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### **Our Re-creation of a Nineteenth-century “Bubble” Economy**

During the nineteenth and early twentieth centuries the American and European economies stumbled from one financial “panic” to another, in which credit dried up and economic activity ground to a halt. The Great Depression that lasted for almost the entire decade of the 1930s came in the aftermath of the high flying financial fling of the 1920s and the collapse in 1929 of the stock market and many of our banks.

After more than a half-century of relative economic and financial stability in which we worried about relatively minor and short-lived recessions rather than financial panics and depressions, we systematically relaxed the regulatory restrictions on our financial institutions and saw a new business culture develop that embraced the pursuit of short-term high returns through high risk investments.

The result has been a series of “bubble economies.” We could go all the way back to the 1980s and the Savings and Loan crisis when the American taxpayer had to bail out almost 750 community financial institutions that had been corrupted by outside interests’ race for short-term high returns. But let’s just go back a decade.

In the last half of the 1990s, new technology companies that had never earned a dollar of profit, some that had never sold a single product or service, were eagerly sought after by investors hoping to be in on “the next big thing.” The result was a desperate competition to purchase an interest in almost any new information technology stock and skyrocketing stock prices for new fledgling firms. The NASDAQ stock market soared higher and higher, bringing the other stock markets along. The value of the

stocks far exceeded any actual revenues, earnings, or profits. The return investors were betting on did not come from what the firms actually produced but from the constantly rising stock prices. Enthusiastic investors and investment analysts argued that this was not pure unsustainable speculation. The expansion in stock values could go on forever, they asserted, because only a few of those dot.com firms had to actually pay off the way Microsoft, Yahoo, or Intel had done to justify the high stock prices. It was a fantasy world that came to an end in the middle of 2000. By late 2003 80 percent of the peak value of the NASDAQ had been wiped out.

With the stock markets going nowhere but down and with near record low interest rates, investors faced limited investment opportunities. Complex, high-risk financial gimmicks including trading in the future value of foreign currencies and commodities and other hedge funds attracted more and more money as investors, addicted to high returns and willing to believe they would be smart and quick enough to manage the risk, looked for the next bubble. The low interest rates also made real estate investments look attractive. The low mortgage rates drew new home buyers, home owners who wanted to upgrade, and second home owners. As residential property values began to rise, the appreciation in home values more than paid the mortgage interest. Owning residential property became what appeared to be a free money machine. Many ordinary home owners, seeing their wealth increase because of the rising value of their homes, took out home equity loans and spent the money on current consumption. Real estate investments seemed to be a sure thing. Property values, many analysts asserted, never go down because there is a “natural” rising demand. Mortgages and new homes were pedaled to people who had no possibility of

making the payments because when the inevitable foreclosure took place, it was assumed that the home would have increased in value enough to pay off the loan. The sub-prime scam that converted what had been a bedrock safe investment, mortgages secured by real property in which the owner had considerable equity, were rolled together with high-risk, non-performing investments and sold around the world.

Now that that bubble, too, has burst, some of the nation's leading private and public financial institutions are reeling and in the process of being bailed out by the federal government. Meanwhile credit is shrinking worldwide, choking off economic activity.

What was a rich investor, still looking for high returns to do? The Federal Reserve has pushed interest rates down, residential property values are sinking, stock market prices are volatile but moving downward. Gambling on rising commodity prices: oil, natural gas, uranium, steel, gold, copper, wheat, etc. has been one outlet. We now appear to have a commodity price bubble underway that has most professional analysts baffled. While it is true that rising demand from the booming economies of China, India, Indonesia, and Brazil have created a rising demand for these commodities, when one looks at the current and near future balance of supply and demand, the current high and rising commodity prices cannot be explained. The speculative cycle of betting on future prices continuously rising that infected the dot.com and housing bubbles is almost certainly partially operating now in commodity markets too. A bursting of that bubble will also inevitably come, but not until considerable damage has been done to our families and economy.

And then what new bubble will inflate and collapse as the search for high, short-term returns continues to force us all to ride this speculative financial and economic roller-coaster? Do we really have to wait for another Great Depression before we re-impose regulation on our financial markets and our business and investment culture shifts its focus away from “money for nothing” to making real long-term investments that rebuild our society and economy?