

Quote of the week : “A man hears what he wants to hear and disregards the rest” - Adam Smith in The Wealth of Nations (borrowed by Simon & Garfunkel for the lyrics of one of their songs).

According to Bloomberg the US gun market is cooling, with Smith & Wesson’s Second Quarter sales down 23%-, & those of its major competitor Sturm Ruger & Co. down 13%-, YoY as inventories of unsold guns have piled up at the retail level - *this, welcome as it may be for those who question the gun fetish of many Americans, was overshadowed by news that a nine year-old girl had accidentally killed her instructor at an Arizona gun range when the kickback of the Uzi SMG she was firing caused her to lose control of it. Her parents ought to be charged with contributing to the delinquency of a minor or even involuntary manslaughter, & one can only hope that the victim’s family will sue their-, & the gun range owner’s-, ears off.*

California, the most populous US state (with 12% of the nation’s population, vs 8% for No.2, Texas, & 6% for No.3, New York), is having a bad year. First, it continues to suffer from a three year drought that, after having prompted more than the usual brush fires & forced one-tenth of its farm land to be left fallow, has now reached the point people are no longer allowed to add water to their swimming pools, have to ask for water at restaurants, are prohibited from washing their cars & have shallow wells go dry. Then earlier this week there was a 5.9 earthquake in the Napa Valley region at the height of its tourist-, & the onset of its grape harvesting-, seasons. And finally, a day or so ago, Hurricane Marie, 800 miles (1,300 kms) West of Mexico’s Baja California peninsula caused swells that created waves 6 metres/20 feet high¹ to hit the Southern California coast, damaging waterfront homes & knocking out pier pilings, but elating surfers.

With all the media focus having been on events further East in the Arab world, it has all but ignored Libya’s descent into failed state anarchy. In the Gadaffi era it produced 1.4MM bbl/d of oil. During the fight to unseat him several private armies were formed that, once he was gone, defied Libyan Army attempts to disarm them. The parliament elected in 2012 was dominated by Islamists with links to Egypt’s Muslim Brotherhood & al-Qaeda and, before its term in office ended late last year introduced sharia law & unilaterally voted to extend its mandate by one year. But in February the head of the army, Gen, Khalifa Haftar² forcibly removed it from office & in the subsequent election in July the Islamists were routed. Meanwhile, in mid-May, Gen. Haftar had launched an offensive against the Islamists in Eastern Libya that resulted in counterattacks that after 41 days of fighting culminated in them capturing the Tripoli International Airport in Western Libya on August 23rd. Two days later, on August 25th, the members of the former Islamist-dominated parliament met and voted to ignore the election outcome & replace those elected in it. Amidst all this Libya’s oil output slid to as little as 120,000 bbl/d in May, although it has since recovered to 600,000 bbl/d & at last report it was claimed that it would be raised further, to 1MM bbl/d, later this year (while, regardless of who runs it, the government supposedly needs 1.6MM bbl/d & a US\$100 oil price to balance its budget) - *unless Gen. Haftar can get the situation under control, it would not be surprising if at some point Egypt’s ruler, the one-time Defense Minister, General/self-appointed Field Marshall & now,*

¹ Still, by Book of Guinness Record standards mere pikers : for the current record high for a wave ridden by a surfer is 78 feet (25 metres) & an application is in for recognition of an 80 foot one, both of them recorded off the coast of Portugal, in 2011 & last February respectively.

² As a young officer he supported, & participated in, Gadaffi’s seizure of power in 1969 & until 1990 had a successful career in his army. But then the two had a falling-out & for the next two decades he lived in the US, in the Washington area, biding his time & acquiring US citizenship.

President Sissi, with 'nod-nod, wink-wink' support from Washington may enter the fray in the belief that, with Libya's population only being 6MM & Egypt having a standing-, albeit largely conscript, army of half a million, along with twice that many reservists, this would be a 'walk in the park'.

Canada's Harper government has egg all over its face. For it has been on a crime bill 'kick' and mistakenly sent the wrong version of one of its toughest crime bills to the Senate, that debated it & sent it on to a Committee for further study. This has never happened before & nobody seems to know how this happened now (though some blame mindless staff cutting), nor how to fix it.

In Ontario the share of Grade 6 students that meets provincial standards in math had gone from 61% to 54% in the past five years, & for Grade 3 students from 71% to 67%. On the other hand, in all fairness, in the Grade 9 'academic' stream the comparable number has risen during the same five years from 82% to 85% & in the 'applied' stream from 40% to 47%. While many parents across Canada have been pushing for a move towards a more back-to-basics approach in teaching math from the various new-fangled methodologies dreamt up by educators, they haven't met with much success anywhere but Alberta.

According to China's Ministry of Industry and Technology slower economic growth has caused the corporate sector's receivables to be up 12.7%-, inventories 12.6%-, & financing costs 16.5%, YoY - *this is clearly not sustainable & cannot help but prompt a further erosion of the, purportedly already questionable, average quality of the Chinese banking system's 'loan book'.*

Next week's NATO Summit in Wales will be faced with a proposal, pushed by Poland & the Baltic states, for new NATO bases in Eastern Europe to give, *at least in theory*, more substance to NATO's ability to deal with Russian threats in the region. Canada is expected to support the idea, & in fact has already stationed a few fighter jets in the region - *while the motivation of the countries is understandable, the macropolitical downside of the idea is that it will heighten the Kremlin's anti-Western paranoia.*

In eight European countries (Austria, Belgium, Denmark, Finland, Germany, *one-time basket case* Ireland, Netherlands & Switzerland) the yield on two-year government bond is now in negative territory, and in three others it's all but negligible (France -0.014%, Spain - 0.107% & Italy - 0.250%) while in Britain it is 0.692% & in Portugal 0.753% - *not particularly a vote of confidence in the European banking system.*

A giant sinkhole, so deep one cannot see the bottom, has opened up on the farm of 71 year-old John Hensby in County Durham, Northeastern England, above an old, long abandoned lead mine. At last report it was 35 feet/12 metres wide & growing, which worries him since his house is only 260 feet/78 metres from its edge.

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CENTRAL BANKERS' NEW GOSPEL : SPUR JOBS, WAGES AND INFLATION
(NYT, Binyamin Appelbaum)

- For two decades the central bankers' dogma was 'stabilize inflation & thereby stabilize the economy'. But their annual Jackson Hole clambake this month made it clear that this is now passé & that the 'new norm' is all about increasing employment & wages, and inflation. Janet Yellen patiently explained that it is now all about keeping interest rates

low, Mario Draghi that he was expanding his stimulus campaign & the BoJ's Haruhiko Kuroda that he will keep pushing to get inflation up to 2%.

- But the reality is that so far their efforts have met with only limited success in meeting their new goals, especially in Europe & Japan, and that increasingly questions are being raised as to the scope for monetary policy to further them at all. Be that as it may, Atlanta Fed President, Dennis Lockhart opined "I would be concerned about being early and premature ... That's more of a concern to me than being maybe a little slow to begin the normalization of interest rates", & Mario Draghi that "The risk of doing too little outweighs the risk of doing too much."

Wage inflation is now the key gauge for them as to how close the economy is to capacity. And while there may be anecdotal evidence that employers have difficulties finding qualified workers, the policy makers believe the stagnant wage levels are proof employers can still find staff at current wage rates & thus see no need to raise them (in contrast, a small Texas businessman friend recently noted "the Mexicans who used to work for \$8 now want \$12").

HONGKONG DATA PROVIDE GLIMPSE OF GLOBAL RETAIL TROUBLES **(G&M, Carl Mortished)**

- Wall Street analysts have been pawing through the mid-year financial entrails of Li & Fung, a century-old, Hongkong-based company that generates annual revenues of US\$15BN-US\$20BN by acting as a middleman between 15,000, sometimes very large, manufacturers of consumer goods &, sometimes very large, retailers all over the world, incl. Target & Wal-Mart in the US (which accounts for 60% of its revenues) for insights as to what the future might hold for US retailers. The message they're getting echoes those from the US Department of Commerce when it recently reported disappointing retail sales in July & from Britain where High Street sales that same month were up a minuscule 0.1% (with the absence of Russians in Europe-, & Beijing's anti-corruption drive-, putting a further damper on global retail sales). Most disconcerting was Li & Fung's message that consumers are "buying closer and closer to the season"; for this will reduce retailers' willingness to place orders well ahead of the time they expect to need them (& make it less feasible for them to depend on suppliers in faraway places, thereby creating a drag on the demand for consumer goods from Asia?).

Consumption doesn't have much scope for real growth when people's real wages decline, as they have in the US for the past two decades, when the past pile-up of consumer debt borrowed from/pre-empted today's consumer spending & when inflation has been chronically understated³. The Fed's pointy-headed Ph.D's, who sought to boost consumer spending by creating a 'wealth effect' with their QE initiatives, had forgotten their Economics 101 lesson eons ago about the declining Marginal Propensity To Consume (i.e. the wealthier people get, the less

³

An egregious real world example of the erosion of Joe & Jill Average Consumer's buying power is bacon. 18 months ago it could routinely be bought for \$5.99 for a 500 gram package, & often was on sale, occasionally for as little as half that, whereas today it is \$6.99 for a 375 gram package (& discounted sales are scarcer than hen's teeth), representing an increase of 55% over 18 months, roughly 20x the 'headline' inflation rate. Ditto for gasoline : between January 1, 2009 & December 31st, 2013 the average price in Canada went from \$2.79 per US gallon to \$4.59; i.e. it increased at a compound annual rate of 11.5%. Another under-reported feature of inflation is package sizing. Toilet paper rolls today are far narrower than they were a decade ago, and tins of Campbell soup & frozen juice that once contained 355 grams of product today contain only 286 grams. And these are things that people need, & buy everyday, unlike cars or computers, the purchase of which is more intermittent & of a more discretionary nature.

of each incremental dollar of income they spend on consumption). If they really wanted to boost consumer spending, they might have taken a leaf out of the book of that populist economic ignoramus, the late former Alberta Premier Ralph Klein, who in 2006 sent every Albertan a \$400 "Prosperity Bonus" cheque, that the vast majority of them, & certainly the lower income ones among them, promptly spent.

IMF'S CHRISTINE LAGARDE 'UNDER INVESTIGATION' (BBCNews)

- Earlier this week she was interviewed, for the fourth time, by magistrates in Paris in connection with allegations that business tycoon Bernard Tapie had been awarded a large arbitration award while she was France's star Finance minister because of his political connections rather than the merits of his case. After the interview, she was put under 'formal investigation' (which in France magistrates can do when they believe there are indications of criminal wrongdoing which, however, does not necessarily always leads to criminal charges).

Tapie once was France's business 'Wunderkind'. Born into a family of modest means, while still in his 20's he started buying companies in trouble, sorting them out & divesting them at a profit. Along the way he amassed a fortune, incl. a rich man's favorite play thing, a sports club, in his case the Olympique de Marseille championship football club, and briefly was a (Socialist) government minister. But, like a 'nova' star, his downfall was as spectacular as his rise had been; for in the mid-90's, when he was in his early 50's, he was charged, among others, with match fixing, tax fraud & complicity in corruption, went bankrupt, & briefly 'did time'. During this period he sold his nearly 80% stake in Adidas to the French bank, Crédit Lyonnais which later sold it at a big fat profit. In the 2007 election, he suddenly emerged, despite his previous Socialist affiliation, as a supporter of Sarkozy, sued the by then defunct Crédit Lyonnais for having defrauded him in the Adidas sale a decade earlier &, in due course, won a 430MM Euro arbitration award, which it has led to the current investigation. The question preoccupying the magistrates is how much, & when Lagarde knew what & whether as Finance Ministershe she signed off on some documents with a signature she has maintained all along is a forgery.

VANCOUVER HOUSING DATA REVEALS CHINESE CONNECTION (G&M, Ian Barlow)

- MacDonald Realty Ltd., which has 1,000+ agents & staff in its various offices in BC, said that one-third of the houses sold by its Vancouver offices in 2013 went to Chinese buyers, both new arrivals & those with Canadian citizenship (*usually* purchased under Ottawa's now defunct Immigrant Investor Program). They see Vancouver as a stable & picturesque place to invest money & have been upscale buyers, with the average price of houses they bought topping \$2MM, half as much again as the average house.

A decades-long phenomenon that has helped to make the Vancouver housing market the most costly in Canada, it has recently been given renewed impetus by President Xi's anti-corruption campaign that, as was the case prior to Hongkong reverting back to Chinese control two decades ago, has prompted Chinese nouveaux riches to think of the need for a Plan B in case it were necessary to skedaddle in a hurry (according to Beijing there are at least 150 Chinese citizens living in North America who are wanted back home for economic crimes/corruption).

HAMAS, ISRAEL AGREE TO INTERIM CEASEFIRE (AP, Karin Laub)

- An ambiguous interim ceasefire reached after seven weeks of fighting keeps Hamas in control of Gaza, and Israel & Egypt in control of access to it, allowing both sides to claim

victory. Meanwhile a senior Hamas leader promised “We will build & upgrade our arsenal to be ready for the coming battle, the battle of full liberation”, thereby enabling Netanyahu’s critics to complain the deal hasn’t defused the military threat from Gaza. In the short run Hamas has gained by having Israel undertake to ease the import into of aid & building materials & to double the fishing zone for Gaza fishermen to six miles offshore. Then one month hence talks are supposed to start on the more complex issues, incl. Hamas’ demand for the building of an air-, & a sea-, port (*which Netanyahu has already said ain’t going to happen unless Hamas disarms, which it doesn’t want, and cannot afford, to do since it would remove its sole meaningful bargaining chip*). And it wasn’t a good omen that in the two hours before the ceasefire took effect at 1900 hrs on August 25th, Hamas fired off 83 rockets, of which 13 were intercepted, as well as 12 mortar shells at a communal farm near Gaza which killed two & wounded seven others, two of them critically, while just minutes before the deadline Israeli airstrikes collapsed a five story building in Gaza & killed 12 Palestinians, incl. two children.

In Washington the State Department’s spokesperson likely hit the right note when she called the ceasefire agreement “an opportunity, not a certainty” (which if history is any guide may well founder on intransigency on both sides, just like the baker’s dozen that preceded them)

NETANYAHU AND THE LIMITS OF MILITARY POWER (Times of Israel, David Horowitz)

- On July 23rd, prior to the launching of the Gaza ground offensive, a poll by Channel 2 found that 82% of Israelis were happy with his conduct of the Gaza operation while a similar poll taken August 27th, after the ceasefire was agreed to, showed this had cratered to just 23%. For they had been assured the operation would have a quick & decisive outcome, whereas the ceasefire agreement is inconclusive & Hamas kept firing rockets until the very last moment, clear evidence that Israel had failed in its primary objective of ensuring sustained peace & quiet for its citizens. But his fellow Israelis may be too hard on him; for while it’s easy, as Foreign Minister Avigdor Lieberman & Economy Minister Naftali Bennett have been doing *ad nauseam*, to urge “smashing” Hamas, doing so without a clear post-smashing Gaza exit strategy would likely have cost hundreds more Israeli- (& thousands more Palestinian-) lives with no guarantee Hamas would stay smashed. And as Netanyahu pointed out during his August 27th press conference, when the smashing was over, the question would remain as to what to do with 2MM extremely hostile Gazans. Furthermore, the fact that 64 Israeli military losses are widely seen as intolerable are indicative of the likely public reaction to a far greater body count. And it was his ordering the total destruction of what he called the “Gaza Terror towers”⁴ & the resultant total lack of international insistence that he desist & of an outcry from both the West Bank & the rest of the Arab world that finally forced Hamas to agree to a ceasefire on the very same terms Israel had held out for all along. And now he can use, & is *already* using, the Gaza experience of the past six years as an example why overall security control over the West Bank can never be relinquished. On the other hand, his press conference was a strikingly candid acknowledgment of the limits of military power, a difficult, discomfiting & unpopular message for an Israeli public long brought up to take it for granted that the IDF can deal with any & all military threats, provided its gets the right orders from the political leaders.

⁴ Whereas the air force had always sought to target specific units in high rise buildings that housed individuals or operations of interest, in the last few days before the ceasefire it had been ordered to just flatten whole buildings regardless of who, or what, else was in them.

The 2006 Lebanon War should have been the first warning for Israelis the IDF was not invincible & that in an asymmetrical warfare situation, the party with the biggest traditional fire power doesn't necessarily win. This was a lesson the US should have learnt in Vietnam but never really took to heart, as evidenced by its Somalia, Iraq & Afghanistan military escapades since. And it is unlikely that the Israelis will act any differently, even if they wanted to, despite the fact that experience has shown that often there comes a time, as the South Africans realized two decades ago, when, after all else has been tried & found wanting, one has to bite the bullet & put all preconceived notions aside to just cut the best deal possible under circumstances. And while many Israeli leftist peaceniks are now starting to say all this could have been avoided if only Netanyahu has focused more on building up, & less on undermining, Abbas, their voices are being drowned out by those who still haven't gotten, or don't want to get, this message; and unless & until they do, the outlook for the Israel as the world has come to know it in the past almost three quarters of a century is likely to dim [the Times of Israel is a 2 ½ year-old, online, politically "independent" newspaper⁵ that now is published in four languages (English, French, Arabic & Chinese, but strangely enough not Hebrew) & David Horowitz its founder & still the moving spirit behind it]

STEINETZ : ISRAEL PAID A HEAVY PRICE OVER GAZA (BBC News)

- Yuval Steinitz is a *hawkish* long-time member of Prime Minister Netanyahu's Likud Party, a former Finance Minister & now his Minister of Intelligence. Earlier this week, after Israel & Hamas had agreed to yet another ceasefire, this one for 30 days, he told Stephen Sackur, the host of the BBC program Hard Talk who was on location in Israel that "We have paid a very expensive price with 70 casualties on our side, with people having to flee their homes in the South of Israel because of the daily barrage of rockets and mortars. This is a very high price for a democracy to pay."

In the interview he acknowledged there had been serious discussions in the Israeli Cabinet about (going whole hog and) re-occupying Gaza & it was hard to escape the feeling that, at least in his mind, there is no room for meaningful discussions with Hamas during, or after, the cease fire period nor any room for making any meaningful concessions to Hamas & that the cease-fire period should be used by Israel to prepare for Plan B, the re-occupation of Gaza.

OVERWHELMING MAJORITY OF JEWISH ISRAELIS SAY GAZA OP JUSTIFIED (Haaretz)

- The Peace Index is a JV of Tel Aviv University & the Israeli Peace Institute. Since 1994 it has each month released polling results about Israeli attitudes towards the Israeli-Palestinian conflict. The latest one, taken 30 days into the 50-day conflict, revealed a broad consensus among the Israeli public that the latest action against Gaza was justified & that, while 92% was pessimistic about its lasting effect, they were still optimistic about Israel's future (& that 63% felt "The whole world is against us.")

A more recent poll by the same paper found that 54% of those interviewed were skeptical about Netanyahu's August 27th claim on national TV that the latest round of fighting in Gaza had resulted in a "great military and political victory", that Israel had dealt Hamas "a heavy blow", & that Hamas had "received not one of the demands it set forth for a ceasefire." And Yuval Diskin, a former head of Israel's Shin Beth (internal) security service, called the outcome "disappointing" & having left a "sense of sourness" that had left the Israeli public "frustrated".

⁵ Although a number of its staff, incl. Horowitz himself, once worked at the left-of-centre Haaretz.

This seems to confirm the impression left by Steinitz that the ceasefire may turn out to be just a brief interlude in the hostilities rather than a period for constructive dialogue (and as to both the Peace Index-, & the Haaretz-, polls it is worth remembering that they involved only rather small population samples (of less than < 500 people) and therefore have relatively high margins for error, & that both are left-of-centre entities, which in Israel means they are more pro-peace than the general population).

PRO-RUSSIAN REBELS TAKE STRATEGIC PORT NOVOAZOVSK ON THE AZOV SEA
(The Independent, Peter Leonard)

- This came after three days of *intermittent* shelling by artillery, some of it allegedly from the Russian side of the border & is the first time anti-government forces operated this far South. It is significant because this 12,000 inhabitant town is located at the Easternmost end of the coastal highway linking the Crimean peninsula with Russia proper & because, if Moscow succeeded in turning it into a land bridge with Crimea it could turn the Azov Sea, and all the oil & gas that may, or may not, lie beneath it, into a Russian inland sea.

Action speaks louder than words : this came on the heels of the meeting between Putin & Ukrainian President Poroshenko in Minsk, the capital of Belaurus, that was to have led over time to a normalization of the relationship between their two countries. And unconfirmed reports from Ukrainian armed forces units in & near the town claim they were outgunned & outnumbered, not by rebel forces but by Russian tanks, artillery & infantry that had crossed the border into Ukraine (in an apparent attempt to force the Ukrainian armed forces to spread themselves thinner & thereby take the pressure of the rebel forces further North near Donetsk).