

Quote of the week - "A man must live like a great brilliant flame and burn as brightly as he can. In the end, he burns out. But this is far better than a mean little flame." - Boris Yeltsin.

Fed rate outlook - Last December the Fed raised its rate target range by 25 bps to 0.25%-0.50%, the first hike in nine years, giving rise to speculation when the next shoe might drop, with some people surprised/disappointed it didn't do so at the July FOMC meeting. On August 16th, Atlanta Fed President Dennis Lockhart told the Rotary Club of Knoxville, TN "I, as one Federal Reserve policy maker (*who this year, however, is not a voting member of the FOMC*) am not prepared to rule out at least one rate hike before year's end" but said he wasn't looking for a particular date. That same day, Bill Dudley, the New York Fed President &, as such, Vice-Chairman of the FOMC, told Fox Business News "We're looking for growth in the second half of the year that'll be stronger than the first half" (*which wouldn't be too remarkable; for the latter had only been 1.2%*) & that hence a September rate hike (*at the September 20-21 FOMC meeting*) "is possible ... We're edging closer towards the point in time it'll be appropriate to raise rates further." And the next day Atlanta Fed President James Bullard (who this year has a vote) told a St. Louis audience there was no reason yet to conclude the US has shifted from the low growth, low inflation "regime" that makes low interest rates appropriate for the foreseeable future (*which he defined as 2 ½ years*) & that hence there was no reason to raise interest rates more than once to, say, 0.63% - *the moderate tone of Bullard, a deemed "hawk", was not quite as surprising as the not quite so dovish one of Dudley (who is one of the heavyweight-, & for long one of the more dovish-, members of the FOMC).*

"Market 'breakdown' to be 'sudden', intense and large" - This is the bottom line of Elliot Management's latest, & bleak, letter to investors. Founded by Paul Singer in 1997 it runs a hedge/vulture fund with AUM of US\$28BN that has generated double digit returns for investors since inception (& is up 5.1% in the First Half). It says, among others, that the bond market is "broken" & the value of money has been debased and that inflation is probably inevitable & that, when it happens, it could be swift & impossible to tamp down -*this article can be googled.*

US productivity - From 1950 to 1995 US productivity grew at a 1.9% CAR¹ & in the next 15 years by 2.6% (*much of it, however, to the benefit of the "1%"?*). But in the last six years, i.e. since the Great Recession, it has slowed to a measly 0.32%. So it isn't surprising that when the Labor Department reported Second Quarter non-farm productivity growth had been negative for the third quarter in a row (by an annualized 0.5%), Capital Economics' Paul Ashworth said "the stagnation in productivity growth was even worse than we previously believed."

The Fed's David Byrne & the IMF's Marshall Reinsdorf noted in a paper earlier this year that in the US (& many other countries) a serious downtrend in productivity had started in 2004 (which Prof. Robert Gordon of Northwestern University attributes to the ending of an era of "unusually lush invention" (& *spread in the use?*) of things like the electric power grid, light bulbs, *computers*, internal combustion engines, telephones, radio & TV and indoor plumbing & running water, while many recent ones, like Facebook, are not adding to (*work place*) productivity in a like manner²

¹ Compound Annual Rate.

² This should not surprise anyone; for, while earlier inventions made people work more efficiently, the more recent ones have entertainment/quality of life-, rather than work-place-, added value.

- Increasing standards of living are a function of GDP growth, the rate of which is more of a function of productivity growth than of fiscal & monetary policy. So it is not altogether surprising that between 1950 & 1980, the annual GDP growth rate twice spiked to 15+% & typically was well over 5%, while since then it only once has exceeded 10% & since 2004 has never been above 5%. This may help to explain the 'natives' restlessness' & Trumpism/Sandersism in the developed world³ today.

GLEANINGS II - 672
Thursday August 18th, 2016

IMF ADMITS DISASTROUS LOVE AFFAIR WITH THE EURO AND APOLOGISES FOR THE IMMOLATION OF GREECE (The Telegraph, Ambrose Pritchard-Evans)

- A devastating report by the IMF's own IEO (Independent Evaluation Office (that reports directly to the Board rather than via Managing Director Christine Lagarde) concludes that its top staff had misled the board, made calamitous misjudgments in Greece, ignored impending signs of the *European* debt crisis (that has been the most damaging episode in the 72-year history of the Bretton Woods institutions), been euphoric cheerleaders for the Euro project & failed to grasp an elemental aspect of currency theory. It also describes a "culture of complacency" prone to "superficial and mechanistic analysis", traces a shocking breakdown in governance to the point that it is unclear who is in charge of this powerful organization & notes that "many documents were prepared outside the regular established channels ... (*and*) on some sensitive matters could not be located." In fact, while the report doesn't outright accuse Mme Lagarde herself of obstruction, it says its investigators had been unable to obtain key records or penetrate the activities of certain "ad-hoc task forces" & in some instances, "had not been able to determine who made certain decisions or what information was available, nor ... to assess the relative roles of management and staff". It says the IMF's whole approach to the Eurozone had been characterized by "groupthink", with staff members who warned the design of the Euro was fundamentally flawed overruled, & had lacked fall-back plans on how to tackle a systemic crisis in the Eurozone; for the possibility of that happening had been ruled out *ab initio* since "The IMF remained upbeat about the soundness of the European banking system⁴ ... largely due to the IMF's readiness to take the assurances of ... euro area governments at face value."
- The three main bailouts (of Greece, Portugal & Ireland) were unprecedented in scale & character; for each was allowed to borrow more than 3x the normal maximum (as a result of which they *between them* accounted for 80% of all lending by the IMF between 2011 & 2014. And as to Greece, as late as 2007 the IMF still thought that "in view of Greece's EMU membership, the availability of external financing is not a concern" & had violated its own cardinal rule by signing off on a bailout in 2010 while unable to offer any assurance the package would bring the country's debt under control and/or clear the way for recovery.

³ It is likely relevant in this context that, contrary to much of the post-WW II years, parents in developed countries today are less sanguine than their parents & grandparents had been that their children will have a better standard of living than they themselves had enjoyed.

⁴ Which in the case of Italy's certainly has been proven to have been a gross error.

This article was dated three weeks ago & yet has had little media coverage since. And 'groupthink' seems to hallmark much of today's global central banking community's thinking.

DREAM OFFICE REIT TURNS TO NIGHTMARE (Financial Post, Barry Critchley)

- On August 11th its units closed at \$16.92, down \$1.67 on the day & 58% from its 2012 \$39.73 high. For it had cut the "fair value" of its assets by \$748.4MM for the First Half [so that the NAV (Net Asset Value) of its units is now \$23.64 vs. \$30.31 three months-, & \$33.22 one year-, ago]. Of the 749MM in total write-downs, \$675MM related to its Alberta property portfolio (the value of which it had cut by 42% to \$931MM), commenting in its Second Quarter report "Based on our leasing experiences and external market data, we decided to significantly write-down our Alberta assets in the second quarter of 2016 to reflect a slower and more prolonged recovery for the Alberta office market." So investors in the Company's units haven't fared well; for in the five years ended August 11th the units have generated a total return of -21.38% vs. S&P/TSX Index's 18.16% - *this should disabuse some people real estate is by definition a "safe investment"*.

There is now 8+MM sf. of vacant office space in Calgary (a 15 year supply & a 20+% vacancy rate), with another 2+MM sf. new office space still under construction. As to the Calgary housing market, while as of the end of June prices were down 'only' 4.1% YoY, sales & inventory numbers tell the real story; for in June 2,028 units changed hands, down from 2,182 in June 2015 & 2,657 in June 2014 (just before the oil price cratered); so, as the inventory of homes for sale rose from 4,820 units in June 2014 to 5,130 one year later & 5,973 last June, in two years the ratio of monthly sales to inventory has dropped from 55% to 40%. The situation is slightly better in Edmonton but this may be a mirage; for the local economy has been propped up by a high level of commercial & residential construction activity downtown [the biggest being the \$600+M Rogers Place, the ice palace new home for the Oilers hockey team⁵ (where ticket prices will be as much as twice what they were at their old home, where they hadn't been cheap by anybody's definition)] that started to slow down in the Second Quarter & will totally peter out in next year's Second Quarter, "with nothing behind it" in the pipeline. Meanwhile, Rachel Notley's NDP government seems to be totally pre-occupied with-, & wasting its time on, doctrinaire left-wing experimentation.

CANADA FACES CHINESE WRATH OVER OLYMPIC SLIGHT (G&M, Yu Mei)

- Chinese state media called CBC commentator Byron MacDonald "abusive" since on August 11th his comment on the 4x200 metre freestyle *swimming* relay was "that little 14 year old girl from China dropped the ball" &, and more specifically that she "went out like stink and died like a pig" (comments for which the CBC subsequently apologized). Those who know Mr. McDonald, a longtime swimming coach who since the 1980s has helped coach Chinese swimmers training at the UofT, say this is a term he often uses for a swimmer who starts strong but fades quickly. In China one user lamented on the Sina Weibo social medium that "This Olympics should be called the anti-China Games", & the Party-run International Global Times responded to some real or perceived slights from the Australians⁶ by accusing them of "barbarism" & "white supremacy" & saying they live in a "second class country ...once "populated by the UK's unwanted criminals."

⁵ That may well prove over time to be the Edmonton equivalent of Montreal's 'white elephant' Olympic Stadium that became a financial millstone around the city's neck for 31 years.

⁶ Incl. its government's support for the The Hague court ruling on its South China Sea claims.

Part of this may be due to official concern that China's athletes are becoming less interested in the fame their achievements bring their country & more in what is in it for themselves. And part of it is due to "medal angst"; for while China was No. 1 in the gold medal count at the 2008 Beijing Games, in 2012 it played second fiddle to the US at the London Games, & at the time of writing (12:19hrs on August 18th in the GMT -6 time zone) its 19 gold medals placed it not only far behind the US' 31 but also behind Britain's 21. Be that as it may, this is not a good omen for Prime Minister Trudeau's August 30th - September 6th visit to China [only two days of which (September 4th & 5th) are set aside for the G-20 Summit. And since he is doing so at the invitation of Premier Li Keqiang, one can only hope, given the apparent power struggle now underway between Li & President Xi, that Trudeau's association with Li will not poison the well for his future status in Beijing, as Prime Minister Harper's was when in 2012 during a visit to China he made a side trip to Chungqing in the interior to meet with the then 'golden boy' Bo Xilai, weeks, if not days, before the latter fell from grace (he is now serving a life sentence).

TINY GERMAN BANK BREAKS TABOO BY CHARGING RICH CLIENTS FOR DEPOSITS **(Reuters, Alexander Hübner)**

- The Raffeisenbank Gmund is a cooperative bank with assets of 145MM Euros in Bavaria near Germany's border with Austria. As of September 1st, it will start charging holders of 'sight deposit accounts' (that allow holders to withdraw their money at any time) of over 100,000 Euros/US\$111,500 a negative interest rate of 0.4%⁷, *necessitated by the fact that, effective August 1st, the cooperative movement's central bank had started charging it 0.4% for its deposits.* While several larger banks are already doing so to its large commercial customers, doing so to retail customers had so far been seen as 'a bridge step too far'. While the BVR (Germany's National Association of German Cooperative Banks) doesn't expect other deposit takers in its 1,000+ outlet network to follow this bank's lead, "because of "the intense competitive situation in the German banking market", Bavaria's 269 member GVB (cooperative banking association) backed the bank's position, with its spokesman declaring "The ECB's extreme monetary policy is creating considerable costs for all banks ... As a last resort, they also have to look ... to be reimbursed for the cost of deposits."

According to Josef Paul, the bank's manager "Some of the customers ... have opted for alternative investments and others moved their money to other banks" ; this is not surprising, for the bank is located in Gmund am Tegernsee, a town on the "idyllic" Tegernsee that is home to many wealthy actors & sports stars with likely little, if any, emotional attachment to the cooperative movement.

EUROZONE SEES ECONOMIC SLOWDOWN (Reuters)

- After 0.6% QoQ First Quarter GDP growth in the 19-country Eurozone, stagnation in the French & Italian economies helped to half it in the Second Quarter to a level up 1.6% YoY.

In the Second Quarter the GDP growth rate was zero in both countries (in both cases marginally better than the -0.1% in the year-earlier period), in France's case down from 0.7%-, & in Italy's

⁷

It says this will only affect fewer than 140 of its depositors & deposits of less than 40MM Euros (i.e. 25-30% of its deposit base).

case from 0.3 %-, in the First Quarter. Japan was the only other major OECD member country to have had no GDP growth in the Second Quarter (vs. 0.5% in the First Quarter, but up from minus 0.4% YoY). And for several other countries the comparable numbers were : US 1.2%, 0.8% & 2.6%, Canada 1.1%, 0.3% & 2.0%, UK 0.6%, 0.4% & 0.4%, Greece 0.3%, -0.1% & 0.1%, Australia 3.1%, 2.9% & 2.1%⁸, and in three non-Eurozone EU member countries Poland, Sweden & Denmark 3.1%, 3.0% & 3.1 % , 0.3%, 0.4% & 1.3% and 0.3%, 0.1% & 1.9% respectively.

RUSSIAN INFLUENCE GROWING IN MIDDLE EAST (WP, Erin Cunningham)

- Iran has long banned foreign militaries from having bases on its soil. But that has apparently changed. For on August 16th the Russian Defense Ministry announced that earlier that day long-range Tu-22 Russian bombers had taken off from a base near Hamadan in Western Iran for raids on targets in Syria's Aleppo-, Deir al-Zour-, & Idlib provinces⁹, prompting Iran's National Security Council chief Ali Shamkani to declare that Iran & Russia "enjoy strategic cooperation in the fight against terrorism in Syria, and share their facilities and capacities to this end." Although Russia in the past year built a new air base in Latikia, the Alawite heartland & the coastal province adjoining Turkey in Syria's very Northwest, immediately to the North of Tartus province where Russia has long had a naval base, its runways were too short for the Tu-22s; so now they have to fly just 650 kms. on bombing runs from Hamadan, rather than three times as far from Russian bases.

The rebels (& ISIS) are Sunni, the regime in Tehran Shi'ite & that in Damascus Alawite, a Shia sub-set that accounts for only 12% of a Syrian population that is majority Sunni). Tehran would be loath to see the Assad regime overturned since, as long as it stays in power, it has a land bridge to its Hezbollah satellite in Lebanon. One can only wonder what it cost Putin to enhance its foot print in the Middle East in this manner. As to Putin helping Assad "fight terrorists", since the definition of terrorism is "the use of violence & intimidation in the pursuit of political aims", both ISIS & Assad seem to qualify for that definition better than the Sunni rebels. But it has become common for unpopular rulers to tag anyone who oppose them as a "terrorist".

OPPOSITION BREAKTHROUGH PUTS CRACKS IN ANC' HOLD ON POWER (G&M, G. York)

- After ten days of tense negotiations Julius Malema's leftist¹⁰ Economic Freedom Fighters party (that got 8% voter support) announced on August 17th it would not join coalitions

⁸ Rather amazingly, the Australian central bank's base interest rate is 1.50% & it has yet to engage in "unconventional monetary policy" moves (although, with inflation now being down to 1.0%, there has been rumours that may change in the not too distant future.

⁹ This is an interesting choice of targets : for Aleppo & Idlib provinces in the very North of the country, adjoining Turkey, are the stamping grounds of the ('sort-of' US-supported) rebels who have made some gains there recently, while Deir al-Zour, in the very East of the country adjoining Iraq, is mostly controlled by the 'common enemy', ISIS which has been losing some ground there lately. And Iran likely did not have let Putin use one of its air bases for nought, unless it had misgivings about Assad being able to hold its own against the rebels.

¹⁰ It ran on a platform that, among others, advocated the nationalization of banks, the expropriation of farm land, a judicial inquiry into corruption allegations & the cancellation of a costly nuclear energy deal (that by most standards is preposterously expensive on a per MW of installed capacity).

with the ruling ANC in the major cities where the latter had lost its majority in this month's *municipal* elections because the ANC was "corrupt" & "arrogant". So in a humiliating defeat for President Jacob Zuma the ANC has now lost control of several of South Africa's major cities and, while the ANC will still be in control of Durban & a few other cities, it is likely to become a largely rural-based party¹¹, administering a huge blow to Zuma's prestige & diminishing his ability to deliver patronage awards & lucrative contracts to his supporters.

Fallible as the ANC regime has been since the end of apartheid in 1994, & reprehensible as Jacob Zuma is personally, this outcome is unlikely to attribute to political stability in the country.

-O-O-O-O-O-O-O-

A landslide US election? - This now seems a media mantra, despite there not having been one in US Presidential elections since 1984 when Ronald Reagan routed Walter Mondale, getting 525 Electoral College votes with 58.8%-, vs. Mondale's 13 with 40.5%-, voter support. Still, the US may be overdue for one since in the 1900's there was a 12-13 split between landslides & non-landslides. *In his August 15th speech in Ohio & the one in Milwaukee on the 17th, Trump sounded less 'Trumpish' than usual, & hammered away at issues that will resonate with many Americans regardless of political proclivity : in Ohio he focused on the need to deal with ISIS more effectively than Obama & Clinton (on their watch it had grown stronger & gained ground worldwide), & in the Milwaukee one he targeted Afro-American Moms (& Pops?), whom he posited (correctly so?) as front-line victims of much (young) black-on-black violence & as voters whose staunch support for Democrats over the years had left many still poverty-stricken, i.e. with no measurable political payback.*

UNPOPULAR CANDIDATES MAKE COMPELLING CASE AGAINST TWO-TERM LIMITS **(G&M, John Ibbitson)**

- According to Gallup the August before he is to vacate the White House 52% of Americans approve of Obama, almost as many as Reagan's 53% at the same stage in his Presidency, but well short of Eisenhower's 62% & Clinton's 60%, but much better than LBJ's 35% (Vietnam), Bush 43's 31% (Iraq) & Truman's 30% (Korea), *all of whom were succeeded by a member of the other party.* With Mrs. Clinton having a -11 favourable/unfavourable 'gap' (between those who view her favourably & those who don't) & Trump a dismal -29, one pollster noted Obama "is way more popular than either of the candidates", This has prompted people questioning the two-term time limit^{12 13}, notionally because in his last term a President is a "lame duck".

¹¹ Since the urban share of the population has been growing for decades (in 1960 the split was 47-53 whereas last year it was 65-35), this is likely to reduce the ANC's potential support base.

¹² The 22nd amendment, passed by a Republican Congress in 1947, & adopted in 1951 after enough states had formally agreed with the idea, was the result of the fact that FDR had run for a third term in 1944, while full well knowing his days were numbered,

¹³ The US Founding Fathers discussed the possibility of including a two term time limit in the Constitution but didn't do so. When the First President, George Washington had served two terms he was pressured to run for a third but refused to & when No. 3, Thomas Jefferson after serving two terms experienced the same pressure, he too declined 'out of respect for Washington', thereby establishing a tradition that prevailed for 135 years until FDR broke the mould in 1944 and Congress formalized it three years later.

The argument advanced is anything but “compelling”. There is significant empirical evidence that business & political leaders often become less effective after 8-10 years in the job (because they begin to believe their own press releases & to surround themselves with lickspitlers?). And a lame duck term is unavoidable no matter how many terms an incumbent serves. This may well be driven by Democrats who are less than 100% comfortable with going into a possibly crucial presidential election¹⁴ with a candidate with lots of skeletons in her closet & whose near-record unpopularity factor among the general public is exceeded only by that of her opponent.

The 2016 Presidential election outcome Gospel according to Nate Silver - In his August 15th status report Election Update : 10 Big Questions About The Election Revisited his next to last question was “What would keep me up late at night if I were Clinton?” & his answer “At some point complacency could become an issue, although it is probably too early to worry about that. In the nearer term, I’d be worried that the race has been so volatile ... things look good now. But conditions in May, and again in July, produced a close race (& elsewhere he opines “if the race goes close, Trump is more likely to win the Electoral College”). Is there anything inherently preventing those conditions from rising again?...”. And his last, question repeated that for Trump & concluded “I might not be sleeping at all. The tactics that helped me win the primary don’t seem to be working in the general election. My position in the polls is deteriorating from middling to dire. More acutely I’d worry about getting cut off by the Republican National Committee or thrown under the bus by down-ballot Republican candidates ... concerned about their own survival. If those things happen, I might not have the resources to win the election even if the debates and the news cycle turn in my favour in September and October.” - *And despite the apparent ‘groupthink’ among TV’s ‘talking heads’, Yogi Berra (a common sense Grade 8 drop-out & quintessential baseball player fifty years ago) observation that “It ain’t over ‘til it’s over.” Is just as valid today as it was then*

¹⁴

If only because the next president may have an all but unprecedented opportunity to stuff the Supreme Court with politically/philosophically judges compatible with his/her own views.