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COMMENT

Vuvuzela

As we grew up we often heard the expression “grass grows greenest in the farmer’s footsteps.” Then we heard from Spain: “El oyo de amo engorda el cabello” which (we believe) translates freely into “When the boss is watching, the cattle grow fatter.” And recently we read (from Roman times) “If you want a prosperous farm, sell your town house.” The message is always the same: mind the store, take care of business. And the message applies, or should apply, with equal force to our world of investments.

But it no longer really does. In two generations money supply and the institutionalization of financial activities have surged enormously. So much money in the markets today is other people’s money (OPM) whereas a hundred years ago most investments were made by people with their own money or, at least, money they had borrowed and were responsible for. Robber barons or little old ladies buying a Scottish Trust, they were investors and/or speculators. “Put all your money in one basket and watch the basket” was an accepted modus operandi. And vast chunks of most businesses were owned by big investors, often the founders of the business. They cared.

Even bonds were (generally) legitimate a century ago. Throughout history the gold standard, or variations thereon, prevented nearly all governments from flooding markets with paper. Bonds had good coverage and were usually redeemed upon maturity rather than rolled into ever bigger tranches.

Today most shares of most public companies are owned, or rather managed, by unrelated third parties with amorphous objectives. Making money is only one objective; political correctness is another. And the trillions of bonds, money market securities and currencies, the products of endless government deficits, defy description but certainly give new meaning to OPM. Far and away the lion’s share of the world’s savings is now deployed in these bits of paper rather than in stocks even though, almost without exception, these securities have no asset coverage or earnings coverage. Furthermore there is almost no hope of the issuing governments balancing their budgets. Ever.

But none of this seems to bother the managers of OPM. They will buy almost any sovereign, or quasi-sovereign, debt, unless issued by the likes of Zimbabwe, and then ask for bailouts when things go wrong.

All too often those entrusted with OPM are not as analytical or value-oriented as people whose own money is on the table. Trades of convenience are often the order of the day. Nobody will be fired for buying a stock index and nobody will be fired for holding lots of cash (yielding almost nothing) in hope of lower markets. Even those who seek insurance against all the foolishness often buy a gold ETF rather than go to the trouble of buying and securing the real thing.

Another popular destination for OPM is real estate, particularly trophy office towers. From the Gulf to Gotham, Carolina to Calgary, the globe is marked with shiny office towers which may, or may not, service debt let alone generate cash. But they do present an easy way for OPM managers to get big money to work, and accounting rules permit valuations that are more generous than they should be. For example, where else can one classify “leasing costs” as a tangible asset, or “tenant relationships” as an intangible asset? And valuations of individual buildings are not subject to the whims of the stock market. It’s significant that frothy finances and bubbly real estate have moved hand in glove over recent decades.

Sadly, money these days is more often invested in areas to please the establishment rather than the beneficiaries. Witness Greece, where the banks holding Greek paper were (partially) bailed out but the Greek people were burdened with more debt. Most other countries (jurisdictions) are in similar shape. Sooner rather than later all these debts denominated in Euros, Dollars or whatever, will be either repudiated or converted to one currency or another and then reduced to nothing by inflation.

The current situation brings to mind a poem by A.E. Housman:

> Far and near and low and louder
> On the roads of earth go by,
> Dear to friends and food for powder,
> Soldiers marching, all to die.

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Rather than soldiers we think of savers and investors marching all to die. At least financially. Led, as were the soldiers, by the powers of the day.

The plethora of OPM is circuitously linked to the fact that there is no monetary system governing the world of finance. There is nobody working the farm or minding the store. The only apparent remedy for our ills available to policy makers is the printing press.

It has been forty years since the last monetary system was in place and the establishment, which blew that one up, has not lifted a finger to replace it. Even at the most recent G8 meeting there was apparently no thought given to the subject even though the G8 Chairman (at a press conference) referred to concern about a possible "cataclysmic" event. It seems crazy, but they favour easy money and chaos over self-discipline.

Historically, if leaders cannot, or will not, deal with realities, markets will. And all the vuvuzelas in South Africa cannot send a louder message regarding the future course of markets than the gold market is sending.

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