

Quote of the week - “there’s no government, there’s no opposition, and those who got us into this mess have run away, they’ve gone to ground.” - Alistair Darling (now aged 62, he was a Labour MP from 1987 to 2015, most recently for an Edinburgh constituency, & Chancellor of the Exchequer from 2007 to 2010) in an interview on BBC Radio Four. Elsewhere he was quoted as saying that he was more worried now than he was during the 2008 financial crisis (*when he was Chancellor of the Exchequer!*) & that *Prime Minister hopeful* Boris Johnson¹ is treating “Brexit like a big game.”

Quote of the week No. 2 - “At its core, Brexit reflects a pervasive phenomenon in the high income world : rising support for populist parties campaigning for a clampdown on immigration. Roughly half the population in Europe and the United States, generally working class, believes that immigration is out of control, posing a threat to public order and cultural norms.” - Jeffrey D. Sachs, Professor of Sustainable Development at Columbia & Special Adviser on Millennium Development Goals to UN Secretary-General Ban Ki-Moon (*high profile as Sachs may be, in attributing the Brexit referendum outcome to the “working class” he is outright wrong; the split among the 33+MM people who voted in it was less among class-, than age-, lines : upwards of 72% of 18-24 year-olds voted REMAIN & 60% of the 60+ year-olds LEAVE. But, unfortunately for the REMAIN side, the turnout among the younger voters was lower than among older ones. So the outcome was decided by those who in many ways had least to lose (other than Social Security benefits that in a doomsday scenario could prove hard to sustain)*)².

Brexit - The situation is complicated by Scotland, Northern Ireland & Gibraltar (upon which Spain has long been casting covetous eyes) having voted to REMAIN, by David Cameron’s resignation & by Bank of England Governor Mark Carney having irritated the LEAVE side by his dire warnings of the economic consequences of leaving (with his most ardent supporter, Chancellor of the Exchequer George Osborne, not being long for this world politically). Under Art. 50 of the 1992 Maastricht Treaty Britain must give notice of its intent to withdraw³ to the European Council (EC), i.e the heads of all 28 member states, after which both sides have two years (during which Britain would remain a full member of the EU) to negotiate a new arrangement (that would have to be approved by a majority of the European Parliament **and** every EU member state - *which could prove a real hurdle*). Alternatively, the British Parliament could simply revoke its 1973 legislation that authorized Britain joining the EEC, the EU’s predecessor, in which case one school of thought holds the stock markets would drop & sterling fall by as much as 15% & another that this will be like Y2K, much hype in advance & few, if any,

¹ Who observed on June 27th that the British pound was now “more stable” at the very time it was at a three decade low against the US dollar & a two-year low against the Euro.

² But the doomsday scenario may not come to pass; for the UK has more favourable demographics than other major EU countries. Thus in the decade to 2010 its annual population growth rose from 200,000 in 2000 (30% net births & . 70% net immigration) to 500,000 (50/50) in part as a result of which at last report it had more GDP growth-positive dependency ratios :

	Young age	Old age	Total	Share of population
	-----Dependency Ratios-----			over age 60
UK	27.2%	27.0%	54.2%	4.7%
Germany	19.9	31.5	51.4	5.4
France	29.3	28.4	57.6	5.7
Spain	22.8	27.2	50.0	5.7
Italy	21.5	33.1	54.6	6.4

³ With the Treaty not being clear about who should originate such notice, the government-, or the parliament as a whole-, of the day of the country in question.

serious consequences after the fact. And Britain's departure could fuel growing anti-EU sentiments in a number of other EU member countries & in due course, lead to a break-up of the EU as it has evolved, top-down, in the past two decades.

Chapwood Index - Many question the CPI's use as the proxy for inflation saying its calculation has been manipulated to minimize the growth of the 'inflation-indexed' Social Security payouts⁴). Addison, TX-based Chapwood Investments has acted on this by providing its clients throughout the year-, & the general public with a lag once a year-, with the growth, in 50 major US cities⁵, in the cost of 4,000 commonly purchased consumer items⁶. Its Chapwood Index suggests that since the mid-1980s the gap between its annual rate of growth & that of the CPI has widened from 1-, to 8+-%. Thus for 2014 it ranged from 8 to 13 percent in various cities, incl. San Diego 13.1% (*vs. the 1.9% CPI reading*), New York 12.4% (1.3%), Los Angeles 12.1% (1.3%), & Chicago 10.9% (1.7%)⁷. And San Francisco, Cal.-based consulting economist John Williams produces an electronic newsletter Shadow Government Statistics. As part thereof, starting from the premise that in the past two decades the quality of government reporting has deteriorated (which he attributes in the case of the CPI to Alan Greenspan's introduction of the idea of "hedonic regression"⁸), he continues calculating the CPI using the BLS' methodology of the Carter/early-Reagan era. And, lo & behold, it too produces 9+% readings for the **real** impact of inflation on household budgets.

Rio Olympics - The 2016 Summer Olympics begin on August 5th, but there is growing concern among athletes about the Zika virus to the point where, despite the IOC's "total confidence" it will be safe, 27 year-old Rory McIlroy, a golfer representing Ireland, announced on June 23rd he wouldn't be taking part (the fourth athlete to do so, the others being from the US, Australia & South Africa). Earlier this month the state of Rio de Janeiro declared a state of emergency over a lack of funds, forcing the central government (*that it likely could ill afford*) to hand it US\$849MM in 'emergency funding' to help meet its *Olympic* infrastructure & public safety funding commitments. Meantime, there's still no shortage of human poop in the waters on, or in, which the Olympic boating & triathlon events will be held, creating serious health risks for the

⁴ If the indexing of these payouts had over the years been at a rate greater than the CPI, the Social Security system would by now be unfunded to a far greater degree than it already is.

⁵ Conspiracy aficionados take note of the fact that, whereas a few years ago a Google search for 'The Chapwood Index' was rewarded with lots of information feedback, today it merely produces a message that "This page cannot be displayed".

⁶ Incl. items such as Starbucks coffee, Advil, dry cleaning, laundry detergent & healthcare, highway tolls, movie tickets, fast-food & pizza, computer paper, Internet service, mobile phone service & cable TV, toothpaste, oil changes & car washes, home repairs, & light bulbs, pet food, school supplies, underwear and magazines.

⁷ According to Chapwood Investments Managing Partner Ed Bukowsky the high inflation rate means that "individual purchasing power is sinking in quicksand and people are unable to maintain their current lifestyle." - this may not be entirely true for homeowners, who can subsidize, have been subsidizing, an excessive lifestyle by monetizing the equity in their homes (as Americans did at a record rate during the US housing bubble a decade ago, & Canadians are doing today).

⁸ Which adjusts the price increase numbers for increases in quality; thus, if a computer cost \$1,000 one year & \$900 a year later, but had 50% greater capacity, the CPI price adjustment would not be 10% but 40% (the problem is that the consumer has no option but to buy this year's model).

athletes in those events. And the risk to athletes' (& visitors'?) personal safety was highlighted when during the June 17th weekend Australian wheelchair basketball player Liesl Tesch was robbed of her bike, at gun point at a bus stop. And the latest embarrassment for Rio came last week when WADA (the World Anti-Doping Agency), with the backing of the IOC, suspended the city's accredited drug-testing laboratory for "not conforming with international standards for drug-testing laboratories" (which means that the drug testing of Olympic athletes' samples may have to be done elsewhere).

The Trump phenomenon - Last February Peggy Noonan came up, in her column in the WSJ, with an explanation thereof that runs as follows : society consists of the protected & unprotected. The former (*incl. all public sector workers?*) do well by the system in terms of jobs, housing, schooling for their kids, (*pensions?*) etc. With the system rigged to ensure it will keep benefitting them, they are blind to (*and, what's more important, often don't seem to care about*) what **really** goes on elsewhere in society. The unprotected, on the other hand, get the short end of every stick. Lousy jobs. Homes in lesser quality neighbourhoods. Schools that don't work for their kids. So while the former **make** policy, the unprotected must **live** it & they have now concluded that the system isn't working for them & that therefore they owe it no allegiance, and they are starting to act on that. Her answer lies in what she calls "a remoralization" of the protected class, i.e. a shifting of the attitude of the upper half of society to their own long-term self-interest & from "You are on your own, *you nitwits*, get with the program" to caring more about their unprotected fellow citizens - *Now in her mid-60's, she was Ronald Reagan's speech writer, has been the author of several NYT best sellers & for many years an WSJ columnist. An ardent admirer of Edmund Burke, Abraham Lincoln & Ronald Reagan, she is a diehard conservative but not necessarily an unquestioning supporter of the GOP (thus she was highly critical of the Bush 43 regime's latter years).*

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IMF CUTS FORECAST FOR U.S. GROWTH (Bloomberg News)

- On June 23th it cut its forecast of 2016 US GDP growth to 2.2% (from 2.4% last April) and suggested there is a clear case for the Fed to proceed on a "very gradual" path in raising rates & that a dovish *monetary* policy tilt will insure against the risk of disinflation and of the Fed having to reverse course & lowering rates to zero. More specifically, it counseled "The path for policy rates should accept some modest, temporary overshooting of the Fed's inflation goal to allow inflation to approach the Fed's 2-percent medium target from above."

The same day the National Association of Realtors reported that in May, as an improving supply increased choices for buyers⁹, existing house sales were up 1.8% MoM, & 4.5% YoY, to 5.53MM units, a post February 2007 high (although this came after the April sales pace had been revised down to 5.43MM from the original 5.45MM-, units and despite the fact that the sale of Manhattan apartments is down 10% YoY & that of coops 20%)..

GOVERNMENTS BLASTED FOR 'LOW-GROWTH TRAP' (Europost)

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While cheap, cheap credit explains why there is a surfeit of buyers, it doesn't explain why there appear to be growing numbers of willing sellers.

- In its June semi-annual Economic Outlook the OECD warns the global economy is slipping into a “low-growth trap” where ultra-loose monetary policy may do more harm than good and that the rich world is responsible for this, given its politicians’ failure to revive demand & overhaul their economies after the 2008 financial crisis. It says too much of the burden of lifting growth has been left to central banks that, after pushing interest rates below zero & pumping money into their economies through asset purchases, are now starting to see diminishing returns, & risking more financial market volatility. Secretary-General Angel Gurría told Bloomberg it is “Overall a rather mediocre picture , a rather dismal outlook ... Trade is growing at 2% to 3% *while* it should be growing at 7%”, while Chief Economist Catherine Mann observed “Monetary policy has been the main tool, ... In trying to revive economic growth alone, with little help from fiscal or structural policies, the balance of benefits-to-risks is tipping ... negative feedback loops are *now* at work ... Monetary policy cannot revive near and long-term growth by itself and distortions are increasing.”

They are ‘preaching to the converted’ (that unfortunately do not include the politicians).

FROM CASH WOES TO DIGITAL #FAILS, TRUMP’S CAMPAIGN IS ‘WORST OF ALL POSSIBLE WORLDS (The Guardian. Ed Pilkington)

- Trump may rule Twitter but isn’t doing much to build the kind of digital fund raising & volunteering network that propelled Obama into prominence in 2008 & 2012. With 70 campaign staff nationally vs. her 732, he is vastly out-organized by Hilary despite his recent announcement of hiring “several new staff members to expand his campaign operations”; thus in a swing state like Ohio, in theory fertile ground for him given its manufacturing base & number of angry white male voters, Clinton has 3x as many workers. And the new campaign filings on June 20th revealed he had just US\$1.3MM cash, vs. Hilary’s US\$40MM.
- During the primaries his Twitter feed, that broadcast his contentious views on cable TV in a constantly evolving feedback loop, was a winning strategy. But in an election candidates, must convince a sea of largely disengaged voters instead of limited numbers of devoted adherents. While his advisers believe his primary strategy will work just as well in the election, experts in mass communication & modern elections say it would be an epic mistake to expect headline-grabbing tweets to sway the whole nation¹⁰, and studies have found that state-of-the-art voter mobilization techniques & harnessing the energy & enthusiasm of volunteers can boost voter turnout on election day by up to 7%. Also says Stanford professor of political science & communication Shanto Iyengar “If the Trump campaign doesn’t invest heavily in developing a sophisticated voter mobilization campaign, I don’t see how they can be competitive in battleground states ... the Clinton campaign is miles ahead in being able to target and mobilize their voters.”

So in the end, it is still all about getting the vote out on Election Day.

BITTER EXCHANGES AS EU PARLIAMENT DEBATES BREXIT (BBC News)

- Britain’s vote to leave the EU has shaken the European Parliament. Many MEP’s are sad to lose the UK & there was a standing ovation for its outgoing Commissioner (*for*

¹⁰ Especially now that Trump’s advantage in the social media seems to be slipping.

Financial Stability), Lord Hill (who warned “the City of London has lost its voice with Brexit”). But there also was a strong sense of defiance & concern for the future, and calls for unity & reform, and the need to connect with its citizens¹¹. But for Eurosceptics it was a sweet moment : the once deemed near impossible had become reality and UKIP’s Nigel Farage told MEPs they were “in denial” & “The UK will not be the last member state to leave the EU”.

- Its first debate on Brexit on June 28 was marked by bitter exchanges. When EC President Jean-Claude Juncker opened the session by saying the British government should “clarify” its position but that the British people’s will should be respected and UKIP Leader Nigel Farage started shouting & clapping, Juncker, to the applause of other MEP’s, responded by asking him “You were fighting for the exit, the British people voted in favour of the exit - why are you here?” & accused him of having “fabricated reality” by saying he would use the UK’s EU contributions to fund its National Health Service. Former Belgian Prime Minister & now leader of the liberal group in the European Parliament Guy Verhofstadt went as far as to accuse Mr. Farage of having used “Nazi propaganda” in the campaign & to note “Finally we are going to get rid of the biggest waste in the EU budget ... your salary”, and to attack the former Lord Mayor of London & a leading candidate as Cameron’s successor, Boris Johnson, referring to “the selfishness of one man prepared to do anything to become the prime minister of the UK.”
- Quotes from the June 28th debate include :
 - “fragmentation is no longer unthinkable and should gravely concern us all” - Dutch Defence Minister Jeanine Hennis-Plasschaert;
 - “Those who said “the European Union is irreversible , well, the British people have told you where to get off” -French National Front Leader & MEP Marine LePen;
 - “The European Union cannot become a hostage to the internal party politics of the [British] Conservatives” - Italian MEP Gianni Pittella;
 - “We in the North of Ireland are not bound by the UK vote ... The last thing the people of Northern Ireland need is a new border with 27 member states.”- UK MEP Martina Anderson (Sinn Fein).

In her toughest words yet, reflecting her government’s concern that other EU member countries could follow Britain’s move, Angela Merkel said the bloc would not tolerate British “cherry-picking” in the negotiations and “There must be and will be a noticeable difference between whether a country wants to be a member of the European Union family or not”.

AFTER BREXIT, ONLY ONE THING CAN KEEP BRITAIN TOGETHER **(The Telegraph, Mark Stanford)**

- While the LEAVE campaign never envisaged the balkanization of the 300 year-old United Kingdom, now the prospect of Scotland & Northern Ireland remaining in the EU would herald its breakup. But there still is a way to prevent this, by having Britain leave the EU but remain in the EAA¹², or single market, the so-called “Norwegian model” (that also applies to Iceland & Liechtenstein). While LEAVE campaigners derided it as involving all the costs of EU membership without a say in EU policy-making, they

¹¹ The widespread lack of which is its Achilles Heel.

¹² The European Economic Area that includes 27 of the 28 EU members.

neglected to mention that it would also meet many of their demands : freedom from the Brussels bureaucracy & the stifling effects of the EU's Common Fisheries & Agricultural Policies, continued participation in the single market without any of the trappings of political union, freedom from the EU's VAT treaty (enabling Britain, like Liechtenstein & Switzerland, to choose the VAT rate that fit the needs of its economy), more flexible trade as it regained the power to negotiate its own trade agreements, either on its own, or as a member of the EEA (who, along with Switzerland, often cooperate in negotiating free trade agreements). And continued access to the single market would reassure investors & ensure the City of London remained a global centre for trading & finance, thus protecting hundreds of thousands jobs.

But it wouldn't address one key demand of the LEAVE side, quit sending of money to Brussels.

S&P LOWERS BRITAIN'S CREDIT RATING (Bloomberg News)

- Britain being stripped by S&P of its AAA rating was based on the country's decision to leave the EU. In lowering it by two full steps to AA, S&P cited the risk of a less predictable, stable & effective policy framework and "the risks of a marked deterioration of external financing conditions" & constitutional issues arising from the majority of voters in Scotland and Northern Ireland having opted to remain in the EU."

The double downgrade was purely emotional & reflects worse on S&P than Britain whose credit quality may well improve if Scotland & Northern Ireland cease to be economic 'boat anchors'.

WHAT CHINA'S BIG NATION COMPLEX MEANS FOR THE FUTURE OF ASIA (War on the Rocks. Shannon Hayden)

- During my two years on the China desk in the Office of the Secretary of Defense we had frequent interactions with our PLA counterparts in the Chinese embassy, who in the process gave clues about their mindset about their neighbours. Like "of course Vietnam should defer to its 'big brother' and be silent". Or, "Yes we can discuss the South China Sea, but the other countries' claims are a joke". And when frustrated if we disagreed with them they typically retorted, with various levels of frustration, along the lines of "China is a big country. X is a small country. What more is there to say?".
- While this may come from thousands of years of thinking of their country as the Middle Kingdom, it is hard to square with modern concepts like international law & dispute settlement. France's Minister of Defense Jean-Yves Le Drian put this in perspective at a recent Shangri-la Dialogue in Singapore¹³ when he said "If the Law of the Sea is not observed in the China seas today, it will be in jeopardy in the Arctic, the Mediterranean and elsewhere tomorrow ... to keep the risk of conflict contained, we must defend the Law and defend ourselves with the Law." And if China sees the last century as a aberration & now plans to resume its 'rightful role' in the world, this won't stop with the South China Sea.
- The past decade in the South China Sea has been a test of the international system from which Beijing has taken these lessons. You are strongest when you change the

¹³ An annual three-day conference organized by the London-based IISS (International Institute for Strategic Studies) that in the past fifteen years has become a prime venue for Defense Ministers from the Asia-Pacific region to exchange views on defense polic. This year session was attended by 600 delegates from 50 countries, incl. 35 Defense Ministers, incl. China's.

situation on the ground¹⁴ : its reclamation efforts have changed the map of the South China Sea (while other claimants are building too, their efforts are minuscule compared to China's). To achieve priority goals, one must be willing to lose elsewhere : Beijing believes its gains in the South China Sea are well worth any punitive measures that may result. Being its neighbours' No. 1 trading partner provides leverage. And finally, while the international community may speak with one voice, actions, or the lack thereof, speak louder than words.

- We should reflect on this as we contemplate, as France's defense minister told us, what may come next. As China gains strength & capability, it will push outward. The South China Sea is but one of its core interests. And given the forward motion permitted there by the international system, the question is "Why stop if no one is stopping you?"

Since September 2015 the writer has been Associate Director of the Southeast Asia Program at the Center for Strategic and International Studies, one of the most highly-regarded Washington think tanks. She seems to totally disregard the possibility that the 21st Century version of the Middle Kingdom may have some of the trappings of a Potemkin Village and that soon Beijing will be faced with demographic-, environmental-, & domestic political-, headwinds/time bombs that will constrain its international posturing potential.

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Or as the old saying goes "Possession is nine points of the law".