbers that are spectacular improvements relative to the recently deflated statistics. Rinse, lather, repeat.\textsuperscript{17} [58]

The fibbing gets \textit{serious} during an election year. When pre-election unemployment numbers plummeted by 0.4%—a monumental drop—the response was immediate, visceral, and seemingly uncontestable disbelief. David Rosenberg expressed it well:

\begin{quote}
I don't believe in conspiracy theories, but I don't believe in today's jobs report either.
\end{quote}

\begin{flushright}
\textit{~ David Rosenberg, Gluskin Sheff and ex-Merrill Lynch}\end{flushright}

Well, Rosie, apparently you \textit{do} believe in conspiracy theories. Within minutes of the report Jack Welch, no neophyte to creative bookkeeping, released his now-infamous Tweet:

\begin{quote}
Unbelievable jobs numbers... these Chicago guys will do anything... can't debate so change numbers.
\end{quote}

\begin{flushright}
\textit{~ Jack Welch, former CEO of General Electric}\end{flushright}

It was an election year, however, so the goofy employment numbers morphed into a hot-button issue. Right-wing pundits accused the Obama administration of cooking the books. Left-wing pundits fired back with the shrill accusation, \textit{“Conspiracy theorists!”} Few remembered that the GOP accused the Democrats of cooking the same numbers back in 2003.\textsuperscript{18} [69]

The whole sordid affair took a strange turn when Zero Hedge noted an odd mathematical relationship between the two carefully measured employment statistics:

\begin{quote}
Measured employment numbers:
\begin{align*}
\text{fully employed/partially employed} & = 873,000/582,000 = 1.5000\ldots
\end{align*}
\end{quote}

Gosh. What are the odds that those numbers were actually \textit{measured}? I would say about 2.000\ldots\%\textsuperscript{19} [70]

Counting those who no longer receive unemployment benefits as no longer unemployed, an accounting gimmick that became chronic once the crisis began, by no means was invented by Team Obama. None of this is new. LBJ was rumored to send economic statistics back to the kitchen for more cooking. The U-6 unemployment numbers account for that mechanical engineer who is now a part-time “deposit bottle recycling engineer and firewood procurement officer.” U-6 is a more accurate measure of the employment stress and is staying persistently above 14\%.\textsuperscript{20} [71]

Election year pandering may contribute to a very odd stock cycle.\textsuperscript{21,22} If you break the 20th and 21st century into 27 four-year fragments corresponding to the election cycle—2009-2012 being the most recent—and average the returns, you get what is called the Presidential Election Cycle (Figure 9). What causes this cycle? One cannot exclude the role of friendly central bankers (sado-monetarists) juicing the markets. Mitt Romney, when he promised to fire Bernanke, may have sealed his fate.
Figure 9. Four-year election stock cycle throughout the 20th century.\textsuperscript{21} [72]

Maybe the four-year cycle in Figure 9 is a statistical anomaly and, even if real, we may not have a clue why it occurs. Nevertheless, it suggests that “Sell in May and go away” has a longer wavelength variant: “Buy the midterm and sell the Presidential.” Urban legend or not, 2013 is looking dangerous.

Events

Dan, quit embarrassing yourself.

~ Caroline Baum of Bloomberg Tweeting to a money guru who claimed that Hurricane Sandy will be stimulative

Acts of God—force majeure—tantalize market watchers and sophists alike but seem to have little effect on even the intermediate term: Economies and markets just keep marching forward. Katrina took its toll and irreparably altered lives, but it primarily illustrated government doing a heckuva job. Hurricane Sandy also exacted revenge against the civilized world (and New Jersey). It may portend things to come, should global warming live up to its billing. There is no doubt that corporations will use Sandy as an excuse for anything and everything. Q4 and year-end reports will have more Sandy-derived debris (including kitchen sinks) than dumpsters along the Jersey shore. Sandy also ushered in like clockwork the absurd claims that Frédéric Bastiat was wrong and that smashing windows and destroying infrastructure is good for the economy. Sandy will increase the GDP, but that is not economic gain. Sandy will be a bump in the road for the nation at large.

As I write this paragraph, cremnophobia—fear of cliffs—is sweeping the land. I submit that base-jumping the Fiscal Cliff may be exciting but doubt it will be some proximate trigger that causes cascading failure. The move to substantially greater austerity seems inevitable and likely to be painfully protracted—think
Japan. The Fiscal Cliff would be a fumble on our own ten-yard line. It is just one down in a very, very long game. Regardless of outcome, this will be a topic for my 2013 Year in Review.

Broken Markets

A strange game. The only winning move is to not play.

~ The W.O.P.R. computer on “Wargames”

Since Cro-Magnon Man began trading flint, furs, and women, there have been nefarious activities in the marketplace. Painting the tape—moving markets at the end of a quarter to dupe customers—is tolerated. The pop icon Jim Cramer spilled his guts describing how players of even modest means can push prices around.23 [73] I bet Jim would like a do-over on that video. Options expiration week is always exciting, as the options dealers purportedly move the equities to minimize payouts on the heavily leveraged options to maximize pain on the plebeians. Insider trading is a death sentence for a nobody, but is a misdemeanor for the big bankers. When caught, the going rate on the punishment of investment banks is a 3-5% surcharge on the profit from the illicit trade. One can only imagine how much it would cost us in punitive rebates if the criminal behavior caused a loss.

In general, however, blaming markets for your losses is a fool's game. Nonetheless, something has changed. The Federal Reserve—the Fed—has explicitly stated a vested interest in both the magnitude and direction that markets move, abandoning all willingness to let markets determine prices. These guys are playing God, taking full possession of our hopes and dreams. In analogy to global warming, their loose monetary policy jacks up prices with markedly increased volatility and enormous social costs. Kevin Phillips’ 2005 American Theocracy is a brilliant account of the demise of Western empires. He notes that the final death rattle is the financialization of the economy. When moving money becomes the primary economic activity, the end is near. Let’s look at some of the symptoms.

The high frequency traders (HFTs a.k.a. “algos” or cheetah traders) have really upped their game. The title of this section stems from Sal Arnuk’s and Joe Saluzzi’s book Broken Markets, which describes the seedy world of supercomputers skimming enormous profits. It is consensus that HFT’s are profitable for the trading platforms but of little merit otherwise. They gum up the system intentionally to garner advantage and dump millions of fake quotes to be cancelled within milliseconds.24 [73] None of this is legal, but all is tolerated. They are now trading for razor-thin profit margins of as little as $0.00001 skim per share but making it up on volume—dangerously large volume. One Berkshire Hathaway trade—a $120,000 per share stock—is rumored to have netted $10 total (0.8 cents per share).25 [74]

The markets are now at great risk. We should not expect that profiteers benefit society. We can demand that they don’t bring the entire system to its knees. I got my ten seconds of fame in an article describing the consequences of the legendary Flash Crash on May 6th, 2010:26 [75]

Wall Street is a crime syndicate, and I am not speaking metaphorically... The banking system is oligarchic and the political system has metastasized into state capitalism. The most important market in the world—the market in which lenders and borrowers meet to haggle over the cost of capital—is the most manipulated market in the world.

~ David Collum, WSJ

Flash crashes are now daily occurrences, as thoroughly documented by market research firm Nanex, and are not restricted to any one market. India tanked 15% in a few minutes.27 [76] The precious metals...
appear to be a favorite playground: “At 1:22 p.m. SLV was forced down by rapid-fire machine-generated quotes—more than 75,000 per second.” Berkshir

e Hathaway—Berkshire Hathaway!—dropped from $120,000 a share to $1 for a few milliseconds. Commodity Futures Trading Commission (CFTC) commissioner Bart Chilton says that the “third largest trader by volume at the Chicago Mercantile Exchange (CME) is one of these cheetah traders in Prague.” (Bart appears to be a supporter of clean markets, though I remain distrustful.) On August 1st, 150 stocks swung wildly. In a heavy dose of irony, the wildest—a 40% swing—was a company called Bunge. The monstrous oil market flash crashed when a 50-fold spike in trade volume hit the tape. Some fear a flash crash in the unimaginably large U.S. Treasury market.

Irrased a fevered pitch when BATS Global Markets (BATS), the third largest trading platform behind NYSE and NASDAQ, listed their own IPO. Their primary customers—the cheetah traders—drove the share price from $16 to 1 cent in 900 milliseconds, forcing the cancellation of the IPO. Knight Trading, while beta-testing their own HFT algo, released it to the wild. While the traders snarfed down celebratory mochaccinos, a pesky sign error caused the HFT algo to buy high-sell low for a very long 45 minutes. One of the most respected trading firms in the business was shopping itself to potential buyers within 24 hours. The standard excuse for erratic market behavior—Disney-like “fat-fingered traders” hitting the wrong key on a trade—became comical alibis for deep-seated structural flaws in the markets.

We have a huge problem. Don’t take my word for it. Let’s listen to what some of the pros have to say:

> All this trading creates nothing, creates no value, in fact, subtracts from value.

> ~ John Bogle, inventor of the index fund

> Essentially, the for-profit exchanges are approving their own rule changes. The lunatics are now running the asylum.

> ~ Joe Saluzzi, cofounder of Themis Trading

> High-speed trading, if we may get our two cents in, is a dubious activity to label as a technological advance.

> ~ Alan Abelson, Former Editor of Barrons

Not all IPOs flash-crashed; some simply beat investors like rented mules using more traditional methods. I had an entertaining Twitter exchange with Sal Arnuk, cofounder of Themis Trading and coauthor of Broken Markets, on May 18th just hours before the now-infamous Facebook IPO:

David Collum:

@nanexllc @joesaluzzi @themisSal A Facebook flashcrash to $0.01 would be fun and educational for the whole family.

Sal Arnuk:

@DavidBCollum doubt that....prepping for weeks

The rest is history. Facebook didn’t flash crash, but weeks of prepping were inadequate. Facebook crashed the NASDAQ market for 17 very long seconds, which is a lifetime when measured in algo
years. The high-profile Facebook IPO—technically a secondary offering—managed to maximize Facebook’s capital by selling shares into the market near its all-time high. Underwriter Morgan Stanley took a beating (possibly billions) defending the opening price of $38 before watching it drop, eventually reaching the teens. Isn’t “defending shares” illegal? While Morgan Stanley was getting hammered, the other underwriters, Goldman Sachs and JP Morgan, were loaning shares into the market for shorting. Despite a huge outcry from those hoping for an IPO opening day bounce, I found this all highly entertaining and a good lesson in risk management. Investors hoping for easy money discovered that IPO stands for “it’s probably overpriced.” Facebook also spawned a cottage industry of Mad Libs (Fraudbook, Faceplant, Farcebook…)

A lesser known IPO failure causing a stir was Ruckus (RKUS), dropping 20% on the opening and blaming it on Hurricane Sandy. Splunk’s (SPLK) IPO was halted after it hovered at $32 and then plummeted to $17 on a 500-share trade. They eventually dropped 30% in an orderly slide. IPOs from the not-so-distant past that continue to inflict pain include post-IPO losses for ZYNGA (-80%), Groupon (-90%), and Pandora (-60%). Investment-grade Beanie Babies and CPDOs sound good by comparison.

The markets are broken. It’s only a matter of time before the vernacular phrases FUBAR and SNAFU will reassert into our language. The Tacoma Narrows Bridge as a metaphor for instability has been around the web for years, but is well worth a peek.

Precious Metals

They (gold investors) want everybody to be so scared they run to a cave with gold. Caves might be a better investment than gold. At least they’re not producing new caves all the time.

~ Warren Buffett

Those elements here and abroad who are getting rich from the continued American inflation will oppose a return to sound money.

~ Howard Buffett

Let’s stay on the theme of broken markets as a transition into a discussion of precious metals. Bill Murphy and the folks at the Gold Antitrust Action Committee (GATA) obsess over powerful and dark forces. Declassified documents showing overt attempts to restrain the price of gold provide a few smoking guns. The Hunt brothers grotesquely misjudged the silver market and willingness of bankers to trigger margin calls and drive them to bankruptcy.

By the early 2000s even novice market watchers could see that central bank selling into the open market could have price suppression as a motive. Chancellor of the Exchequer Gordon Brown participated in the most famous market timing fiasco by emptying much of Britain’s gold stash below $300 per ounce. That got him promoted to Prime Minister.

Then there is the very strange phenomenon of central bank leasing of gold. I surmise that the idea was presented to the populace as a way to make money from the shiny yellow metal that just sits there in vaults. Why not lease it? The gold carry trade commenced, but lease rates are fractions of a percent per annum. No profit motive there. Central bank leasing of gold to the large bullion banks—the Too Big to Fail group—at a fraction of a percent interest seems to serve two purposes: (1) provide essentially free capital to the banks, and (2) apply downward pressure on the gold price. Rumor has it they are
going to stop publishing the leasing rates.

The game began to falter in 2001 when neither the announcement of British bullion sales nor the actual sales dropped the price, commencing a decade-long run in the metals. That is not to say the central banks have given up. Sudden and repeated margin hikes at the COMEX trapped the levered longs, and affiliated mob-like hits by insiders became commonplace. A rumored huge short position by JP Morgan-Chase (JPM) may lurk beneath the London Whale saga. JPM’s commodity guru, Blythe Masters, began denying the silver short as the whale story started to surface, claiming that JPM’s silver positions were simply hedges for their customers. Why would silver bulls hedge their investments? Data from the Office of the Comptroller of the Currency brought to light by Rob Kirby eventually showed that JPM has a whopping $18 billion naked short position in silver, corresponding to 50% of the estimated global above-ground silver supply. Is it any wonder that silver gets “monkey hammered” with some regularity by the invisible hand? Naked shorting on such a scale is both illegal and reckless. To the extent that JPM is at risk, taxpayers are at risk. CFTC Commissioner Bart Chilton unabashedly claims that big money with outsized short positions are moving the silver market, although he won’t name names yet and hasn’t done squat. Let me help you out Bart: Start with JPM. I am wildly bullish about the metals going forward. Gold and silver’s returns look like a normal year within a secular bull market [editor’s note: this section was written by David prior to this week’s smackdown of the precious metals]. Precious metals investors waited with baited breath as a descending triangle starting in mid-2011—a classic chart pattern recognized in technical analysis (TA)—marched to judgement day (Figure 10). Folklore says when the highs and lows converge, the price will resolve boldly to the upside or downside. OK. That sounds really stupid, but that’s state-of-the-art TA. In any event, it seems like gold took the 50% probability route to the upside thanks to an auspicious goose from more quantitative easing (QEIII). But that’s just T&A (chart porn) for the gold bugs.

The future is unknowable, yet $85 billion per month of QE IV is most definitely bullish for tangible assets. Central bankers around the World are printing around the clock. Of course, the usual cast of top callers were braying about a top. Notable gold bears included Warren Buffett hammering gold in the Berkshire Hathaway annual report, quickly followed by a show of support from his poker buddy Bill Gates. Buffett wrote an article entitled “Why Stocks Beat Gold and Bonds” and then promptly bought a gold-mining company. Charlie Munger again displayed his tin ear with a decidedly anti-Semitic quote about gold (not worthy of repeating, only criticizing). There are credible arguments against gold, some better than others. An optimist might believe that central bankers will begin to behave themselves…but only in the
land of unicorns and Skittles rainbows. Some claim it is a crowded trade. Many argue that gold has been a horrible inflation hedge. To this I note that shovels and bulldozers both move dirt but are very different tools. Equities and gold have similarly differentiated roles as inflation hedges.

Secular (multi-year) bull markets are said to attract investors in three specific phases: (1) first arrivals are wing nuts and whack jobs and precede anybody in their right mind, (2) the smart money arrives once the bull offers evidence there is serious money to be made, and (3) retail investors—the rabble—show up in the final phase. Once group (2) sells to group (3) in what is euphemistically called “distribution,” the invisible hand of the market throws a toaster oven in the pool and the bodies start floating to the surface. This year was dominated by smart-money gold supporters with gravitas and serious bucks. Hedge fund managers supporting gold with dire warnings of monetary chaos included luminaries George Soros, John Paulson, David Einhorn, Jim Rogers, Ray Dalio, and Kyle Bass. Einhorn and Dalio both took special care to condemn Buffett’s gold bash. Bill Gross, head of PIMCO with almost two trillion dollars under management, noted gold “will be higher than it is today and certainly a better investment than a bond or stock, which will probably return only 3% to 4% over the next 5 to 10 years.” Bill has caught the fever. Billionaires Hugo Salinas Price and Eric Sprott are avid precious metal investors and devout believers in organized price suppression.

Central banks became net buyers starting in 2009 after years of selling and have been increasingly aggressive (Figure 11). (I call central bankers both “smart money” and “feckless”; I’m still working on resolving that paradox.) Chinese and Korean central bankers have explicitly stated gold is the only safe asset. Such reports are picking up in intensity. Other events seemed new to 2012. The International Monetary Fund (IMF) has flipped to net buyer. South Korea, Paraguay, Turkey, Vietnam, and Russia all increased their gold holdings. Iran swaps oil for gold with China and Turkey.

What made this year so interesting was the part occurring below the surface. Gold may soon be designated a Tier 1 asset. Banks are required to maintain minimum balances of Tier 1 assets to ensure the safety of the system. (They need to work on that.) When the next credit crisis arrives, rather
than selling gold to raise Tier 1 assets, banks will be incented to buy gold. It is beginning to act like a currency. The ramifications are multifold.

For the first time, we are beginning to hear discussions of some form of gold standard. It would probably be a variant of the gold-exchange standard of the early 20th century. I would be satisfied if gold was simply allowed to compete for supremacy in the open market. The most important step would be to pass gold legal-tender laws, which are at various stages in a dozen states.60 [117] (This could elicit a states’-rights battle.) Rendering gold’s price change denominated in dollars as a non-taxable event would be the big move. Bernanke tried to take on the push for a gold standard in a series of lectures at George Washington University.61 [118] I found his arguments unpersuasive, exactly what you would expect from a guy who believes that profound monetary injections and inflation are valid monetary tools. The gold standard seems like a distant possibility given the Republicans endorsed the idea in their platform; we know they lied—their lips moved. The counter argument stems from a survey showing 37 prominent economists all opposed a gold standard; 37 economists couldn’t possibly be right.62 [119]

One could dismiss discussions of a gold standard if it were not for the second really interesting topic—global gold movements. Let’s be clear, this story is muddled. There are three variants of gold conspiracy theory that may (or may not) lay the foundations:

(1) Thesis 1: Gold exists in the vaults of the Fed and Fort Knox, but we don’t own it anymore. We are told that the gold possession is as simple as a forklift moving a pallet from one wall to the next within the same vaults. Doubts about ownership are exacerbated by the unwillingness of the authorities to independently audit the gold since the 1950s despite calls for it from Congress. This is odd by any standard.63 [120]

(2) Thesis 2: The gold in the vaults is of a substandard quality. This idea is way out there but cannot be summarily dismissed. What does low quality actually mean? Supposedly we have delivered sub-standard gold on a number of occasions.64 [121] There were rumors years ago that the gold in the bank of England was reported to be “flaking,” leading one intrepid analyst to declare that it doesn’t matter “provided they don’t try to sell it.”65 [122] Oh, I just wet myself. As a chemist, I can assure you if it flakes it ain’t gold and that analyst-dude is a perma-doofus. Tungsten-impregnated gold surfacing in retail gold markets has fueled speculation that the central banks are hoarding tungsten.66 [123] The conspiracy theorist in me wonders if the occasional fake gold bar would be good for tamping down an incipient gold mania.

(3) Thesis 3: There is no gold.67 [124] The claim that the gold is missing holds a certain logic. If the Fed leased physical gold to the bullion banks and these banks sold it into the open market for beer money, then it’s gone.68 [125] It is very odd that the Fed pools the physical metal and the leased metal on a single line of their self-reported balance sheet (to save space, I guess).69 [126]

The status of sovereign gold stashes is unclear. Here’s where it gets really interesting. Sovereign states are starting to repatriate their gold—they want to bring it home. It started in 2011 when our close friend and ally Hugo Chavez requested 100 tons returned to Venezuela, with a correlated spiking of the spot-price of gold and gold backwardation. (Backwardation is a grammatical abomination indicating that short-term demand for a commodity is high and commodity traders flunked English.) Demand began in earnest starting in the Netherlands and spreading to other postage-stamp-size countries Paraguay, Ecuador, Vietnam, Switzerland, and Germany.70 [127], 71 [128] Germany? Germany may be growing weary of sharing a fiat currency with the PIIGS—Portugal, Italy, Ireland, Greece, and Spain (vide infra).

It seems like gold is coming out of the closet. My concern is that we will quickly move from fear of
deflation to disquieting inflation culminating in uncontrolled inflation. If the dollar goes south fast, do you think investors will seek safe-haven in another fiat currency? Those who headed to Swiss Francs got their heads handed to them this year in an instantaneous 10% debasement. There must have been some forex traders doing laps around the drain that morning. I cannot rule out a run on fiat currencies—a collapse of the entire Bretton Woods currency system. Mitigating such tail risks would not be completely irrational. Am I saying that this time it’s different? No. I am saying our fiat currency will join the other fiat currencies as historical footnotes. As the insane posters at Zero Hedge like to say about gold, BTFD (buy the dips).

Resources and Energy

I'd put my money on the sun and solar energy. What a source of power! I hope we don't have to wait until oil and coal run out before we tackle that.

~ Thomas Edison (1931)

Eventually the point is reached when all the energy and resources available to a society are required just to maintain its existing level of complexity.

~ Joseph Tainter, author of Collapse of Complex Societies

The resource sector provides me with a potential inflation hedge and represents a bet on a secular change in energy availability, all the while allowing me to pretend to be normal. In previous years I have endorsed Chris Martenson’s Crash Course with unbridled enthusiasm—a must see, which emphasized the case for increasingly constrained oil production, and delineated my enthusiasm for natural gas equities. Many of my views have not changed.

Investment giant Jeremy Grantham continues to actively warn of acute resource depletion. He submits that rapidly rising raw material prices are not a bubble but rather a civilization-altering paradigm shift. Simply put, we are depleting everything. The CEO of Gulf Oil, in a decidedly ambiguous statement, noted that “oil consumption in the next seven years is not going to grow and could drop off as much as 15%.”

Suggestions of constrained oil supply continue to work their way into the mainstream. Data shows Saudi production has remained remarkably constant. Many doubt they can ramp it or even sustain it. The former vice president of Saudi Aramco warns of unwarranted optimism that price hikes stem from “the reality that the oil sector has been pushed to the limit of its capabilities.” There are claims that the Saudis will be net importers by 2030 but from whom? David Greely of Goldman Sachs indicated that it is only a matter of time before “OPEC spare capacity becomes effectively exhausted, requiring higher oil prices to restrain demand.”

Other Goldmanites suggest that “a disturbing pattern has emerged where each tentative recovery in the world economy sets off an oil price jump that, in turn, aborts the process… Oil has become an increasingly scarce commodity. A tight supply picture means that incremental increases in demand lead to an increase in prices, rather than ramping up production. The price of oil is in effect acting as an automatic stabilizer.” A hyperbole-free interview of prominent oil economist James Hamilton sheds light on a world facing tighter supplies. A counter-argument to all these gloomy views came in a report via Bloomberg stating that the U.S. will
pump “11.1 million barrels of oil a day in 2020 and 10.9 million in 2025.” This may be true, but anybody who projects oil production a dozen years from now to three significant figures has credibility issues. That did not stop viral dissemination across the Twittersphere.

Some suggest that natural gas will fuel our economy for hundreds of years. Others say the case is wildly overstated: Bakken wells lose 90% production within five years. Still others focus on the environmental catastrophes and legal boondoggles affiliated with fracking. It seems clear that, come hell or high water, we are going to frack, and we are going to witness a secular shift to a natural-gas-dependent economy. It would be great if this works and does so without environmental calamity. I am agnostic on both. The equity valuations are tame, especially given the current razor-thin profit margins that are projected to expand. I continue buying the equities betting that powering the globe will be profitable.

Fresh water and, by direct correlation, food face huge supply issues in China, the U.S., and emerging markets around the world. Staying close to home on this one, the Ogallala Aquifer under the Great Plains was reported to be down to one third of its original depth and is projected to “run dry in two to three decades given recent withdrawal rates.” Atlanta is in a legal battle with Florida and Alabama over 20% of the flow from Lake Lanier. No matter how you cut it, this is foreshadowing trouble ahead. I looked into water-sector investments a decade ago but couldn’t tease out opportunities.

The blogosphere has made the case for highly constrained rare-earth elements crucial to wind turbines and solar cells. The bulls note that China controls 95% of the market and suggest that building alternative energy programs based on the rare earths will drive the price to the moon. I had dinner with the CEO of Chemetall, a major dealer in metals and metal catalysts. He assured me that rare earths are not rare, and that China has driven competitors out of the marketplace; higher prices will fix that when needed. I could detect no agenda in his answers.

The Baptists

The lapse of time during which a given event has not happened is…alleged as a reason why the event should never happen, even when the lapse of time is precisely the added condition which makes the event imminent.

~ George Eliot in Silas Marner

We were all worried about these issues in 1927, but you can only worry about things for so long.

~ Anonymous

Prior to any financial dislocations there are many who preach of the coming crisis. In 1924, Roger Babson warned of credit excesses that would lead to catastrophe. Charlie Merrill of Merrill Lynch fame sought psychiatric help due to his inexplicable bearish views; as legend goes, he and his psychiatrist emptied their investment accounts and dodged the carnage. The stock futures speculation in the 1920s was so obvious that Congress held hearings to discuss it well before the crash. The crash and subsequent multi-decade global devastation arrived to the total shock of many. Town criers could be heard screaming of a coming tech crash in the late ’90s by those who listened. We had congressional hearings on derivatives speculation wherein Brooksley Born methodically laid out the plotline for the coming storm in unregulated derivative markets. I wrote a 2002 email describing the coming
subprime crisis and banking collapse. Prescient? Not really. I was simply parroting ideas scattered over the Internet. The few who played the housing bust with leverage get the limelight; countless thousands saw the housing excesses in the years leading up to 2007.

This year had its share of preachers of unassailable credibility telling us of more trouble to come. Are they farsighted or fooled? I haven’t a real clue. I can say, however, that their advice demands your attention.

Let’s begin with the most prolific of doomers, David Stockman, former Wall Street insider and Reagan budget genius. Stockman was omnipresent, telling anybody who would listen of a coming mayhem in the bond market and accompanying pension crisis, labeling our current economic status as “the end of a disastrous debt super cycle that has gone on for the last thirty or forty years.”

David places blame squarely on the Fed by suggesting “if we don’t drive the Bernankes and the Dudleys and the Yellens and the rest of these lunatic money-printers out of the Fed and get it under the control of people who have at least a modicum of sanity, we are just going to bury everybody deeper.” Somewhat paradoxically, he noted, “if the Fed doesn’t keep printing, it’s game over.”

John Hussman undermines the very foundations of monetary easing in one of the most cogent arguments that I have read. He is a deep-value guy whose analyses have refreshingly long-time horizons and whose portfolios have been bludgeoned in the short term.

George Soros rattled Newsweek readers when he suggested the global credit retrenchment is “about as serious and difficult as I’ve experienced in my career...comparable in many ways to the 1930s. We are facing now a general retrenchment in the developed world, which threatens to put us in a decade of more stagnation, or worse. The best-case scenario is a deflationary environment. The worst-case scenario is a collapse of the financial system.” He predicts a collapse of social order, suggesting “it is about saving the world from a downward economic spiral.” George is known for talking his book, but what position is he talking up? This is not a trick question...well maybe it is. (Answer: Gold. Lots and lots of gold.)

Bill Gross suggests that "a 30-50 year virtuous cycle of credit expansion which has produced outsized paranormal returns for financial assets—bonds, stocks, real estate and commodities alike—is now deleveraging because of excessive ‘risk’ and the ‘price’ of money at the zero-bound." He concludes that "we are witnessing the death of abundance and the borning of austerity, for what may be a long, long time." Detractors like to pick on Bill’s DOW 5000 call years ago. With inflation adjustment—accurate inflation adjustment—that decade-old call is approaching spot on.

Jim Rogers predicted that some of the Ivy League institutions would go bankrupt. Harvard had a terrible credit seizure in 2007-09 due to their hedge-fund-like endowment, but Jim’s prediction was made in 2012. Jim doesn’t think we are done yet.

Nomura’s Bob Janjuah is always good for brutal assessments. Bob noted that “markets are so rigged by policy makers that I have no meaningful insights to offer.” Bob goes on to note in a later piece that “central bankers are intentionally mispricing the cost of capital, in an attempt to push the private sector to misallocate capital into consumption and into asset purchases at the wrong time and at the wrong price.” He blames Greenspan and Bernanke explicitly for tens of millions of American citizens who are “either homeless and/or on food stamps.” Bob can really turn a phrase. “Financial anarchy” is always good for a few chuckles. Say what you really think, Bob. The world’s central bankers are reserving their own special place in hell.
Ray Dalio, head of Bridgewater Associates—the largest hedge fund in the world—has been bearish for awhile and is becoming quite the gold bug. In January he noted that he was bearish “through 2028.” In subsequent presentations, he seemed to change his tune by referring to our global state of affairs as a “beautiful deleveraging,” which he defines as some sort of optimal inflation/deflation cross-dresser operating through a combination of defaults and debt monetization. I guess beauty is in the eyes of the beholder. One prominent market watcher—me—suspected that Ray had an eye on a Romney-cabinet-level appointment. We’ll never know.

Legendary investor Jeremy Grantham with $150 billion under management, Thomas Brightman of Research Affiliates, and Robert Gordon of NBER lit up the blogosphere late in the year with conclusions that global growth would drop to the 1% zone. Their predicted durations—decades or more—were newsworthy. Grantham suggests that demographics and resource depletion will cause us to never regain our previous growth rates. He had previously amplified a notion first presented by Adam Smith in *The Wealth of Nations* by showing that a sustainable 3% compounded growth rate, rather than the “greatest invention of all time,” is total mathematical nonsense. A cubic meter of physical wealth expanding at 3% over the Egyptian dynasty—admittedly a long time—would fill ten solar systems—a large volume.

Billionaire Richard Branson joins Grantham in predicting that capitalism is destroying the planet, focusing in particular on the perpetual growth model that will consume everything. The great story about Richard is that he is rumored to have tried to hit up Obama for some weed in a recent trip to the White House. We don’t know if Obama’s “Choomwagon” was in the shop.

Richard W. Fisher, President and CEO of the Federal Reserve Bank of Dallas Texas, was a buzzkill for the fluffers at the Fed, noting that there is “a frightful storm brewing in the form of un-tethered government debt.” He says that he chose the phrase “frightful” to “deliberately avoid hyperbole.” Fisher suggests that the long-term fiscal situation of the federal government will be unimaginably more devastating to our economic prosperity than the subprime debacle and the recent debauching of credit markets that we are working so hard right now to correct.

2012 was a big year for taking the bear case to the Halls of Power. Jim Rickards, author of *Currency Wars*, presented his concerns about currency debasement to Congress. James Grant and Robert Wenzel in speeches at the Federal Reserve both hammered the Fed for horrendous monetary policies that are destroying our currency and capitalist system. Jim is a total genius, and he is very attention-worthy. Legendary hedge fund manager and cherished confidant David Einhorn poked at the Fed with his “jelly donut” speech. It was Silence of the Lambs at the Buttonwood Conference when he pointed out what they should have known: Artificially low interest rates drive up commodities and reduce income streams to a trickle, forcing consumers to save more and spend less. He throws in a little money multiplier logic and—voilà!—stimulus is totally negated.

Einhorn accuses the Fed of “offering some verbal sleight-of-hand worthy of a three-card Monte hustle.” David wonders out loud: “We have just spent 15 years learning that a policy of creating asset bubbles is a bad idea, so it is hard to imagine why the Fed wants to create another one.” I wonder out loud: How much did Fed policy have to degenerate to force the Einhorns of the world to focus on monetary theory rather than investing?

We had several bootleggers-turned-Baptists. The technical term is “tranny.” John Reed confessed his sins while CEO of Citibank, explaining how Citibank and Travelers, with the aid of a very friendly
administration, destroyed the Glass-Steagall safeguards that had protected consumers from financial disaster since the ‘30s. Sandy Weill, the next CEO of Citigroup, shocked the world by suggesting that big banks “be broken up so that the taxpayer will never be at risk.” What’s gotten into these Citi-boys? Would it be too much to ask for a *mea culpa* from Robert Rubin? Yes.

William Cohan, former Wall Street investment banker and author of several best sellers including a comprehensive history of Goldman Sachs, pointed out the cracks in the seams—the *omerta*—at Goldman, flaws in the FINRA arbitration system, the mathematically nonsensical $100 million IRA of Mitt Romney, the SEC’s lack of oversight on nefarious activities at Citigroup, and a striking exposé of Robert Rubin’s deep-seated political power.

These guys are some of the sharpest knives in the drawer. They view the world through darker lenses than most. Whether they are right or not, you’ve been warned.

### The Bankers

> It is well enough that people of the nation do not understand our banking and monetary system, for if they did, I believe there would be a revolution before tomorrow morning.

~ Henry Ford

The most newsworthy story about Goldman Sachs may be that they weren’t in the news that much. Of course, there were a few skirmishes. Disgruntled employee Greg Smith took his best shot at the Goldman Death Star, but both his interview and book proved toothless. Smith told us that Goldman employees showed scorn as they ripped the faces off their clients called “Muppets.” Anybody who read Michael Lewis’s *Liar’s Poker* knows that clients are chum for the brokerages. Goldmanites had to run out the back door without putting their pants on when it was discovered that they were part-owner of a website focusing on the sex-trafficking of underaged girls. It also was reported that many Goldman folks were tipping off Rajaratnam, although that story is now passé. Most importantly, however, JPM managed to knock Goldman below the fold.

Problems for JPM began in 2011. As noted in my 2011 summary, MF Global—a reincarnation of the formerly bankrupted and scandal-riddled Refco—had collapsed, segregated funds had been rehypothecated (rehypothecate = used repeatedly; see also, “stolen”), and the money was lost speculating at the track. Remaining funds (including stored gold bars, if they weren’t already rehypothecated) were quickly snarfed up by JPM under the arcane principle of law referred to as “finders keepers, losers weepers.” We finished 2011 knowing that Corzine was a weasel and in a world of trouble and serious money had “vaporized”—not to be confused with “stolen”—to use language from a planted story. Vaporized money brings to mind the must-see South Park episode, “And It's Gone.” The authorities were handed a Madoff-quality scandal to finally prove they are the best regulators money can buy. Twitter hound Mark Melin was posting hourly updates on nefarious activities while legal beagle James Koutoulis was gearing up for a big class action suit.

Just as night follows day, 2012 brought us…crickets. Nothing but chirping crickets. The case was dropped. How the hell did this happen? The JPM legal team exploited the chaos and rushed MF Global into bankruptcy. Chris Whalen explains that bankruptcy gave JPM “first dibs” creditor status whereas a fraud charge would have diverted the funds to less worthy folks—the rightful owners.

To ensure the transition went smoothly, former FBI Director and political hack Louis Freeh was put in charge of overseeing this mess. Freeh promptly asked the bankruptcy court to allow payouts to MF
global executives for the long hours spent cleaning up.\textsuperscript{128} [187] (I’d give them free room, three square meals, and snappy orange jump suits.) Freeh then diverted funds from clients to legal defense funds of MFG execs.\textsuperscript{129} [188] The other MFG trustee named Giddens—the other MFG trustee?—pressured litigants to release the banks of all liability to receive reimbursement, suggesting that (1) the money didn’t really vaporize, (2) stealing money and then giving it back when caught should not be a crime, and (3) extortion is legal if you are a trustee.\textsuperscript{130} [189] Within a week it was announced that the Rule of Law had been downgraded to a guideline.

As often used in comedies, we use an epilogue to track the fates of the major players. Jon Corzine bought himself a “Get Out of Jail Free” card by remaining a major fundraiser (a bundler, to be exact) for Team Obama.\textsuperscript{131} [190] The Department of Justice (DOJ) stood ready to indict Corzine if he missed a payment. Immunity to Corzine’s consigliere would have revealed some serious dirt, but the DOJ declared there was no case and walked.\textsuperscript{132} [191] Corzine is exiled in the Hamptons sans ankle bracelet on an OJ-esque quest for the lost funds and a new job as a hedge fund manager. Rumors that Corzine’s life insurers put his policy in a risk pool have not been confirmed. Team Obama got a second term in the White House, and nobody in the administration has been indicted for racketeering. The sordid story of MFG has been relegated to case studies in MBA ethics classes. (Evidence aside, they do have such courses.) The main character, Jamie Dimon, landed a leading role in the next scandal and was put on the shortlist for Secretary of the Treasury.

As the replacement regulators and DOJ were playing Pull My Finger, rumors among the blognoscenti surfaced of a big London-based commodity trader who was in trouble.\textsuperscript{133} [192] The trader was originally referred to as “The Caveman” but soon became “The London Whale.” Mike Mayo, one of the elite banking analysts, downgraded JPM a day or so before the story broke and later attributed the problem to “negative incentives and the revolving door” (corruption from the unholy alliance of banking-government).\textsuperscript{134} [193] Jamie Dimon initially claimed it was “a tempest in a teapot ,” but then JPM announced burgeoning losses in the billions. Eventually, even CNBC bought a ticket on the London Whale Watching Tour. Those guys are sleuths.

JPM was in very big trouble. (Just kidding; of course they weren’t.) Damage control was swift and effective. JPM liquidated an estimated $25 billion of assets to both clean up the mess and book enough profits to guarantee that their reported earnings would show that this was not a BFD (big deal).\textsuperscript{135} [194] The London Whale, aka Bruno Iksil, was labeled a rogue trader, which is a technical term for a “rainmaker turned patsy.” With dripping irony, Bruno’s boss is named Achilles Macris.

Normally, the story would end there, but the Greatest Banker in the Universe—Jamie Dimon—faced a stark choice: Either claim that he screwed the pooch—uniquely so—or admit that the banking system is still hopelessly corrupted. The forthcoming mea culpas were slathered with gobs of sincerity. “We were total idiots. We can’t pour water out of a boot with the directions on the heel.” (paraphrased, of course) Jamie testified to Congress for no apparent reason, getting grilled by Congressman Tim Johnson who, because of a massive stroke in 2006, was not particularly threatening. Spencer Bachus, Chair of the Financial Services Committee, treated Dimon with kid gloves and let him testify not under oath because JPM is his second biggest donor. What’s appalling is that Bachus sold us down the river for a take of $119,000 over the congressman’s career.\textsuperscript{136} [195] That was money well spent. Supposedly, the entire Financial Services Committee cost a little over $800,000.\textsuperscript{137} [196] Peter Schweizer’s book, \textit{Throw Them All Out (vide infra)} documents in lurid detail that congressmen and congresswomen are prostitutes, but cheaper. In an interview in Davos, Dimon was able to put the problems to rest, noting that “most of the bad actors are gone.” You betcha.

Of course, other banks wanted a piece of the action. Barclays made a feeble grab for fame by taking the
lead in the Libor scandal. Libor, the London Interbank Offered Rate, is a compilation of self-reported lending rates that influence interest rates throughout the $500 trillion global credit markets. Self reported? Whatever could go wrong? It turns out Barclays was cheating the numbers. The retribution was swift and severe: Barclays was fined a whopping $200 million, which cut into some of their profits on the scam. The British Banking Society, using language right out of Casablanca, said that they were “shocked.”

Meanwhile, journalists around the globe, scrambling to figure out what Libor meant, spouted scholarly analysis like Milli Vanilli. It soon became evident, however, that all of the banks were fudging their numbers. The scandal was promptly downgraded three levels to an embarrassment when 2008-vintage articles by Mark Gilbert and Gillian Tett surfaced that described the rate rigging. The Fed knew about it in 2008. Liborgate could clog the courts for awhile as borrowers lawyer up hoping to identify damages.

The blogosphere thinks Liborgate is “huge.” I find the scandal oddly anticlimactic given that central banks around the globe openly rig rates on a daily basis. James Grant concurs with this minority view. It is galling, however, that the scandal seems to reach the highest levels of the banking cartel—the central banks. For me, it is profoundly disturbing that global capital has been fully sequestered from price discovery.

The British Banking Association was shocked again when Standard Chartered Bank got accused of illegally laundering $350 billion for Iran. Rogue New York banking regulator Benjamin Lawsky filed his charges as the Justice Department was on the verge of declaring that Standard Chartered’s trades “complied with the law.” Standard Chartered promptly entered settlement talks with everybody. A Deloitte partner involved with the scandal offed himself. For him, the scandal was a big deal.

The hits just kept coming. HSBC got charged with money laundering for terrorists, drug cartels, and organized crime syndicates. It seems that HSBC must have picked up BCCI’s clients after their scandal-induced collapse in the late ‘90s. This ‘affiliation’ with organized crime is silly: Banking is organized crime. Reuters reported that HSBC could be fined over $1.5 billion for money laundering and face criminal charges. Of course they could, but they won’t.

US Bancorp got charged $55 million for scamming customers with overdraft fees by illegally maximizing the number of checks put into overdraft. In a possible script for the MFG sequel, Cantor Fitzgerald was accused of “undersegregating” funds. This is like “kind of pregnant.” The whole thing seems “sort of criminal.”

The more generic thieves and scoundrels returned with an encore when CEO of Peregrine Financial Group (PFG) stole rehypothecated customer funds for several years. The CEO of Attain Asset Management (AAM) captured the spirit of the outrage against PFG, noting “This time it’s personal.” PFG CEO Wasendorf attempted suicide, presumably hoping to front run the AAM CEO to (paraphrased) “put a cap in his ass.” Jeffries promptly began a Chapter 7 liquidation of PFG positions after a failed margin call. Once again, Chris Whalen explained the nuances. Apparently, this time they did it right by sending PFG into receivership to the advantage of the customers: Reuters reported depositors got 30 cents on the dollar. I imagine that debt subordination by big money folks somehow played a role.

Whistleblowers took a serious beating this year. FINRA, Wall Street’s self-policing arbitrators, managed to bankrupt a Morgan Stanley broker with a fine of $1.2 million after he accused Morgan Stanley of
adding hidden fees to retirement accounts. When the case was followed up, nearly half of the 18 hrs of tape, mandated to be saved, “disappeared.” The transcript of an anonymous whistleblower testifying to CFTC was a great read. The CFTC removed it from their website, but a copy was saved. A lawsuit by Securities and Exchange Commission (SEC) whistleblower David Weber alleges that the SEC is involved in all sorts of nefarious activities, including specifically tracking potential whistleblowers. David Einhorn also presents the SEC as profoundly corrupt in his book, Fooling Some of the People All of the Time.

We found out this year that Deutsche Bank had been accused by three independent whistleblowers of hiding $12 billion in losses to avoid a bailout during the bailouts (if that makes any sense). This scandal is a dog’s breakfast: (1) the whistleblowers—one of them a risk officer—got fired within days of the complaint; and (2) the current SEC’s chief enforcement officer was in charge of the legal compliance at Deutsche Bank and was its general council during the cover up.

I have painted the banking industry with an ugly brush. I’m sure most bankers are good, honest people. If so, it’s time you guys start cleaning up your profession. When you find yourself saying, “Somebody should do something,” that somebody is you. If you stay silent, it’s just a Sandusky sequel.

The Federal Reserve

I simply do not understand most of the thinking that goes on here at the Fed, and I do not understand how this thinking can go on when in my view it smacks up against reality...Do you believe in supply and demand or not?...Let’s have one good meal here. Let’s make it a feast. Then I ask you, I plead with you, I beg you all, walk out of here with me, never to come back. It’s the moral and ethical thing to do. Nothing good goes on in this place. Let’s lock the doors and leave the building to the spiders, moths, and four-legged rats.

~ Robert Wenzel, in a speech at the NY Federal Reserve

Well that pretty much captured my sentiments. The Fed gets their pick of the litter coming out of PhD programs. They are a politically (in)dependent group with a dual mandate of supporting the banks and maximizing bank profits. The dozen or so members of the Federal Open Market Committee (FOMC), by virtue of arrogance and hubris, have become intellectually neutered and are now menaces to society. Why listen to an organic chemist—an academic, to boot? Let’s see what the pros have to say.

A first year investment banking associate knows more about credit creation than the entire FOMC combined.... Our colleagues at the Fed have consistently failed to understand the operations of financial markets and how credit operates in our society. This may surprise some of you, but it doesn't surprise me at all.

~ Chris Whalen, Founder of IRA Risk Analytics

I have to say the monetary policies of the U.S. will destroy the world.

~ Marc Faber, Elite Barrons Round Table Member

The little sliver of remaining hope was officially pronounced dead [with QEIII]....we are witnessing the greatest monetary fiasco ever.

~ Doug Noland, Federated Investors
The Chinese aren't loaning to us anymore. The Russians aren't loaning to us anymore. So who's giving us the trillion? And the answer is we're just making it up. The Federal Reserve is just taking it and saying, 'Here, we're giving it.' It's just made up money, and this does not augur well for our economic future.

~ Mitt Romney, unemployed

When I read direct quotes and commentary about Bernanke's policy of driving up asset prices in general and equity prices in particular, I almost want to cry over the ludicrousness of this position. The Fed is pursuing the same road to ruin as it did between 2003-2007.

~ Albert Edwards, Societe Generale

Bernanke, and his MIT ilk, has made monetary policy into a laboratory for monetary theoreticians.

~ Kevin Warsh, former Federal Reserve governor

It’s the general global landscape where you have an incredible mispricing of risk that’s being delivered at the hands of academics at the central banks of the world.

~ Wellington Denahan-Norris, CEO of Annaly Capital

I am a little—maybe more than a little bit—worried about the future of central banking. We've constantly felt that there would be light at the end of the tunnel, and there’d be an opportunity to normalize but it’s not really happening so far.

~ James Bullard, President of Saint Louis Federal Reserve

Let’s briefly break away from 2012 condemnations and snag a quote from my favorite book on Austrian economics and the Great Depression:

The end result of what was probably the greatest price-stabilization experiment in history proved to be, simply, the greatest and worst depression.

~ Phillips et al. in Banking and the Business Cycle (1937)

Of course, the big news was the third wave of debt monetization referred to as QE IV, QEtc, QEInfinity, or Cash for Clunkers II. The Fed is jamming over $80 billion of high-powered money per month into the economy. Initial promises to monetize aggressively until 2015 have been extended to infinity and beyond. The Fed pretended it was sterilized—the long-term debt purchases were being offset by short-term debt sales. “Operation Twist” (QE II), however, recycles the short-term debt right back into long-term debt. Problem solved.

There is some room for debate as to why they are pushing monetary policy to the edge of the known universe. They tell us that it is to improve the economy and help the little guy by throwing savers under the bus with repressively low interest rates. Last I looked, the savers are the little guys. It has been estimated that if interest income as a percentage of total personal income had remained at its 2008 level, the total would now be an additional $1.5 trillion.\textsuperscript{159} \cite{218}

To achieve their goal of stabilizing the banks—not all the banks, just the really big ones—the Fed has completely dismissed any notion that the debt markets should be allowed to clear, which is Austrian-speak for establishing market-based pricing. James Grant calls it “waging war on the pricing
mechanism.” The Fed does this via purchases of 60-80% of all the newly issued federal debt because our foreign creditors have gone on a buyers’ strike. Without the Fed’s unprecedented interventions, bond prices would plummet (sponsored by Red Bull, no doubt), affiliated interest rates would spike, bond holders would get crushed, and the federal government would have to borrow at rates that would completely choke our already auto-asphyxiated federal budget. We’re now homing in on why the Fed is monetizing debt. (Note to readers: When you read an article stating some variant of “low rates show everything is rosey,” that person is an idiot.)

The irony here is that the Fed’s zero interest rate policy (ZIRP) is choking the savers, as noted by David Einhorn (vide supra). Similar cases have been made by Chris Whalen and others. William R. White, former Head of the Monetary and Economic Department at the Bank for International Settlements (BIS), wrote a must-read paper entitled, Ultra Easy Monetary Policy and the Law of Unintended Consequences. The Fed’s policies are Soviet-style stupidity and a short trek to financial perdition. Even worse, Daniel Kahnemann, Nobel Laureate and expert in behavioral psychology, would probably argue that the Fed’s decision making is no more accurate than “monkeys throwing darts.” Milton Friedman indirectly made a similar case against central planners in an interview with macroeconomist Phil Donohue.

The Bootleggers

Why does the New York Times hate the banks?

~ Jamie Dimon, CEO of JP Morgan

It’s not the New York Times, Mr. Dimon. It really isn’t. It’s the country that hates the banks these days.

~ Joe Nocera, New York Times

I have beaten on the bankers hard and will continue to do so until somebody can say their house is clean. I should, however, let these bootleggers and affiliates—the Baghdad Bobs of Finance—speak for themselves. As you read these quotes, ask yourself: Did they really say that? Really?

Low Fed rates didn’t fuel the housing bubble.

~ Alan Greenspan, former Chair of FOMC

This is the United States of America. That's what I remember. Guess what.... It's a free f***ing country.

~ Jamie Dimon, CEO of JPM

Hanging bankers won’t help…Public anger over the financial crisis is wrong.

~ Tony Blair, former Prime Minister of England

Large numbers of people who have ‘lost’ their house through foreclosure have actually realized a profit because they carried out refinancings earlier that gave them cash in excess of their cost. In these cases, the evicted homeowner was the winner, and the victim was the lender.
~ Warren Buffett, Berkshire Hathaway

The evidence that I've seen and that we've done within the Fed suggests that monetary policy did not play an important role in raising house prices during the upswing.

~ Ben Bernanke, Chair of FOMC

We economists...have reason to be proud of our analyses over the past five years. We understood where we were heading, because we knew where we had been.

~ Brad DeLong, economist at UC Berkeley

Quantitative easing isn't being imposed on an unwitting populace by financiers and rentiers; it's being undertaken, to the extent that it is, over howls of protest from the financial industry.

~ Paul Krugman, Princeton University and Nobel Laureate

The demonization of Wall Street and bankers is very much a function of the press and of Washington [223], and not much more broadly held.

~ John Thain, former CEO of Merrill Lynch

Wage and price controls distort markets...prices are prices...We're not going to monetize US debt.

~ Ben Bernanke, FOMC

Thank the people of AIG for having the courage to do what they did.

~ Robert Benmosche, CEO of AIG

To claim that it's effectively a gift you have to claim that the prices the Fed is paying are artificially high, or equivalently that interest rates are being pushed artificially low. And you do in fact see assertions to that effect all the time. But if you think about it for even a minute, that claim is truly bizarre.

~ Paul Krugman, Princeton

There is a German word, backpfeifengesicht, that reputedly translates to “a face badly in need of a fist.” It seems appropriate for some of these characters, which would generate some serious schadenfreude. For these gentlemen, however, I'll let pop culture respond:

What you have just said is one of the most insanely idiotic things I have ever heard. At no point in your rambling, incoherent response were you even close to anything that could be considered a rational thought. Everyone in this room is now dumber for having listened to it. I award you no points, and may God have mercy on your soul.

~ The Principal in Billy Madison

Personal Debt

I spent all my money on women and wine, and the rest I wasted.
Debt permeates all levels of the global economy. In the U.S., debt is growing much faster than the GDP (Figure 12). A montage of over 50 charts showing all facets of debt is well worth a peek. Authorities are convinced that more spending and more debt will be our salvation. Daniel Bell, a Marxist from the turn of the 20th century, took the other side of this bet, suggesting that the consumer would eventually consume themselves. Apparently, I’m a Marxist. In this section I would like to briefly discuss personal debt. (Special aspects of student and mortgage debt are cordoned off into their own sections.)

Figure 12. Accrued debt with annotations showing dollars of debt required per dollar of GDP (source link lost).

The so-called resilient consumer is getting squeezed from every direction. The income of the average family has dropped from $53,000 to $47,000 in only 5 years. Deleveraging is evidenced by a dropping debt-to-income ratio in Figure 12, yet two thirds stem from defaulted mortgages. The national savings rate has once dropped to zero from historical norms of 10%. Credit card debt is said to be the leading cause of suicide among adult males. Trimtabs reports a 40% drop in net median family worth since 2007.

Should the average family of four earning $47,000 happen to rashly buy everybody iPhones, they just committed 4-5% of their gross income to phone service. I’m not sure even families earning $150,000 should spend that much on phone service. Television and children’s activities used to be largely free; now we pay. Internet, as amazing as it may be, is a necessary expense. Don’t think so? See how your kids do in school without it. Figure 13 shows the ratio of personal consumption versus compensation. That rise stems from a combination of decreased savings and increased debt.
In 2010 I discussed an insidious and overlooked contribution to inflation—accelerated depreciation. It is still overlooked by the mainstream so I am going to take one more abbreviated whack at it. For example, in 2009 I broke a 40-year-old blender. The Boskin Commission\textsuperscript{14} would argue that its replacement is even cheaper than the price tag would indicate because it has more buttons. Government statisticians actually “hedonically” adjust the price down for improved quality. Alas, that really cheap blender died after only two years of dedicated service. Chintzy goods at affordable prices have trapped consumers in a vicious replacement cycle. If Boskin \textit{et al.} had looked at the \textit{per year} cost of the blender, they would have corrected for depreciation with a 20-fold price multiplier before comparing the relative prices of old and new. The net domestic product—the gross domestic product with depreciation included—is an antiquated concept that needs resurrection.\textsuperscript{170} Meanwhile, the consumers are choking on their vomit trying to keep up with depreciation.

\section*{Mortgage Debt}

There is not a menace in the world today like that of growing public indebtedness and mounting public expenditures.

\textit{\textasciitilde Warren G. Harding, former President of the United States}

Harding was considered to be one of the least competent presidents. Could have fooled me. Mortgage debt presents its own unique issues. We are slowly winding down the mortgage bubble that burst in 2007 through a combination of defaults and debt restructurings. To say, however, that a modest uptick in housing activity means that the problem is solved is ridiculous (Figure 14). Is housing recovering? Not really. Maybe sentiment has begun to change but only with the unprecedented force of a central bank behind it.
Figure 14. Home building employment (red) compared with home builder sentiment (blue).

There are still an estimated 11 million homeowners underwater on their mortgages, including more than a million people who have just bought in the past two years.\textsuperscript{171} Ill-advised efforts to bail them out—foreclosures clear the market—seem to have faltered. Special Inspector General of the TARP Neil Barofsky discovered Geithner never intended to aid homeowners, only to delay foreclosures for a year or two so that they could occur orderly. Writedowns are taxable income,\textsuperscript{172} which prevents homeowners from accepting them. Distressed real estate purchased by speculators appears to decrease the housing glut. Unfortunately, this shadow inventory still exists if the speculators intend to flip the houses for a quick capital gain. The market won’t clear until demographics and income growth clear it, both of which are going backwards.

There seems to be some resolution of the catastrophe caused by the Mortgage Electronic Registration System (MERS) in which the ownership of millions of houses are being thrown into legal purgatory by foreclosure. Bank of America supposedly offered to take a deed in lieu of foreclosure, presumably to get the deed legally.\textsuperscript{173} Legally dubious foreclosures are clearing through the legal expedient of turning a blind eye. Efforts in California to use eminent domain to clear out problematic underwater mortgages are so egregious that I have deferred them to the section on Civil Liberties and the Constitution.

**Student Debt**

Bart: don’t make fun of grad students. They just made a terrible life choice.

~ Marge Simpson

You’re f*cked.
Robert Reich, former Secretary of Labor, to Class of 2012

Student loans have soared from $200 billion in 2000 to over $1 trillion today (Figure 15), surpassing credit card debt. Some say there is a student loan bubble, but the Bush-era legislation ensuring that student debt cannot be discharged even in bankruptcy suggests there is no bursting mechanism. Nevertheless, something will give, because loan delinquencies are going parabolic. The paradoxical effect of the full-recourse loans is that banks are happy to provide almost unlimited funding to a slice of society rich in ill-conceived ideas. This debt is also localized in the most financially vulnerable demographic slice during a severe economic downturn. It ain’t just the kids. An estimated $38 billion in student loans are owed by seniors 60 and older, probably stemming from desperate efforts to retool their careers as well as co-signed loans for children and grandchildren.

As if the debt burden was not enough, potential employers are checking credit reports. High student debt can render you unemployable. Seems unfair. The average medical school graduate has $161,000 in student loans. The ultimate irony is that those young doctors on the cusp of achieving the American Dream cannot afford a starter house. Ben Bernanke’s son is said to be $400,000 in the hole. Bernanke is indeed the father of a gigantic credit bubble. Financial independence for twenty-somethings—a rite of passage only a few years back—has become increasingly out of reach.

An entire generation has been set up for debt servitude. We are eating our young. The source of the problem is a complex and nuanced confluence of factors. The chronically profligate boomers, stressed by inflationary pressures and dazed by the equity and real estate downturn, are in no position to help their kids pay for college. The cost of a four-year college education has also soared, while earnings after college have stagnated (Figure 16).

The number of 26-year-olds living with their parents has...
jumped almost 46 percent since 2007. \[182\] [241]

Figure 16. Plot comparing college costs and earnings in early adulthood. \[183\] [242]

What is causing the rapidly escalating college costs? As a professor of 33 years, I can offer a few thoughts and opinions.

(1) College tuition—the cost of running a small city—may be the single best measure of inflation. The tuition growth squares well with the inflation numbers posted by John Williams of Shadowstats.com.

(2) Rapidly growing federal and state mandates to universities escalate bureaucratic costs. You know all those extra positions you see in secondary schools that didn’t exist when we were kids? Universities have them too.

(3) Universities are much more complex, interconnected organizations than they were 30-40 years ago.
(4) The quest to attract the best possible students and faculty has produced something akin to an arms race among the schools, forcing up the costs of chasing the competition.

(5) Universities are financial enterprises that can approach $1 billion annual operating costs and are managed largely by academics often lacking the requisite training. The Dean of Arts and Sciences at Cornell is a physicist—a smart guy by any measure. What prepared him to run a $100+ million enterprise?

(6) Guaranteed payers—banks offering unlimited student loans in this instance—are always inflationary.

I have an aversion to debt jubilees, but I suspect we are heading for a federally sponsored bailout of borrowers and those who traffic in student loans. How do we prevent a repeat of this debt problem? First, a warning: Don’t buy into the increasingly common claims that college is a waste of money. Such blanket statements are counterfactual. One rich dude bribed 100 kids not to go to college.\[243\] Some will be fine but others are going to get hit by the cluster truck. There are, however, many circumstances in which a kid should not go to college.

Students must be good consumers. It’s not just a degree; it’s an education. This means choosing paths wisely and working hard. Not all majors or institutions are created equal; enough said. Debt is a bad idea if it is not self-extinguishing—paid off with the net gain in proceeds from the education. If the kids lack direction or need a break, parents need to let them take time off. You read that right—it’s the parents, not the kids, who oppose the change. Save your money until it will be used wisely. For their part, schools need to focus on strengths and, in many cases, specialize. Paul Smith’s College, a small college in the Adirondack Mountains, is a great example. They educated my older son. His profound success after an inauspicious secondary education stems from the school’s focus—only four, highly pragmatic, majors. What a great model!

How do we fund college educations going forward? I understand the origin of full-recourse loans but find non-dischargeable debt to be anathema to the American system. We’ve got to curb predatory lending; full recourse loans with interest rates and penalties akin to subprime debt is loan sharking. The libertarian in me says \textit{caveat emptor}, yet this is a vulnerable demographic lacking fully developed frontal cortices. The best idea may involve creditors purchasing a percentage of the students’ earnings after graduation for a fixed period (10% for ten years, by example). It’s a form of venture capitalism. I would gladly invest in a tranche of loans to MIT students promising a slice of their earnings—at the right price, of course. For those schools in which the bet is a bad one—the loans are too big, attrition is TOO high, or incomes after graduation are on average too low—the resulting market-determined high interest rates would force change or the institution would fail.

The idea of “no child left behind” would take a beating, but I don’t buy the notion that we need more college-educated adults. We need better-educated adults. Whether this means education in a four-year college or a trade school is highly student dependent. Father Guido Sarducci’s “Five Minute University” has an appeal.\[244\] Another very entertaining parody makes a case for Princeton.\[245\] I would also say beware of law schools. They can be great opportunities but can also be exceedingly expensive holding tanks for college graduates still lacking direction.\[246\]

By the way, would somebody—anybody—start teaching courses in personal finance at the high school and collegiate levels? That void is what got us into this mess in the first place.

\section*{Municipal and State Debt}
This is not a boating accident.

~ Richard Dreyfus in Jaws

The balance sheets of municipalities and states are a total mess. Forbes recently noted 11 states flagged for dangerous finances. It’s not just the sand states that are in trouble. Syracuse, NY is considering a debt restructuring due to excessive expenditures and pension promises. Reuters reported that outstanding bonds, unfunded pension commitments, and budget gaps exceed $4 trillion for the 50 states. That’s approximately $40,000 per taxpayer in the country. Illinois is now $150 billion in the hole, yet the voters defeated legislation designed to stem rising pension costs.

California’s estimated annual deficit rose from $9 billion to a considerably larger $15 billion in a matter of months. California alone owes over $600 billion, with New York coming in a distant second at $300.1 billion. These are self-inflicted wounds. Orange County paid lifeguards annualized salaries of $200K. Hermosa Beach meter maids racked up an astonishing $300K annual salaries. Stockton, San Bernardino, and Mammoth Lakes all filed for bankruptcy protection this summer. San Bernardino City officials sped up the filing to preempt legal action by creditors. Under Chapter 9, all court cases and other legal actions are halted until the bankruptcy case is over.

Rock star banking analyst Meredith Whitney predicted serious financial stresses for municipalities, yet she made the fateful mistake of predicting what and when. The Mayans taught us that you never predict both. At year end, the criticisms have been mounting. With that said, Moody’s is looking to downgrade some California municipal bonds. Buffett picked up a pile of municipal bonds at deep discount during the crisis, presumably using inside knowledge of the Fed backstop that he helped design, only to dump a bunch of these bonds this year. The muni bond story is just getting started.

Corporate Debt

In aggregate, US balance sheets are in very poor shape.

~ Andrew Smithers, CEO of Smithers and Co.

You may have heard recently that…U.S. companies…are sitting on growing piles of cash they are ready to invest in the economy. There’s just one problem: It’s a crock.

~ Brett Arends, MarketWatch

Andrew Smithers and Brett Arends are the only two guys I know who claim that corporate balance sheets are not in good shape. Everybody else raves about the robust corporate balance sheets while focusing on only one side. Corporations are flush with cash and chock full of debt (Figure 17). They are hoarding cash, presumably in anticipation of more credit constraints. The DOW 30 has a net debt (debt minus cash) of $500 billion despite fortress balance sheets by a minority including Microsoft, Cisco, and, if you believe them, JPM. Only 7 of the DOW 30 have net positive cash positions. Pensions of large-cap companies are also significantly underfunded (vide infra). It is estimated that major corporations globally will be refinancing $45 trillion of debt over the next couple of years. None of this suggests strong balance sheets, only generous credit lines.
Sovereign Debt

There are two ways to conquer and enslave a nation. One is by the sword...the other is by debt.

~ John Adams, former President of the United States

There’s always the Federal Government to bail us out, right? Maybe, but we’re in serious trouble. The U.S. debt doubled in only four years (19% annualized). A recent Treasury report indicates that in less than a year we added $2.1 trillion to the national debt. Although it is tempting to point fingers, a screw-up of this magnitude requires a bipartisan effort. The Federal debt and deficit inspired Egan-Jones to downgrade U.S. debt,\(^202\) which then inspired the SEC to investigate them (Egan-Jones, that is).\(^203\) The spendthrifts declare that we had a financial malaise to deal with. I wonder if history will look favorably on a Keynesian experiment in which we injected $1 million of government stimulus for each newly created job.\(^204\)

It is estimated that we are collecting only 60 cents of every dollar spent by the Federal government. This is not the beginning of the end of some debt frenzy. It is the end of the end. *Who is buying all this debt?* Funny you should ask. The Fed is buying 60-80% of it. *How do we afford it?* Oddly enough, the Fed...
controls the interest rate on federal debt. Uncle Sam has an unbelievably cushy line of credit thanks to Fed largesse. The whole Fiscal Cliff debate illustrates that austerity is too inconvenient to deal with right now. We can worry about tightening the belt later. But this secular bond bull market is very long in the tooth. At some point rates will rise just like night follows day. Each 1% rise in rates on $16 trillion dollar debt adds an additional $160 billion to our interest rate payments.

*What if we just really suck it up?* Seriously. What if we go to the extreme by dropping all discretionary spending? No more military, highways, education, parks, etc. and pay only the interest on the debt and other payments mandated by statute. *We still fall short of a balanced budget.*

For those confused about the Clinton-era balanced budget, it was a hoax—we had gobs of off-balance-sheet expenses putting us in the red. The reported deficit is the innocuous part. If one looks at unfunded liabilities—promises made to the populace for which we haven’t a clue where the money will come from even *after projected tax revenues are included*—we are in huge trouble. Years ago, Kotlikoff, Burns, and Smetters estimated $44 trillion of unfunded liabilities. Kotlikoff is now estimating over $200 trillion—40 *Krugmans!* (1 Krugman = $5 trillion)

That comes to an IOU of $2 million dollars per viable taxpayer. So let’s not trivialize this issue by suggesting that this will hurt our grandchildren. As far as I am concerned, they are on their own. This is gonna crush you and me.

**Pension Crisis**

Demography is like a glacier: It doesn't move fast, but it is very predictable...it's inexorable.

*~ Neil Howe, author of The Fourth Turning*

We have a massive, multi-dimensional pension problem. Let’s begin with a look at the personal pension plans most commonly associated with 401K plans and related IRAs. Optimistic retirement planners at Fidelity recommend socking away 8x annual income by retirement. That's not enough. More conservative estimates reach as high as 20x or even 25x your annual salary in savings. Further problems stem from the bond market, which approximates 40% of all retirement portfolios. In the downturn, huge gains in principal mitigated the pain of the equity losses. The best-case scenario going forward is that rates stay low forever, resulting in miniscule cash flows and no loss in principal. The more likely scenario is that interest rates rise and prices drop causing significant losses in principal. There is no slack left. Reaching for yield buying sketchy forms of fixed income is likely to be a road to ruin. Bold assumptions of 7-8% annual returns on pension portfolios will require double digit equity gains. Buffett and anybody else actually paying attention, however, will tell you that *dropping* rates, not low rates, helps equities.

Only the legalize-marijuana crowd on CNBC believes rising rates will not hurt equity returns.

Let us look at what is nearly a best-case scenario, a family in the top 5th percentile—the 5 percenter. This family is defined as earning $154,000 and a net worth of $1.2 million, which, by coincidence, is about an 8-fold ratio of savings to annual earnings. A couple at the demographic heart of this 5 percenter also is likely to be a late stage boomer on the doorstep of retirement. Way to go, Fidelity! Using assumptions based on standard portfolio theory and grounded in legally mandated IRA withdrawal rates, the 5 percenter should withdraw only 4% to ensure the money lasts—$48,000 per year. This is a problem. I’ve got to imagine that a 5 percenter is going to find a 50th percentile cash flow in retirement austere. The *average* boomer with a net worth of $180,000 spinning off only $7,000 per year is within an error bar of living on Social Security. 40% of the boomers literally will have only Social Security.

What about all those folks with defined benefit plans? First, defined benefit plans are becoming
anachronistic, having been abandoned years ago by companies unwilling to shoulder the risk. Nonetheless, 341 of the 500 large caps in the S&P have retained some semblance of a defined benefit plan.\textsuperscript{212} It is also estimated, however, that the pension plans in 97\% of these companies are underfunded.\textsuperscript{213} A paper by William R. White out of the Dallas Fed estimated that the 1,500 leading companies in the U.S. have a 30\% pension deficit of $689 billion.\textsuperscript{162} Despite the Pension Protection Act passed in 2006 aimed at protecting workers against companies using pension pools as cookie jars to boost earnings, the crisis in 2007 and affiliated lobbying campaigns convinced law makers that such protections were too inconvenient.

The municipal and state pension problems are acute. The Illinois State Pension Fund is currently 40\% underfunded; there is no obvious way out of their hole short of a Federal bailout. Some states are topping off their pension plans by borrowing money from…wait for it…their state pension plans! Read that last sentence again.\textsuperscript{214} Fully funding the state pensions would cost >$30,000 per taxpayer.

There is no guarantee that the defined benefits plans will survive. Chapter 11 corporate debt restructurings and Chapter 7 liquidations will continue to chip away at this liability. The Chapter 7 liquidation of Hostess and ensuing Twinkie riots—at least I rioted—leaves some wondering what kind of union-management stalemate could drive a company into bankruptcy. The 2,500 workers lost it all. Chapter 9 bankruptcies for restructuring municipal debts and negating pension commitments, unheard of only several years ago, are likely to become well known.

Unimaginable ink has been spilled discussing and analyzing the coming Social Security crisis. It’s an off-balance-sheet Ponzi scheme. Social Security also will be increasingly important as the other support mechanisms fail. With cooked inflation numbers and affiliated inadequate inflation adjusted payouts, it’s easy to imagine seniors getting stiffed.

**Roth IRA: A Bad Idea**

Cost of living now outweighs benefits.

\textit{~ Headline from The Onion}

Before leaving the world of pensions I’m gonna pick a fight with Roth IRAs. When the Roth IRA was first announced I had a unique—as in only-guy-on-the-planet unique—visceral response. The original IRA was very farsighted: Savers were allowed to compound wealth unfettered by taxes while the government deferred tax revenues to future generations. By contrast, the Roth IRA pulled tax revenues forward, leaving future generations to take a hike. Imagine the truly awesome demographic problems we would have if the Roth had been introduced in the 60s and the entire baby boom generation became entirely tax exempt. Was this an oversight? I don’t think so. The introduction of the Roth and the substantial revenues from regular-to-Roth rollovers coincided with the Clinton administration’s efforts to balance the on-balance-sheet Federal budget for the first time in decades.

That is my minor gripe. To set up my really big gripe we must first dispel a widely held misconception and a common oversight.

(1) In a regular IRA, the money is taxed at the end, whereas in a Roth IRA taxes are levied up front. If the two are taxed \textit{at the same rate}—this is a \textit{critical} provision—the outcome is \textit{identical}. They are not just similar, it’s an identity. Break out your calculator if you must. There is no differential advantage offered by compounding in the Roth over the regular IRA. Simply put:

\textit{Any advantage of the Roth IRA relative to a regular IRA necessarily stems from a lower tax
rate while working than in retirement. Period/full stop.

(2) The tax rates of the Roth and regular IRAs are fundamentally different:

Roth IRA: Front-end loaded taxes paid at the *marginal* tax rate (highest tax bracket).

Regular IRA: Back-end loaded taxes paid at the *effective* tax rate (integrated over all tax brackets).

The distinction of marginal versus effective tax rate is critical and seems to be lacking from most analyses. One can calculate marginal and effective rates for any income online.215 Let’s return to the top-5-percentile family—the 5 percenter. If they had used a regular IRA, they would be paying a 7% *effective* tax rate incurred on their $48,000 per year withdrawal in retirement. They paid an approximate 32% *marginal* tax rate—the tax rate at the top bracket—to shelter a few thousand per year in a Roth IRA. The numbers simply do not work.

It is worse than that. Let us consider the lucky soul family—the extraordinarily rare couple—who actually accrued 25 annual salaries in their retirement account. For this family a 4% annual withdrawal will be equal to an annual salary while working, placing them in the same tax bracket (ignoring unknowable tax law changes). Even so, they paid 32% marginal tax on the Roth to avoid a 22% effective tax rate incurred by the regular IRA. The numbers *still* don’t work. I do not understand why the Roth is being sold so enthusiastically to the public.

Now ponder all those folks who rolled over a lump sum from a regular to a Roth IRA. They not only paid the marginal tax rate on the rollover but caused the marginal rate to spike to a higher level! It’s hard to imagine that will prove to be a smart move. Congress is considering moving all pension funds to what is effectively Roth IRA rules as part of their Fiscal Cliff negotiations.216 You young guys are about to get hosed.

**Europe**

*The ECB is going to buy bonds of bankrupt banks just so the banks can buy more bonds from bankrupt governments. Meanwhile, just to prop this up the ESM will borrow money from bankrupt governments to buy the very bonds of those bankrupt governments.*

~ Kyle Bass, CEO of Hayman Capital

Watching Europe is like reading *Waiting for Godot*—it is unintelligible. This is unfortunate because these folks may determine my fate. The problems begin with the PIIGS—Portugal, Italy, Ireland, Greece, and Spain—suffering from insolvency. We were assured that the Maastricht Treaty and Haagen Dazs Accord that spawned the Euro explicitly forbade deficits and bailouts.217 Well that was then and this is now. Christine Lagarde, head of the IMF, held a press conference literally flashing a big, black purse suggesting that it needs some serious money, and—Shazam!—a €700 billion bailout was in place before the weekend was over. Soon there were trillion-euro bailouts with fuzzy names such as Long-Term Refinancing Operation (LTRO), European Stabilization Mechanism (ESM), European Financial Stability Facility (EFSM), and Monetary Injection Liquidity Fund (MILF). Spiking interest rates of the PIIGS were driven down to levels that look like AAA-rated debt of Pfizer and General Electric. The European Commission (EC), International Monetary Fund (IMF), and European Central Bank (ECB)—the so-called Troika—are the enforcers. The banks get what the banks want.

A Greek exit—shortened to Grexit by Willem Buiter—would have created a fiscal crisis as well as an
acronym crisis—PIIS. We endured an insane discussion about whether or not Greece should suffer austerity.²¹⁸ [²⁷⁷] Versus what? Rich, prosperous, and productive? The only legitimate employment was hawking gyros to rioters. A photograph of the Greek Ministry of Finance showing total chaos went viral, becoming a metaphor for the nation.²¹⁹ [²⁷⁸] Nobody got the memo: Austerity is not a choice; it’s a result. Any banker who lends to Greece will be the author of his own (and our) misfortunes. Iran stopped shipping oil to Greece. Just when Greece appeared to be plumbing the bottom, they suffered a locust attack—a real one.²²⁰ [²⁷⁹] Greece is the smallest pawn on the chessboard and with little bargaining power. They were asked to sign a bailout agreement with deep-seated sovereignty issues, yet the document was written in a different language with an incomplete translation.²²¹ [²⁸⁰] However, the Greek default could cost the banks trillions, and the Greeks know this.²²² [²⁸¹]

The bailouts are coming from Germany because everyone else is on the receiving end. Yet, with an economy 20% the size of the U.S. economy, the Germans are trying to prop up a gaggle of countries that are collectively bigger than the U.S. economy. Europe has $30 trillion unfunded pension liabilities. It’s not going to work. Discussions of why the Americans should bail out Europe—even more than the hundreds of billions of QE II that ended up in European banks—led to a classic Santelli-Liesman love-fest on CNBC.²²³ [²⁸²] The banks get what the banks want.

Soon Spain began to slip into the abyss,²²⁴ [²⁸³] something I had been waiting for since 2009. [³] Shockingly, Mariano Rajoy, Prime Minister of Spain, declared, “We support a rescue mechanism, the bigger the better.”²²⁵ [²⁸⁴] It was all part of a shakedown of the EU, and it seemed to work. Money began flowing into Spanish banks. (Bankia actually got a bailout before the bailouts officially began because they couldn’t wait.)²²⁶ [²⁸⁵] Spain put a €2500 cap on cash transactions,²²⁷ [²⁸⁶] which is emblematic of an end game. Meanwhile, Spain is bidding for the 2020 Olympics. They will be sponsored by Lowenbrau.²²⁸ [²⁸⁷]

Then came the Italians. Bill Gross noted that “Italian banks are now issuing state guaranteed paper to obtain funds from the European Central Bank (ECB) and then reinvesting the proceeds into Italian bonds, which is QE by any definition and near Ponzi by another.” The oldest bank in the world, Banca Monte dei Paschi di Siena founded in 1472, got bailed out. I wonder how many times that has happened in the last 540 years.²²⁹ [²⁸⁸] The wheels of justice in Italy were moving forward; they convicted scientists for failing to predict an earthquake.²³⁰ [²⁸⁹] The guys who cause earthquakes are still on the lam.

What happened to the assurances of the Maastricht Treaty that no sovereigns would be bailed out? It seems simple enough to me. Politically disconnected sovereign states are strongly shackled together by a common currency and borderless multinational banks. Why would the politicians in the sovereign states agree to self-destructive austerity deals rather than giving them the Icelandic Salute—a default and the finger? That’s easy, too; the banks own the politicians, probably via Cayman Island subsidiaries. (In the olden days, it would have been the Swiss, but their money-laundering ways are at risk.)²³¹ [²⁹⁰] One of the many subplots is a mountain of credit default swaps that would break the banks if they were triggered.²³² [²⁹¹] No problem: The banks refuse to declare the credit event. The banks get what the banks want.

The LTRO is particularly insidious because it subordinates existing debt, inducing a bad case of transurphobia (fear of haircuts). The more LTRO money, the less capital remains backing the existing debt.²³³ [²⁹²] Which legal body gets to make this decision? That’s what the Troika is for—democracy not included. These guys are undermining the debt markets in fundamental ways.

The 2012 Nobel Peace Prize was awarded to the European Union,²³⁴ [²⁹³] rumored to be for “keeping
their shit together” and for “displaying an unprecedented willingness to not start another world war.” The great part about this wave of absurd Nobel Peace Prizes is that, in theory, I could get one—a dollar and a dream.

A World Economic Forum (WEF) report says we must double global debt by 2020 (to $210 trillion) to keep the global economy growing.\(^{235}\) If that’s the price, shrinkage is sounding pretty rational. The killer phrase was that “most of the growth will come from the government segment.” That ain’t economic growth.

Let us not forget the troubles in the UK. Goldman announced that they were installing one of their boys (Mark Carney) as head of the Bank of England, prompting David Stockman to ask, “Is there any monetary post in the world not run by Goldman Sachs?”\(^{236}\) UK family debts are up by almost 50% in a year. That is serious slippage. The Bank of England cranked $140 billion into the system in one day—equivalent to 177% of the annual global gold production.\(^{237}\)

The Brits \textit{et al.} are eating a lot of “toast sandwiches,” otherwise known as the "austerity sandwich”—two slices of bread wrapping a piece of toast (butter/salt optional).\(^{238}\) Irish taxpayers withheld property taxes in protest to the Troika. This smacks of a “peasant rebellion” claiming taxation without representation. With this history ringing in his ears, Sir Mervyn King, Governor of the Bank of England, noted, “I have deep sympathy with those who are totally unconnected with the origins of the financial crisis who suddenly find that the returns on their savings have reached negligible levels. These are consequences of the painful adjustment prompted by the financial crisis and the need to rebalance our economy.”\(^{239}\) We feel your pain too, Sir Mervyn. Can I offer you a toast sandwich?

The whole mess has been summarized and bulleted by countless bloggers. A few are worth reading.\(^{240}\),\(^{241}\) Credit Swiss noted that “Portugal cannot rescue Greece, Spain cannot rescue Portugal, Italy cannot rescue Spain, France cannot rescue Italy, but Germany can rescue France.”\(^{243}\) Of course, in February Baghdad Ben Bernanke noted that "the ECB is well capitalized."

**Asia**

Asia is, by comparison, a relatively serene place. There was a seemingly ominous event when the Bank of Japan was said to be selling its bonds (JGBs) for the first time in years.\(^{244}\) This smelled like the beginning of a large deleveraging. Recent reports suggest that they are back to monetizing debt in a big way.\(^{245}\) Some bears such as Greg Weldon, Simon Johnson, and Kyle Bass view Japan as ground zero for financial carnage.\(^{246}\),\(^{247}\),\(^{248}\) Japan has spent 20 years losing 80% on the Nikkei—the so-called “lost decade” to those who can’t count—and now the carnage begins in earnest? Losing all of their nuclear reactors also seems ominous; I am guessing they were not using them as backup sources.\(^{249}\) Demographically, their population will continue to age for decades. This is not a pretty picture.

There are others who think China will be the source of fireworks. On the bearish side, you have Jim Chanos placing some serious shorts in position.\(^{250}\) You must take this as a serious omen. The average bloke does not understand the thoroughness of analyses by guys like Chanos and Einhorn. (Chanos, for example, was way ahead of all of Hewlett Packard’s auditors in detecting an $8 billion screwup in their purchase of Autonomy.\(^{251}\)) Besides a bloated real estate market and terrible bank balance sheets, China is said to have a huge buildup of finished goods—channel stuffing—which will cause trouble at some point.\(^{252}\) This is consistent with often-cited suggestions that the authorities are
terrified of unemployment and accompanying social unrest. On the other side, Stephen Roach and Jim Rogers, both highly respected market watchers, are rather enthusiastic about China. Years ago Rogers predicted strife in China would come to a head, and that would be the time to buy. I am quite confident, however, that I have no prayer of understanding China either now or in retrospect.

The Baltic Dry Index[^253] is a widely followed indicator of global economic activity (Figure 18). As you can see, the global economy is looking a little green around the gills.[^254]

![Baltic Dry Index Chart](http://www.peakprosperity.com/print/80283)

Figure 18. Baltic Dry Index as an indicator of global economic well being.[^254]

I leave this section with an aside that is too curious to ignore. We were told this year that Japan had unwisely dumped $138 billion into Lehman before the company’s collapse and were promptly reimbursed by the Fed.[^255] Makes you wonder about those two Japanese businessmen caught crossing the Italian border with $134 billion of Treasury bonds.[^256] The Treasury denounced them as fake, but the Italians thought they were real. Who could launder them? (Silly question: HSBC would gladly do so for a cut.)

**Government Corruption**

Geithner heard this information and looked the other way. Geithner and other regulators should be held accountable, they should be fired across the board. If they knew about an ongoing fraud, and they didn't do anything about it, they don't deserve to have their jobs. I hope we see people in handcuffs.

~ **Neil Barofsky, Special Inspector General of TARP**

What we’re showing here is that cronyism is now permeating our justice system.

~ **Peter Schweizer, author of* Throw Them All Out***

2012 witnessed plenty of government corruption. It is my thesis that corruption within government is getting worse for three reasons: (1) government is a larger percentage of our peacetime GDP than in any other time in history, (2) thanks to the Supreme Court, unlimited funds flooding into election cycles drown out all other interests, and (3) profound financialization of the economy—movement of money for the
sake of money—due to unprecedented Fed interventions and deficit Federal spending aggregates
criminal elements and elicits criminal behavior. To put it simply, the crime syndicates all had IPOs.
Almost without fail the punishments for white-collar crime—really substantial graft—are a small
percentage of the booty obtained from the crime. Failures to investigate and prosecute men of wealth
and power are emblematic of a kakistocracy—government by the most unprincipled.

Attorney General Eric Holder was up to his ears in dirt. Holder’s law firm defended Corzine against
prosecution by Holder’s Department of Justice.257 [316] The law firm won that battle. This was the same
Eric Holder who was charged with contempt of Congress for not forking up information about the “Fast
and Furious” Mexican arms deals.258 [317] This was the putative sting in which Federal agents sold arms
to Mexicans to track the arms but somehow forgot to include tracking devices. Congress also appears to
have forgotten to follow up on the contempt charge. I asked Peter Dale Scott, a UC Berkeley
octogenarian and multi-decade scholar on the politics of drug cartels, if he knew what the real story was
behind Fast and Furious. He assured me that “there is something very wrong with the picture and the
official explanation for it.” Oddly, the investigation into the arms deals was terminated by...you guessed it,
the Obama Department of Justice.259 [318] That would be Eric Holder.

The authorities continue to cauterize the wounds from the mortgage fiasco by out-of-court settlements
with banks, allowing no admission of guilt, no criminal prosecutions, and cash settlements representing
small fractions of the profits. (I get in more trouble for leaving the seat up.) We thought the authorities
finally levied a severe fine on the banks and brokerages with a sizeable $25 billion settlement for
fraudulent foreclosures, only to find that most of the money—all but a few billion dollars—came from the
bailout money and even their own write-downs of losses on defaulted mortgages.260 [319] Dean Baker
notes that Obama gave bankers immunity from prosecution, and in return, bankers agree to accept
government money to cut mortgage principle.261 [320] Everything but the reduction in mortgage principal
came to pass.

Although this is not easily prosecuted corruption, the racketeering (RICO) laws seem appropriate. To
clarify, I am recommending RICO laws be used on the government officials who participated. Even the
document that represented the attorneys generals’ settlements with the banks was shown to be
fraudulent.262 [321] The New York Times reported that money intended for homeowners in the fraud
settlement, as little as it was, got diverted by the states into general operating funds.263 [322]

Walmart got caught bribing Mexican politicians to foster their business interests South of the Border.264
[323] Somebody bribed the Mexicans? Shocking indeed. This does not happen in the U.S. because we
have registered lobbyists. Those same lobbyists will ensure that Walmart’s transition to redemption is
seamless.

The SEC, to evade a Freedom of Information Act (FOIA) suit, expunged data pertaining to Citigroup as
part of their catch-and-release program.265 [324] Citigroup is protected by the Rubin mafia. This is politics
Geithner Style. It will be interesting to see where the starting lineup for Team Obama ends up after they
finish their first term. The FOIA by Bloomberg showed how the revolving door totally commandeered the
Dodd-Frank act to make sure it was banking-friendly.266 [325] The average salary boost on passing
through the government-Wall Street revolving door is estimated at 1400%.267 [326] I’m sure that top dogs
like Geithner will do considerably better. Don’t let the revolving door hit you guys in the butts.

Another proud moment for the Obama administration’s push for alternative funding energy: Electric car
battery maker Ener1, which received more than $100 million in government handouts, has filed for
bankruptcy protection.268 [327] I’m beginning to suspect cronyism here! Peter Schweizer’s book Throw
Them All Out (vide infra) documented in repulsive detail the shovel-ready cronyism that occurred during the financial crisis.

There were old-school politics going on when Mississippi Governor Haley Barbour left office. On his way out the door he pardoned a number of seedy characters, including eight men convicted of killing their wives or girlfriends.269 [328] The Mississippi Supreme Court upheld the decision. In Mississippi, the Rule of Law is a bad joke, and True Blood is a documentary. We have, however, not plumbed the level of the Thai politicians. A Thai senator shot his secretary with a machine gun in a restaurant and got a $625 fine for it.270 [329] Very Cheney-esque.

If you want some fun, find the Clinton pardons. The original list I saw had over 1,100 and was easily located. The list was laced with drug busts and bank frauds. I can only find partial lists now. Even so, the number who were in prison for drugs or some form of bank fraud is striking.271 [330] This would partially explain how Clinton left office burdened by onerous legal fees and now has an estimated net worth of $80 million.272 [331] That’s a lot of honoraria for rubber chicken dinners. Tony Blair also seems to have laundered serious money into shell companies.273 [332]

State Supreme Court judges run for office in 38 states. Jeffrey Toobin warns us that the lobbyists discovered them in the mid-90s and are diverting some of their resources.274 [333] In 1990 candidates for state supreme courts only raised around $3 million…in the races to the high courts, candidates now raise more than $50 million.

The government sold $5 billion worth of AIG stock acquired during the bailouts. AIG bought $2 billion of it, presumably using money from government bailouts. AIG was shockingly profitable owing to $17 billion of tax credits (gifts by the taxpayer).275 [334]

Harvard had a publicly embarrassing cheating scandal in which over a hundred kids in one course were accused of plagiarizing. What course would warrant such bad behavior? Introduction to Congress.276 [335] I’m sure the kids will do better in their Introduction to Ethics in their MBA programs.

Recall the must-see Miami Vice episode entitled, “Prodigal Son?”277 [336] Tubbs and Crocket trace the drug money straight to a wrinkly old banker who explains that the drug money ensures payment of South American bank debt. I remember at the it time that made sense, and it seems haunting now. It is rumored that Mr. Burns in the Simpsons was modeled after the Miami Vice banker.

Civil Liberties and the Constitution

There is very grave danger that an announced need for increased security will be seized upon by those anxious to expand its meaning.

~ John F. Kennedy, former President of the United States

There may be a number of people who cannot be prosecuted for past crimes, in some cases because evidence may be tainted, but who nonetheless may pose a threat to the security of the United States.

~ Barack Obama, President of the United States

One of my favorite bloggers, Charles Hugh Smith, cogently summarized instances in which incarceration was used to protect democracy and civil liberties.278 [337] How ironic. Doug Casey provided a haunting
account of creeping fascism in Germany in the ‘30s and how it occurs incrementally.\textsuperscript{279} It is an easy case to make that we are in a battle to preserve civil liberties simply because every year is a battle to preserve civil liberties. Civil liberties are forfeited one at a time. The battle lines are being drawn. You should fight every fight, no matter how big or small.

There is an ongoing battle for ultimate control of the Internet. Legislation includes the Stop Online Piracy Act (SOPA), the Protect IP Act (PIPA), and the Anti-Counterfeiting Trade Agreement (ACTA).\textsuperscript{280,281} Superficially they are designed to achieve the named goals. The notion is that pirating sites can be blocked if they are interfering with trade. Their reach, however, is far greater. An accusation alone is sufficient to block a web site prior to any clear evidence of guilt.\textsuperscript{282} Authorities could shut down search engines Yahoo, Google, or Bing suspected of \textit{enabling} these hooligans. SOPA got shelved after there was, ironically, a massive Internet-derived protest. The digital world has taken our lives by storm. The Internet is as profoundly democratic as Gutenberg’s printing press. Keep it wide-open at all costs. Efforts to control information flow will keep appearing like the proverbial camel nose under the tent. And here comes the next one on cue in 3…2…1…enter the Trans-Pacific Partnership (TPP)!\textsuperscript{283}

The implications of armed drones are staggering. We are not the only country with drones; they are proliferating around the globe. We managed to survive thermonuclear risk for half a century, and yet we find ourselves racing toward a Skynet-like drone war of staggering magnitude. The skies will be littered with drones like aerial minefields. It is terrorism to those on the receiving end, causing blowback to be almost a certainty. Congress passed a law opening U.S. skies to unmanned drones.\textsuperscript{284} Companies are lining up to launch them—an estimated 30,000 drones within a few years—forming a nouveau industrial-military complex. As a guy who finds automated speed-monitoring devices irritating and automated ticketing profoundly disturbing, the drones make me crazy. Even if unarmed, is this not Constitutionally prohibited unlawful search? What event will elicit armed variants to protect us from the bad guys? And if all that isn’t spooky enough, the drones are being engineered for autonomous (human-free) response.\textsuperscript{286}

Digital monitoring of “crimes against traffic” frees up police for more hands-on police work. Petty arrests now justify strip searches. \textit{The Economist} describes increasing predilections toward stop-and-frisk policies within the cities.\textsuperscript{287} Legal scholar Jonathan Turley estimates that over 700,000 unwarranted stop-and-frisk searches occur each year in NYC alone.\textsuperscript{288}

Jonathan Turley also notes that the Administration claims the right to assassinate a U.S. citizen either here or abroad, and it would seem that we did such a thing.\textsuperscript{289} Of course, the target deserved it because he undermined America! The FBI has described extremists as those who “may refuse to pay taxes, defy government environmental regulations, and believe the United States went bankrupt by going off the gold standard.”\textsuperscript{290} Y’all should be careful because you never know what is flying 50,000 feet right above your heads. Obama is the only Nobel Peace Prize winner with a kill list. God save the poor soul spotted by drones entering Manhattan with a Big Gulp. Mayor Bloomberg’s war on Big Soda could turn violent.

Sergey Aleynikov was arrested in 2009 for the most egregious of crimes—stealing software from Goldman Sachs. The Goldman Stasi are good at their jobs, getting him into custody within hours. In 2010, he was convicted and sentenced to 8 years in jail for this profitless crime despite the probation office’s recommendation of 2 years.\textsuperscript{291} The system seemed to correct itself when the \textbf{United States Court of Appeals} threw the case out in 2012, ruling the source code was not a "stolen good."\textsuperscript{292} It was a pyrrhic victory for Aleynikov. They arrested him again using a different jurisdiction to avoid double jeopardy.
Joshua Dressler, a criminal law professor at Ohio State University [353] said that “it was highly unlikely that the separate Federal and state prosecutions in the Aleynikov case would violate the Constitution.” I think they just did. At least now Sergey doesn’t have to start his car in fear.

The National Defense Authorization Act (NDAA) was enacted to protect us against terrorists. 294 [354] Of course it was. It provided government authority to incarcerate an American citizen indefinitely without access to legal defense or the courts. Protestors challenging the unlawful incarceration were (you got it) arrested. 295 [355] In September, a Federal judge ruled it was not even in the same zip code as the Constitution and put a permanent injunction to protect us. 296 [356] Here’s the really troubling part: It had been passed by a large majority in Congress and a 91:9 vote in the Senate, and signed by President Obama. When the outcry began in earnest, Obama assured us that his administration would never act recklessly. I beg to differ: Signing the bill was reckless. I’ll take it a step further: Signing the bill was treason. Read your job description, Mr. President. Watch for that part about upholding the Constitution. And by the way, Team Obama is fighting the injunction. 297 [357]

There is little doubt that municipalities in the sand states would do almost anything to dig themselves out of the mortgage crisis. The brain trust in San Bernardino, with the legal help of one of my colleagues (Professor Robert Hockett) got the idea to use eminent domain to commandeer underwater mortgages—mortgages that exceed the value of the house. 298 [358] The idea is to pay “fair value” (red flag!), bundle them up (red flag!), and sell them to private investors (red flags!). There would be no shortage of cronies willing to buy up these bundles. The subplot might be that this is a veiled attempt to clean up the MERS boondoggle that is causing foreclosures to throw the title of houses into a legal vortex. As preposterous as this sounds, it’s probably Constitutional given the eminent domain case in Connecticut that some believe drove Sandra Day O’Conner to retire from the court. 299 [359] It may, however, be illegal in California. 300 [360]

The Citizens United suit gave Super PACs their unlimited political power by allowing them to spend unlimited money on political campaigns provided they follow a few guidelines. 301 [361] Journalist and civil servant Jim Hightower referred to the majority justices as "five traitors to the democratic ideal." It is indeed odd that support for freedom of speech may have profoundly oppressed free speech. A banking Super PAC overtly promoted by American Banker is blood curdling in its goal to defeat any candidate that is not friendly to banks. 302 [362] A suit to ban excessive donations in Montana got nuked. 303 [363] According to the Supreme Court, money is speech. As a corollary, if you don’t have money, you will lack a voice.

Corporate civil rights seem to be in the news. An Occupy Wall Street (OWS) protestor carried a sign, "We will know corporations are people when Texas executes one." It seems clear that corporate civil liberties without civil responsibilities is a problem. It is not true, however, that this was a recent or rapid change. Organizations began to accrue Constitutional protections beginning with a case of Dartmouth College versus the State of New Hampshire in 1819. Ted Nace’s Gangs of America tracks through the Supreme Court decisions that incrementally granted civil liberties to corporations. Despite the hyperbolic title, it is a balanced, scholarly analysis.

Why are civil liberties eroding? One notion is that tension between the central planners and free market crowd led to a societal compromise in the 1930s. Capitalism was allowed to flourish, but with safeguards to keep communistic ideals in check. With the fall of the Berlin Wall and the Soviet Block, the proletariat (in the U.S., that is) had no alternative system to keep powerful individuals mindful of their needs. Glass Steagall fell in the late 90s, the banking cartels grew, and wealth disparity—financial apartheid—emerged.
Limits of Government

A sinking economy requires stimulus from two agents, the Federal Reserve and the government.

~ Rich Yamarone, Director of Argus Research

During the time of the Soviet Union the role of the state in economy was made absolute, which eventually led to the total non-competitiveness of the economy…I am sure no one would want history to repeat itself.

~ Vladimir Putin, communist

We have witnessed a seemingly endless battle for the Grand Compromise between those supporting central planning versus market forces. 18th century economist Edmund Burke warned of the role of intellectuals trafficking in snark and trumpeted the Law of Unintended Consequences. Burke also recognized the wealth disparity in 18th-century France and accurately predicted the murderous end result. 19th-century economist Alexi de Tocqueville described the genius of America as not the equality of outcome but rather equality in the eyes of the law. 20th-century economist Joseph Schumpeter also viewed intellectuals with disdain and capitalism not as flawed but fragile. Friedrich Hayek, famous for his opposition to John Maynard Keynes, supported the notion of social safety nets, just not so many and not so invasive. I think Hayek’s stroke of insight was recognizing significant analogies with Darwinian evolution to understand that complex systems arise and persist more by trial and error than by explicit human engineering. Hayek’s *Fatal Conceit* describes the folly of intellectuals thinking they are smart enough to mess with free markets, hoping to obtain only intended consequences. My reading of Keynes is that he was a profound interventionist—a knob twirler—and was also a radical socialist.

The Yamarone quote illustrates that we have degenerated to a society in which even the big money guys—supposedly the bright bulbs—think that government will solve our problems. While watching a Yale panel discussion on the economy, I was struck by the explicit endorsement of government solutions by the panelists. Apparently, we are all Keynesians now. I could buy into a variant of the Keynesian model in which government acts as a financially interested party, buying goods and services when they are cheap and pulling back when they are expensive. It would naturally be counter-cyclical. Unfortunately, there is no chance it will ever work that way. Paraphrasing my dad who was paraphrasing Milton Friedman, government does everything inefficiently, so don’t ask them to do more than you must. It’s not about the morality of what government does; it’s about the low quality and horrendous inefficiency.

Hernando De Soto warns that the U.S. is forfeiting a critical feature that distinguishes it from Third World countries—well-defined property rights. The MERS catastrophe that threw the title of millions of properties into question was an 80-car pile-up on a foggy freeway that will be corrected by legal fiat. By contrast, mutation of the banking system into a cartel, while by no means unprecedented, is a serious problem. Now that this gargantuan organism has control, there is no means to wrestle it back. When you can purchase a politician for $100,000, how can we expect real change? The Citizens United case that opened the political process to unlimited capital is profound because attempts to unring that bell are opposed by unlimited capital. The power of the banking trusts has gone beyond the failsafe point. The Fed—the One Ring that controls them all—is the key. It will be a long trek to the Crack of Doom.

Challenges to our civil liberties, overreach of eminent domain, domestic drone surveillance, and attempts by elected officials to knowingly subvert Constitutional rights all attest to the insidious Orwellian creep of government into our lives. It is not obvious to me that we can negotiate our way out of this one. Some problems do not have solutions if you define a solution as a fix with tolerable pain. I suspect that
resolution will occur, but it will be something historic. We are in a barrel speeding down the Niagara River toward the Falls. This is not an episode of *Batman* or *McGyver*: all palatable solutions have passed. We will experience the Falls up front and personal. Those in power will claim they did their best when, in fact, they were the root cause. Bernanke, one of the reputed world’s experts on the Great Depression, never mentions loose monetary policy in the 1920s as the cause. It is a lie by omission; a profound one at that.

I close with a simple directive: Watch Ron Paul’s farewell speech to Congress. You owe it to yourself. He’s the one that got away. To paraphrase Marlon Brando, “He coulda been a contender.” If you’ve had enough of darkness, try this John Cleese seminar on creativity—it’s brilliant—or this photo montage of history’s most epic photos. Soon I will be off like a prom dress, but first I wish to share the books that I read this year, and the all-important acknowledgements.

**Books**

Every year I summarize books that I read. I am a slow reader so I try to chose them carefully. I’ve overdosed on crisis books for over a decade (beginning with *crisis foreshadowing* books) but succumbed to the temptation a few more times. I also slipped back into pop psychology mode.

*The Clash of Economic Ideas: The Great Policy Debates and Experiments of the Last Hundred Years* by Lawrence H. White

White describes the debates that took place throughout the 20th century, pitting the free market advocates against the central planners. Although White shows his colors as a free marketeer, he does a beautiful job of letting the reader ponder the debate rather than force-feeding the conclusion. The book might not be wonky enough for the pros, but I found it to be very scholarly—a great book for a wide swath of macroeconomic enthusiasts. This is the stuff economists-in-training seem to miss in modern curricula. I took the plunge prompted by an Econtalk interview of the author.

*Broken Markets: How High Frequency Trading and Predatory Practices on Wall Street are Destroying Investor Confidence and Your Portfolio* by Sal L. Arnuk and Joseph C. Saluzzi

I don’t really know Sal Arnuk but am a big fan of Joe Saluzzi, occasionally swapping barbs about the horrendous price discovery process in modern markets. Joe and Sal describe in detail how high frequency traders are eroding the foundations of the markets—not just equity markets—through their relentless game of high-frequency Whac-A-Mole. Although Sal’s and Joe’s knowledge of the markets and passion for change is uncontestable, their frustration at times overwhelms the prose. I recommend the book, but some enthusiasm for trading may be required to nudge this book into the five-star group.

*Bull by the Horns: Fighting to Save Main Street from Wall Street and Wall Street from Itself* by Sheila Bair

I wasn’t going to touch this book if it were not for a personal endorsement from Chris Whalen. Bair, Chair of the FDIC (Federal Deposit Insurance Corporation), describes the incredible turf wars and petty battles below the surface of the bailouts. I previously had sensed Sheila was one of the good guys; the book reinforced it. She describes Bernanke as *generally* well-meaning, Geithner as a relentlessly pro-Citigroup promoter and Rubin pawn (to the point of racketeering), and a host of others who clearly need severe beatings. It is an antidote to the highly lopsided Sorkin treatise, *Too Big to Fail*. Here is a Bair interview.

*Bailout: An Inside Account of How Washington Abandoned Main Street While Rescuing Wall Street* by Neil Barofsky
Neil entered the crisis plotline as the young, feisty special investigator general to oversee the TARP bailout (SIG-TARP). From his presentation, he was green and naïve, unready for the thugs he would be dealing with. By example, he figured out relatively late in the game that the gaping holes in the bailouts used by the banks to siphon trillions from the Fed were left there by design, not by mistake. The big loser is Geithner, who comes across yet again as a despicable human being. I was disappointed not to get more insight into Elizabeth Warren's role as Chair of the TARP oversight committee. Barofsky has done many interviews; an Econtalk variant is particularly thorough.

Reckless Endangerment: How Outsized Ambition, Greed, and Corruption Led to Economic Armageddon by Gretchen Morgenson and Joshua Rosner

This is an excellent and detailed analysis of the financial crisis, deeply probing the mortgage industry's role (more than simply explaining the basics found in all of the crisis books.) Some may find this old news that they would like to put behind them. My only caveat is that one should read this book or Nocera and McLean's All the Devils Are Here, but not both.

The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White, and the Making of a New World Order by Benn Steil

Benn is a fellow at the Council on Foreign Relations (CFR) with what I would call an Austrian economic slant. The book will be released in March. In it, Steil describes a fascinating battle between Harry Dexter White and John Maynard Keynes before, at, and after the 1944 Bretton Woods Conference in which the future world currency regime was hammered out. We get deeply insider views of the events in a prose and presentation that I found gripping. Keynes's role as a diplomat, unknown to many, may have been his most important single contribution. Heads up: Steve Hanke of the Cato Institute and Johns Hopkins University also has a book on the Bretton Woods Conference coming.

Throw Them All Out: How Politicians and Their Friends Get Rich Off Insider Stock Tips, Land Deals, and Cronyism That Would Send the Rest of us to Prison by Peter Schweizer

Many may know Schweizer from a 60 Minutes episode that revealed broadly based, scandalous insider trading by Congress that is legal for them. This is the book upon which the 60 Minutes episode was based. Schweizer tells horror story after horror story of graft that would get normal citizens sent to prison. What is appalling is how often they sell the taxpayer out by billions of dollars so that they can make a few hundred thousand dollars. Obama comes out looking particularly bad as the author describes how shovel-ready projects were really about massive kickbacks for campaign donors. It was not, however, a partisan hatchet job.

Thinking About Capitalism by Jerry Z. Muller and Modern Economic Issues by Robert Whaples

These two trimester-length audio books from The Teaching Company focus on basic principles of economics from a decidedly descriptive slant (as mandated by audio). It's easy listening stuff that is appropriate for those trying to become comfortable with foundational principles. I liked them because they provide these principles in particularly clear and cogent prose. Never pay retail; they go on sale at 80% discount many times during the year.

The Clash of Generations: Saving Ourselves, Our Kids, and Our Economy by Laurence J. Kotlikoff and Scott Burns

This is a follow up to Kotlikoff's The Coming Generational Storm describing the impending problems from off-balance sheet obligations. The authors, in conjunction with Kent Smetters, did the seminal studies on unfunded liabilities—promises that are unfunded even when projected tax revenues are subtracted. The authors now estimate them at over $200 trillion. I found the The Coming Generational Storm more
appropriate for my needs. The clash of generations is part warning and part investment book for those who are not familiar with this issue. I think the authors manifest ‘doomsayer’s fatigue’—the need to be optimistic after years of seeing a dismal future. I am, nonetheless, a huge Kotlikoff fan.

Thinking, Fast and Slow [382] by Daniel Kahnemann

Kahnemann is probably the most prominent contributor to behavioral economics, garnering him the Nobel Memorial Prize in Economics. He works with Nassim Taleb and appears to be Taleb’s mentor. Thinking Fast and Slow presents the constant battle between the instinctive thoughts and more decidedly cognitive reasoning, explaining how we make decisions and how they can go astray. It is more thoughtful than Gladwell’s Blink, sometimes demanding deeper thought.

How We Decide [383] by Jonah Lehrer

Lehrer’s book came recommended via an Econtalk interview.312 It is yet another Blink-genre book looking into how humans make decisions. I love these books but this treatise is presented at a much lower level than Kahnemann’s and is remarkably similar to a book entitled Sway by Ori and Rom Brafman. Consumers of pop psychology should probably check out Ed Yong’s interview on Econtalk discussing the underlying flaws in this type of social science.313

The Wisdom of Crowds [386] by James Surowiecki

Surowiecki discusses how collections of people with limited individual insights, if acting truly independently, display collective “wisdom” and how that wisdom is lost when they start acting in a correlated fashion. There are many cute snippets describing the results that, at times, become a little too loosely connected. Aficionados of this genre will find it both fun but partially redundant to other works (Taleb; Kahnemann; Gladwell).

My Stroke of Insight: A Brain Scientist’s Personal Journey [387] by Jill Bolte Taylor

Jill, a Harvard neurophysiologist, wakes up one morning and finds herself having a stroke in the highly rational left brain. Her deductive reasoning goes on- and off-line, throttling her back and forth between euphoria and panic. The story describes the stroke and the long recovery in hysterically funny prose from an especially insightful perspective of a neurophysiologist. I found the audio book to be an excellent medium.

Steve Jobs [388] by Walter Isaacson

In case you’ve been living under a rock, this fully sanctioned biography that was in no way edited by Steve or his family is simply the best biography I’ve ever read. You get a bird’s-eye view of the computer revolution from soup to nuts through the detailed stories and words of all of the key players. Steve was a unique personality with a unique ability to translate unimaginable compulsive behavior into profound success rather than total failure. My conclusion: Sell any shares of Apple Computer because it ain’t the same company without Steve.

Secrets: A Memoir of Vietnam and the Pentagon Papers [389] by Daniel Ellsberg

Ellsberg describes the events leading up to, during, and following the release of the Pentagon Papers, the media-driven exposé of nefarious activities by a string of administrations. It is not really about the content of the papers. Presidents who lie to the American populace seem rather pedestrian in this era. It was interesting but only in the four-star category.

Human Prehistory and the First Civilizations [390] by Professor Brian M. Fagan
I have listened to dozens of trimester-length courses provided by The Teaching Company as audio books. With only one exception, they have been great. In this course, Fagan does a great job of following the lineage from the origins of humans starting about 8 million years ago through to the ancient (prehistoric) civilizations across all continents. It’s both informative and very easy listening. Reminder: Never pay retail for these books: they go on 80% sale routinely, bringing the price down to about $70.

*Bonhoeffer: Pastor, Martyr, Prophet, Spy* by Eric Metaxas

Bonhoeffer was a cleric and a spy in Nazi Germany who eventually gets executed for his role in a conspiracy to kill Hitler. (That is not a plot spoiler; the author tells you he died right up front.) The biography describes the church-state battle, which was very new to me. In my opinion, however, there was way too much church and not enough state. Despite over 500 bonkers reviews at Amazon I found it to be boring.

**Acknowledgements**

OK. This ain’t a book; it’s just a friggin’ blog. I’ve got to take this opportunity, however, to thank some folks who have generously shared their time and insights so as to make thinking about capitalism a special experience. You guys have made a difference. Chris Martenson brings gravitas to the debate on resource depletion and, in conjunction with Adam Taggart, graciously publishes my Reviews and invited me for my favorite interview. Rick Sherlund of Goldman Sachs/Nomura and friend of 40 years inadvertently and unknowingly triggered a discontinuity in my perception of markets with the most innocuous of statements. *Bloomberg* reporters are especially accessible. I have exchanged hundreds of emails with Mark Gilbert, head of *Bloomberg’s* London Office, Caroline Baum, and many other colleagues. Dave Lewis, a former Louis Bacon protégé and scholar of a higher order I call a friend although we meet up only sporadically. I have had dozens of exchanges with an eclectic mix of characters ranging from Elizabeth Warren on the left and Lew Rockwell on the way right. Within that enormous chasm includes multiple and meaningful exchanges with Stephen Roach (Morgan Stanley), James Howard Kunstler, Art Cutten (Jesse’s Café Americain), Byron King (Agora), John Rubino, Bill Fleckenstein, Benn Steil (CFR), Gerard Minack (Morgan Stanley), Doug Noland (Federated Investors), Richard Daughty, Jack Crooks, Grant Williams, and Jim Rickards. I thank Richard Uhlig, former CEO of Morgan Stanley’s banking subsidiary, for giving a two-hour guest lecture on mortgage-backed securities in my honors chemistry class. (The kids loved it!) Meetings and conversations with economists Larry Kotlikoff and Steve Hanke are enormously appreciated. I have especially cherished numerous exchanges with David Einhorn, a truly unique individual and intellect, culminating in a meeting with David and subsequent breakfast with his parents. (Mom is quite the bear.) I was profoundly honored when David Weidner included me in a WSJ article on the flash crash and Demetri Kofinas and Lauren Lyster invited me to do an amazing interview on Capital Account. These experiences are special and wholly orthogonal to my exposure in chemistry. Lastly, Bruce Ganem rekindled my interest in markets, politics, and economics. Our colleagues will never forgive you.
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Links

The superscripted links are found here [57].
2012 Year in Review - Reference Links

by David Collum
Monday, December 21, 2009, 11:46 AM

Tags: 2012 Year in Review [1]

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Limits of Government


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