**2014 Year in Review: Pushing Out on the Existential Risk Curve in a Global Game of Tetris.**

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**Background: The Author**

> "I don't write about what I know: I write to find out what I know."
>
> ~Patricia Hampl

Every December, I write a Year in Review[ref 1–7] first posted on Chris Martenson's website Peak Prosperity[ref 2] with a secondary posting at Zero Hedge.[ref 3] What started as a brief introspective shared with a handful of e-quaintances has mutated into a detailed account that has accrued as many as 100,000 clicks. Each year I try to identify themes in events that evolve. As the title suggests, I have not seen a year in which so many risks—some truly existential—piled up so quickly. Each risk has its own, often unknown, probability of morphing into a destructive force. Groping for a metaphor—I love metaphors and similes—I feel like we're in the final throes of a geopolitical Game of Tetris as financial and political authorities race to place the pieces correctly. But the acceleration is palpable. The proximate trigger for pain and ultimately a collapse can be small, as anyone who's ever stepped barefoot on a Lego knows.

> "If the world seems to be turning 'round faster than ever, you're not alone. Grab hold of something, it shows no sign of abating."
>
> ~Josh Brown, CEO of Ritholtz Wealth Management

My lack of credentials is absolute—the Paris Hilton of finance—but has not prevented me from being a poseur in the *Wall Street Journal*[ref 8] and *The Guardian*[ref 9] and on *Russia Today*,[ref 10,11] and a host of podcasts.[ref 1] On the heels of a threesome with Bob Lehman and Grant Williams on BTFD.tv following last year's review,[ref 12] 2014 started with a bang on BTFD.tv in a New Year's Eve hexabox shared with a trader who cut his chops selling dime bags on street corners and a person who on close inspection appears to trade the trannies.[ref 13] Subsequent interviews on *Peak Prosperity*,[ref 14] *Wall Street for Main Street*,[ref 15] *Kunstlercast*,[ref 16] *Stansberry Radio*,[ref 17] and *Red Pill Radio*[ref 18] offered more opportunities to Milli Vanilli my way through finance and politics. I shared the podium with T. Boone Pickens and Alex Jones as an invited speaker at the *Stansberry Investment Conference*: "Boone. I agree with you. That first billion is being a bitch."[ref 19] (I took another swipe at the Roth IRA.) I almost made *Rolling Stone*, but Matt left me at the altar. (I still can't get that tune out of my head.) As this review is being uploaded to the web, I'm doing an interview with Erin Ade on *Boom Bust* (*Russia Today*), which will be posted on YouTube.[ref 20]

> "Risk means more things can happen than will happen."
>
> ~Elroy Dimsen, London Business School

**Content**

Footnotes appear as superscripts and contain associated hyperlinks. The whole enchilada can be downloaded as a single PDF **here** or viewed in parts via the hot-linked contents as follows:

Links

Each review begins with an account of my efforts to get to a financially secure retirement. I continue to cling doggedly to my belief in the Austrian business cycle theory and the need for a hard-asset-rich portfolio despite two consecutive years of decidedly lousy returns. The bulk of the review, however, describes thoughts and observations—just the year's events told as a narrative. The links are copious, albeit not comprehensive. Some are flagged with enthusiasm (must see). I am a quote junkie: quotations capture people's thoughts in their own voices, and *they* do the intellectual heavy lifting.

I try to avoid themes covered amply in previous reviews. Some topics seem to go into quiescence, whereas others move to center stage without warning. Precious metals are a personal favorite. Every year seems to pick up a theme, possibly reflecting the news cycle (although my sources are anything but mainstream). Geopolitics were huge this year. Sections titled Baptists and Bootleggers, Bankers, and the Federal Reserve cover the gamut of human folly. Owing largely to central banking largesse, the system seems to be wound tighter than a golf ball. The third and hopefully final leg of a secular bear market that began in 2000 may be visible—but record debt, bank interventions, low interest rates, and the onset of global currency wars may simply be bricks in the Wall of Worry. Naysayers relentlessly remind us how many terrible things have not happened. All year I kept thinking of a poignant declaration:

> "Hey guys: It's a dud!"
>
> ~Lt. Red Winkle en route to becoming pink mist in *Pearl Harbor*

I finish with synopses of the books that shaped my thinking. You will not find any new releases from Geithner or Clinton: I am selective.

**Sources and the Fourth Estate**

> "There are people that don't see the use in Twitter, and I get that. Who wants to mentally joust with the smartest, most relevant, and most connected people in the world?"
>
> ~Tony Greer, Buckingham Research Group

Before laying out a heap of content myself, a few comments about sources are warranted. Despite occasional bursts of glory and some serious journalism salted throughout the mainstream media, we have witnessed rot. The only commentary on TV worth expending ATP on is *The Daily Show* and its spawn. I do not need right- or left-wing propaganda. It is nauseating, especially given that so many reporters and academicians feigning impartiality are said to be on the payroll of political parties.[ref 21] The former editor of one of Germany's main dailies[ref 22] admitted to being "bribed by [American] billionaires," and a CIA operative referred to journalists as "cheaper than a good call girl."[ref 23] The once-illustrious

CNBC ratings are now plummeting for a simple reason: it sucks. Simon Hobbs and Steve Sedgwick can put a sock in it. Mandy suggested that “over indebtedness comes from financial illiteracy.” Steve Liesman illustrated it by stating that “debt is the great bridge between working hard and playing hard in this country.” I can feel my IQ dropping. Wayne Rogers of *Mash* fame hammered a Fox host by noting, “You're a moron because you talk too much, and you don't think through it.”[ref 24] Well said, Wayne.

> @DavidBCollum Ask Fisher why a committee of bureaucrats sets the price of capital.
>
> @steveliesman Because the alternative is the vagaries of the supply of gold.

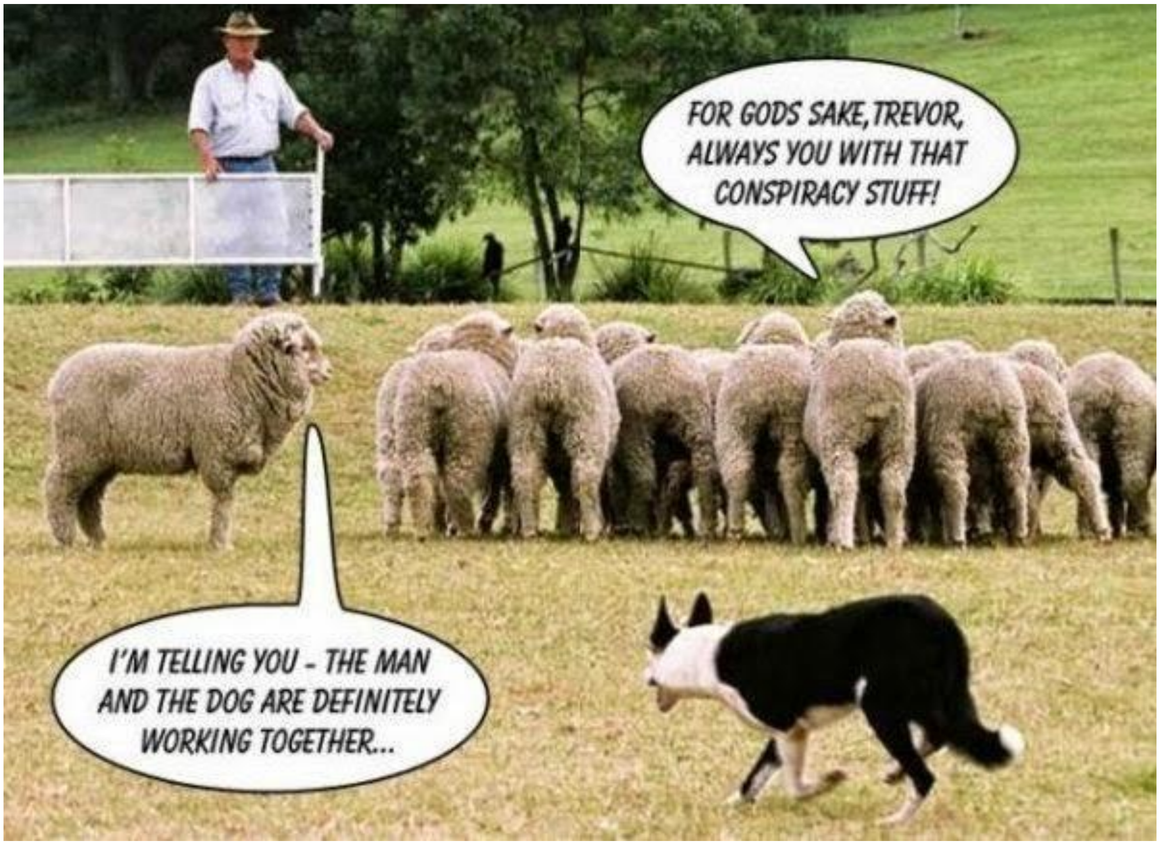
My primary sources are an eclectic gaggle of bloggers—guys like Michael Krieger[ref 25] and Charles Hugh Smith[ref 26]—and select news consolidators. My actions speak to my enthusiasm for Peak Prosperity.[ref 27] The 500-pound gorilla is Zero Hedge—edgy, ahead of the curve, and accurate enough. Newcomers this year include David Stockman's *ContraCorner*[ref 28] and a new Internet news network called *RealVision*[ref 29] created by Grant Williams and Raoul Pal. Twitter may or may not be a good investment, but a good Twitter feed is a gateway to the world. You never know what you'll find:

> “@zerohedge Ha ha, you are such a dickhead . . . it's wonderful.”
>
> ~David Andolfatto (@dandolfa), senior vice president, director of research, Federal Reserve Bank of St. Louis

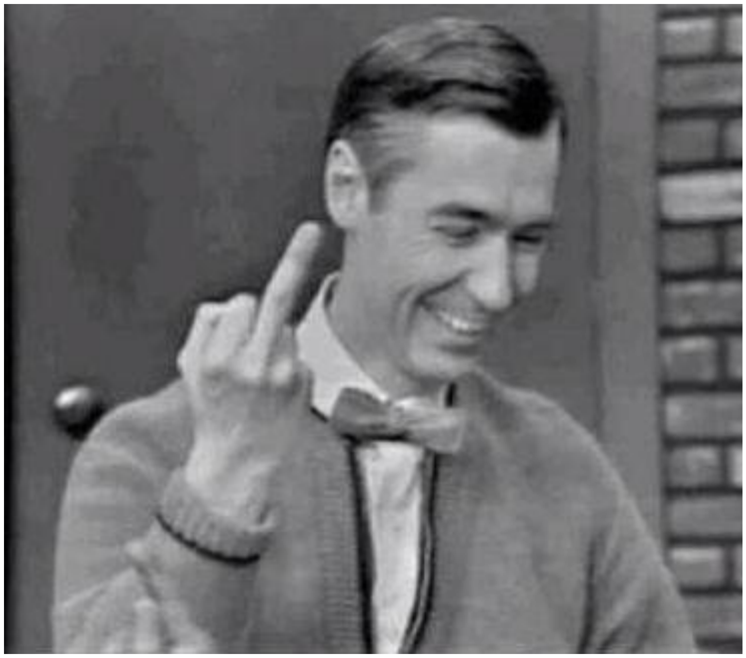
> “I still think we should buy them. He is on your schedule for Dec 15 or 16—we will need to sell him. I have a plan.”
>
> ~Anthony Noto (@anthonynoto), CFO of Twitter, struggling to keep tweets and direct messages separate

**On Conspiracy Theorizing**

> “I’m not going to censor myself to comfort your ignorance.”
>
> ~Jon Stewart




These markets are making me a little schizophrenic—like Jerry (Mel Gibson) in *Conspiracy Theory*—so this blog is really a group effort. But I vehemently denounce those who claim there are no conspiracies and who try to protect their beliefs by labeling the rest of us conspiracy theorists. I could cite famous folks who share my views, but on this one I stand alone: Men and women of wealth and power conspire. Period/full stop. If a market can be rigged, it is being rigged. If numbers can be cooked to advance an agenda they probably are being cooked. It is usually the glib intellectuals—guys like Cass Sunstein[ref 30]—who denounce conspiracy theories as intellectually childish and those who consider them as diseased. *You are trying to shut me up with a pejorative label.* I will let one of the iconic educators of our time respond:



**Investing**

> "You have to decide whether to look like an idiot before the crash or an idiot after it."
>
> ~John Hussman, Founder of Hussman Funds

I have changed little in my portfolio since last year. The only consequential change is that I resumed purchasing physical gold after a decade-long hiatus, increasing the total tonnage by approximately 20%. Owing to life's events, I have a dramatically enhanced cash position and a relatively small standard equity index. I am in *no* rush to alter the cash position. Rebalancing continues to occur primarily through market forces and by splitting my retirement contributions into equal portions cash and energy equities.

| | |
|---|---|
| Precious metals etc: | 21% |
| Energy: | 10% |
| Cash equiv (short term): | 60% |
| Standard equities: | 9% |

My net change in wealth at the time of this writing (12/15/14) of -1.2% is poor when compared to the S&P 500 (+8%) and Berkshire Hathaway (23%) for the third year in a row. Also for the third year in a row, the return on the S&P gains arose largely from p/e expansion fueled by gargantuan leveraged stock buybacks (see below). Those crazy enough to challenge the investor flash mob by shorting this market have absorbent Pampers slapped on what used to be their faces. Corrections elicited phrases like "levels not seen in two weeks."

Despite a very large cash and physical gold (+1%) positions, a small but strong standard equity position, and some added savings keeping me near even for the year, the carnage inflicted by vicious selloffs in the commodities smarted. At the time of this writing, my year-to-date results were influenced by gold (1%), silver (-12%), the XAU (-18%), the XLE (-16%) as a proxy for the energy sector, and the XNG as a proxy for the natural gas sector (-15%). Metal investors were bludgeoned by a late season sell-off and self-doubts and were berated by pretty much everybody on the planet, prompting CNBC to underscore the "vomiting camel" chart pattern (Figure 1). As social indicators go, that one could have called the gold market bottom.


Figure 1. Emetic dromedary pattern.

In a longer-term view, the total gain in personal wealth (including savings but *excluding* a large, positive one-time item) of 335% since January 1, 2000—the very challenging 15 years that followed the good times—compares favorably to the S&P (40%; *ex*-dividends) and Berkshire (329%, which *includes* accrued savings). It is going to take a crushing market event to regain a large lead I had on Buffett at one point. I remain a believer in the secular precious metal bull (albeit with white knuckles and self-loathing) for a rather simple reason: I think central bankers will destroy us. I see a secular equity low in our future, and the only way to exploit it is to park on cash and wait and wait and wait some more. In fact, that's one of the great advantages amateurs have over the temporally sensitive pros. I can stay irrational longer than the markets can stay liquid. I hope someday to exploit the hell out of opportunities in the energy sector that are being offered to us on a platter by the Saudis and the Obama administration. Until then, the Saudis can keep crushing the domestic energy markets (see below), and I will continue to white-knuckle my way through this mess.

> King Arthur: Look, you stupid bastard, you've got no arms left!
> Black Knight: Yes I have.
> King Arthur: Look!
> Black Knight: It's just a flesh wound.
>
> *~Monty Python and the Holy Grail*

**The Economy**

> "By 2011, it was clear—at least to me—that the Great Recession was no longer an accurate moniker. It was time to begin calling this episode the Lesser Depression."
>
> ~Bard Delong, economist at UC Berkeley, channeling James Rickards

> "I am delighted to join you at a time when, despite the effects of the severe winter weather, the economy is on the firmest footing it has been on since the recovery began."
>
> ~Charles Plosser, Federal Reserve Bank of Philadelphia, channeling David Lereah

We have the best economy money can buy. Fed governor John Williams suggested that "we are actually getting closer to getting at a normal economy." How would we know with you Fed plonkers in the way? According to David Stockman, total revenue has grown by just 31% since 2009 while profits have skyrocketed by 253%.[ref 31] We either did some serious regression to the mean from '09 to the present or will be doing so going forward. World-record profit margins[ref 32] suggest regression to the mean is in our future. I did a quick survey of the Forbes 100 and estimate that 17% are explicitly in finance. Others are called "diversified." I've gotta wonder if the economic gains are from various unconstructive economic pursuits (cf. Japan in the 1980s). *Caveat aequitas emptor*: if left unchecked, business cycles die of old age, and we are in the sixth longest (of 34) since 1854.[ref 33] If you want some serious doom porn, check out a few of Michael Snyder's Listicles of Horror (my moniker) posted at *The Economic Collapse Blog* and secondarily at Zero Hedge.[ref 34,35,36] The guy sees dead people.

As always, the difficulty is culling fact from fiction. In May, the ISM manufacturing indicators dropped precipitously and unexpectedly. A few hours after starching some more socks, ISM announced "my bad" and said that recalculations show that the economy is accelerating.[ref 37] Nonetheless, economic indicators began missing estimates by wide margins.

> Maxim: Facts miss pundit estimates rather than vice versa.

Mavens in the US blamed bad weather for their complete inability to hit the dartboard. Oddly, German pundits blamed their joblessness on good weather,[ref 38] whereas Goldman suggested that the Germans actually have strong growth . . . because of the weather.[ref 39] Fed governor Plosser says the economy is great "despite the effects of severe weather."[ref 40] The CEO of Walmart doubts the weather argument altogether, instead suggesting that everybody is unemployed and broke.[ref 41] Charles Dudley Warner insightfully noted, "Everybody complains about the weather, but nobody does anything about it." I suspect the vital signs of the economy are stable, albeit with help from a high-capacity monetary respirator.

The weather *is* whacking California. One of our breadbaskets is going bone dry owing to a multiyear, high-sigma (500-year) drought. Analogies to the Dust Bowl are inescapable.[ref 42] Some towns are shipping in *all* water by truck.[ref 43] California will soon run out of Nevada and Oregon's water. One orange grower bulldozed 400 acres of trees (why?), suggesting that "if this persists in the next year, the devastation . . . will be biblical."[ref 44] California halted fracking because it may be contaminating aquifers.[ref 45] (I must confess that of all the risks of fracking, destroying a big aquifer tops the list.)

Of course, housing is considered central to our economy. Maybe I have Assburger's syndrome or 80HD, but I go nuts trying to figure out whether housing is strong or weak. Choose an indicator and make any case you want. Owens Corning reported a weakness in roofing materials: the corporate numbers don't lie.[ref 46] (Just kidding. Sure they do.) Some plots show existing home sales rising; others show existing home purchases rising. Dudes: they're the same numbers—a kind of housing velocity that *may* offer evidence that the market is loosening finally. That said, 20 million homeowners are still underwater,[ref 47] rendering them professionally immobile. A nice list of the riskiest real estate markets in country shows Hartford, Connecticut, leading the pack with a potential downside of 35%.[ref 48] (Canada and England now make us look like pikers, however, given that their busts remain prospective.)[ref 49,50] And remember that iconic plot of mortgage resets foreshadowing (to those paying attention) the '08–'09 crisis?[ref 51] Well the resets are back—$200 billion worth of resetting home equity lines of credit (HELOCs).[ref 52] When the Fed finally normalizes rates, price discovery is gonna be a real bitch. The Fed never had an exit strategy.

Some argue that labor numbers are cooked like every other stat. That gets you labeled a conspiracy theorist (and got me labeled "pathetic"). John Crudele cites a Bureau of Labor Statistics whistle-blower claiming "I wouldn't trust any data from the Census Bureau."[ref 53] Who knows, but they seem contrived. Government indicators of employment aside, the labor participation rate continues to plummet (Figure 2). We appear to be unwinding the gains from the feminist revolution, except it's *men* hitting the sofa with pork rinds and a remote in hand.[ref 54] It was claimed and broadly disseminated that 11 states had more people on welfare than employed (despite rising numbers staffing welfare offices), but it might not be that simple.[ref 55] The rallying cry of the boomers—"I'll work till I drop"—needs to include "or until I lose my job." That said, the aging boomers are Hoovering up most of the new jobs (Figure 3).[ref 56] Gotta wonder whose couch the millennials will crash on when their parents go to the light with unpaid mortgages. The dichotomy of part-time versus full-time jobs continues to distort perception. By example, the 800K part-time jobs gained in June were offset by 500K full-time jobs lost.[ref 57] Total hours worked in this instance is crudely a wash (which is evidence of stagnation), but the lost benefits are definitely bad, and it has been disastrous long term (Figure 4). Walmart just cut health insurance for some 30,000 part-time employees,[ref 58] causing serious angst among those who hate Walmart out of principle. At least we have Obamacare.

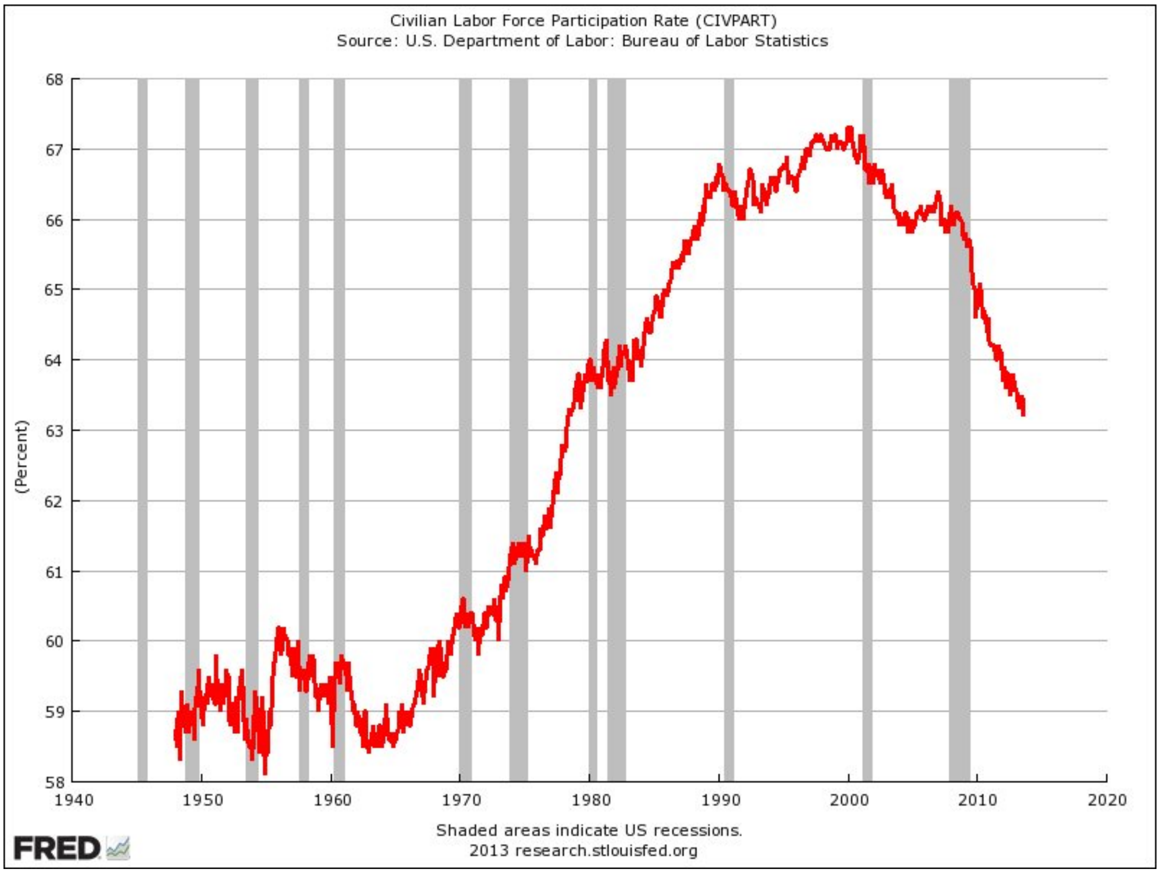



Figure 2. Labor participation rate.

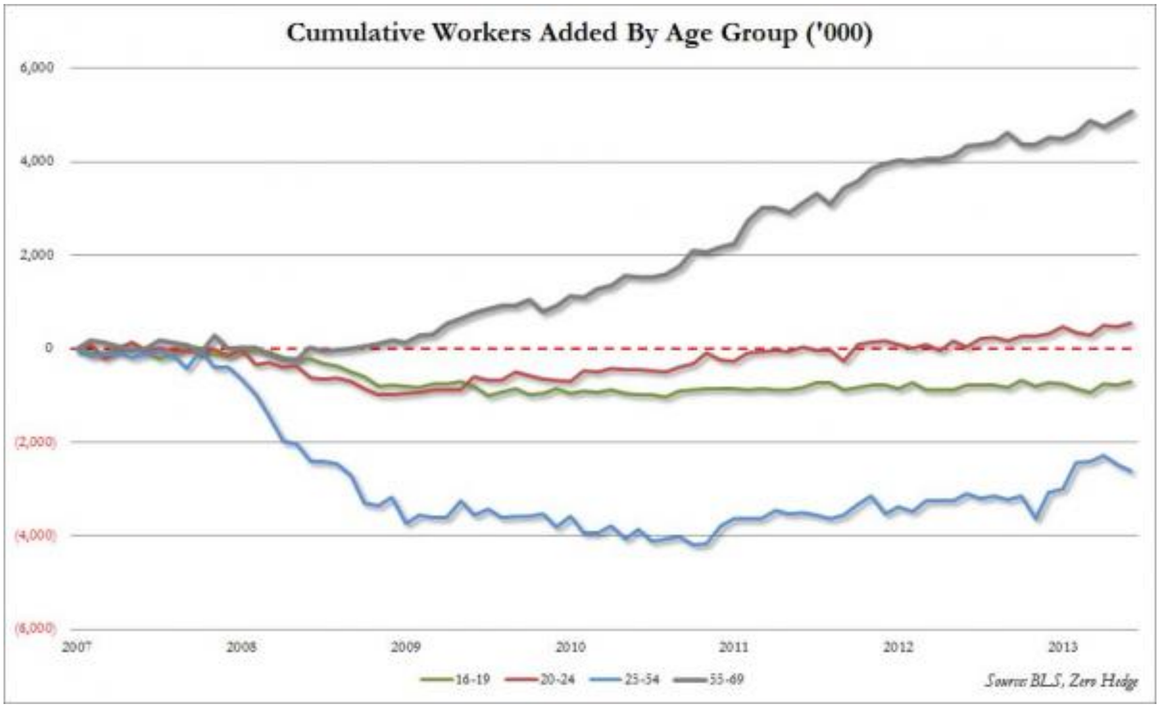



Figure 3. Joblessness by age.


Figure 4. Total hours worked.

Attempts to wrap my brain around the economy sometimes reveals moments of hilarity and absurdity. A “highly regarded study” found that children entering the job market today have the same chance of climbing the income ladder as children born in the 1970s.[ref 59] There is nothing quite like a decades-out extrapolation unguided by actual data. Prominent economist Justin Wolfers posted very cool plots showing that happiness correlates with earning power.[ref 60] OK. Money makes me happier too, but I am surprised that earning $500K gives you a 100% chance of being happy. As Einhorn said to Bernanke, “ How do you get to 100 percent certainty about anything?”[ref 61] Graphically slick charts like Wolfer's can seem very compelling and still be dubious (Figure 5).[ref 62] A Pew Foundation study concluded that teen pregnancies are good for the economy and wealth creation.[ref 63] They hedge their euphoria by noting that “it's obviously unrealistic to hope that the U.S. can return to the teenage birth rate of the Baby Boom.” One can only hope. As the cops often say, “spread 'em.”

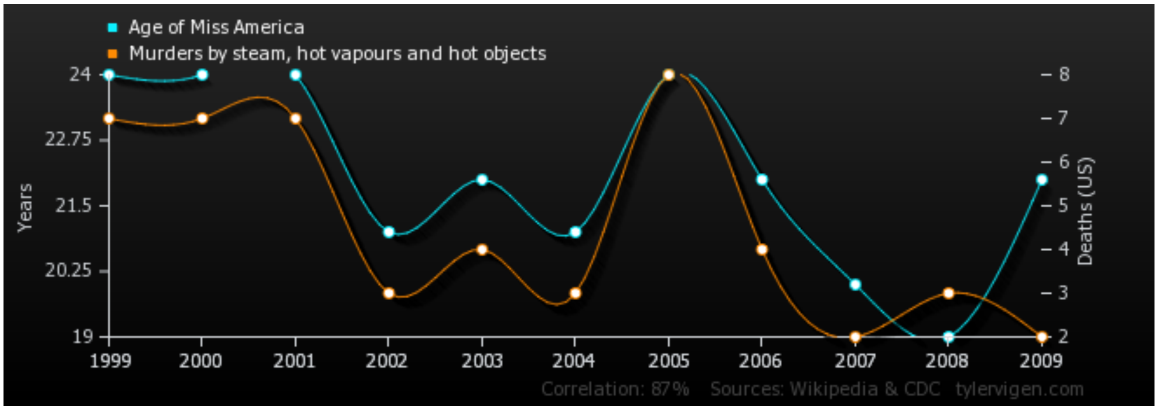



Figure 5. Obviously strong causal relationship between Miss America and deadly hot vapors.[ref 62]

**Bending, Breaking, and Broken Markets**

> “Looking at Wall Street stock and bond trader screens, the world looks like a model of stability.”
>
> ~Jon Hilsenrath

> “Given how sensitive markets are to headlines at the moment, there are no charts to send today.”
>
> ~Citi technical analysts

IPOs are always great entertainment because 80% of these nuggets of speculative bliss don't have earnings.[ref 64] Alibaba (BABA), the Amazon of China, opened at the monumental 20× sales and puttered around for a while until it caught a late-year ramp. The shares, however, are a derivative—they offer no direct claim to ownership or a stream of revenue—suggesting that any measure of valuation is meaningless.[ref 65] Twitter opened with a lot of fanfare, sloshed around, and finished the year marginally up. Peter Thiel noted that Twitter is a "horribly mismanaged company—probably a lot of pot-smoking going on there. But it's such a solid franchise it may even work with all that."[ref 66] Put in tight stops, Peter. The IPO of Vascular Biogenics opened, tanked, and was unwound—they took a mulligan.[ref 67] Presumably the wrong people got hurt. Soon after their IPO, the founders of GoPro cameras, circumvented the lockout period by placing shares in a family trust and selling them.[ref 68] Irritated investors sold the news but soon forgave them. Pre-IPO Snapchat looks like a real gem with no business model, no revenue, no profits, and a $10 billion valuation.[ref 69]

> "Sorry if you missed your IPO window. Don't worry, we'll blow up another one of these bad boys soon enough."
>
> ~Josh Brown (@reformedbroker), CEO of Ritholtz Wealth Management

Stock buybacks have dominated the market. According to the most recent Capital IQ data, the single biggest buyers of stocks in the first quarter were none other than the companies of the S&P 500 itself—$600 billion this year alone—simultaneously driving equity prices up and capital expenditures (Capex) down.[ref 70] How ironic. Years ago Peter Lynch used share buybacks as evidence insiders knew their shares were underpriced. Those were quaint times. Now they are used to boost share price by eroding balance sheets; investors profess to understand p/e ratios but are oblivious to balance sheet rot. Some estimate that, accounting for leverage, *all* earnings of the S&P are being plowed back into repurchase programs.

IBM is the poster child, buying back almost $40 billion while nuking its balance sheet with debt.[ref 71] Apple completely gutted its huge cash hoard buying back shares,[ref 72] which should stress holders of 30-year Apple debt issued when the balance sheet was strong.[ref 73] Oracle missed earnings and revenues but borrowed $10 billion to buy back shares.[ref 74] Oracle "returned" $21 billion of borrowed money in two years via buybacks and spent only $1.2 billion on Capex,[ref 75] making it essentially the largest royalty trust in the universe. Ford has $90 billion in *net* debt (debt minus cash) and is buying back shares—the functional equivalent of a leverage buyout . . . by the owners.[ref 76] Jonathan Glionna of Barclays explains: "There are a couple of reasons why companies do buybacks. One is that it seems to work; it makes stocks go up."[ref 77] Yes, Jonathan, and so did stock splits in the late '90s. This consequence of ultra-loose credit will unwind someday and inflict medieval pain on investors. One Zero Hedge poster suggested the FASB should allow buybacks to be categorized as Capex. Pure genius.

> "Few are ready to curb financial booms that make everyone feel illusively richer. . . . The temptation to go for shortcuts is simply too strong, even if these shortcuts lead nowhere in the end."
>
> ~Bank of International Settlements, June 2014

CYNK was the epitome of nuts. Only Zero Hedge was on this story at the outset.[ref 78] CYNK is a small media company—one employee, no business model, no revenue, possibly a post office box—that ran up 100-fold in months to a market cap of over $1 billion. Traders were monitoring its price relative to the four-second moving average. During the manic phase I tweeted that CYNK could "drop 50% in microseconds." Ten minutes later it dropped 30% in 30 minutes. Not a bad call for being off by three orders of magnitude. This one got embarrassing to the regulators, so they shut it down, trapping some traders.[ref 79] One poor fool—a *seriously* poor fool—had all his retirement savings in it. Two weeks later CYNK reopened at a humbling 86% lower price.[ref 80] It seems to have found strong support at $0.10. It's now a contrarian value play. The major risk is that the employee might quit.

The markets were interrupted daily by mini flash crashes—"meltups" or "meltdowns" owing to algos on 'roids. One of the biggest was the October 15th treasury meltup in which the yield on the 10 year dropped 0.4% in a few minutes—a testament to the stunning illiquidity of a once-bottomless market that finds its roots in Fed and central bank intervention (see below).[ref 81]

Concerns about valuation started to gurgle into the public consciousness. Buffet's favorite indicator—stock capitalization-to-GDP ratio—is now second only to that accompanying the 2000 bubble (Figure 6).[ref 82] Serious debates began as the Case-Shiller p/e ratio (CAPE) began to soar with the eagles—40% above the mean—prompting Robert Shiller to exclaim with his legendary histrionic flare "the US stock market looks very expensive right now."[ref 83] Henry Blodget, despite his reputation from the past, has become decidedly bearish—Hussman bearish—noting that he is "still nervous about stock prices" and suggesting that "stocks are likely to deliver lousy returns over the next seven to 10 years."[ref 84] James Montier says the market is 50–70% overvalued.[ref 85] John Hussman continues to hunker down for horrible prospective returns.[ref 86] He evaluates stocks like a state function—a path-independent analysis of where we are now and where we ought to be in 10 years, assuming mean regression. Because everybody is planning to sell at the top, Hussman astutely notes that *somebody* must own these assets on the way back down. For them it will be a mean regression indeed.

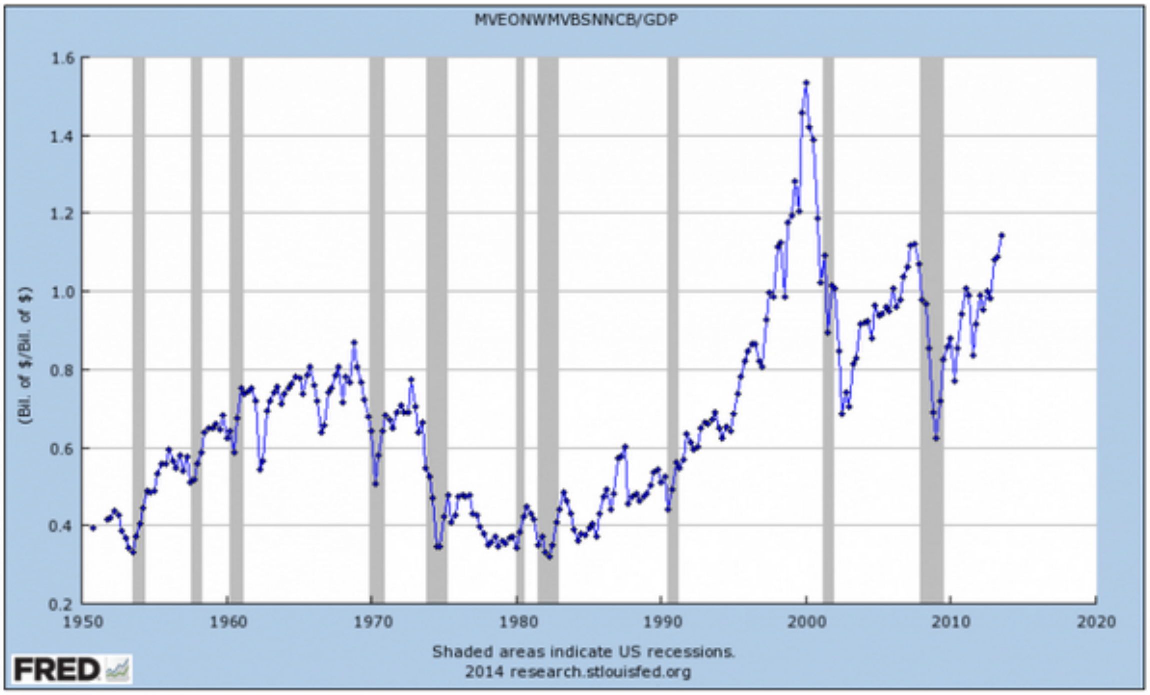



Figure 6. Stock capitalization-to-GDP ratio.

Of course, as valuations get high, the metrics soon come into question. Recall the eyeball and click-count alternatives? Articles began questioning the merits of CAPE.[ref 87] Alas, Lance Roberts, an analyst of considerable insight, noted that in his experience, the end is near when valuation metrics come under question. The Russell 2000 is sporting a p/e of 80. Michael Sincere's article "Why the Market Will Never Go Down" was satire at its finest,[ref 88] eliciting scathing reviews from those who didn't get it.

> "Negative earnings are excluded, extraordinary items are excluded, and P/E ratios over 60 are set to 60."
>
> ~Disclaimer in a biotech exchange-traded fund that reports a p/e of 41

Many watch for absurd signs of a top—magazine covers, Dennis Gartman going bullish, etc.—and they were there if you looked. Facebook bought WhatsApp for $19 billion, paying the equivalent of four years of user fees that are charged after a free trial year.[ref 89] It makes me wonder WhatsUp. Articles recommending using HELOCs to buy equities appeared,[ref 90] which is more evidence of a zombie apocalypse or the last days of disco than a market top. As a dog returneth to its vomit, pro forma earnings are being embraced again (sigh). The S&P 500 price has increased five times faster than GDP.[ref 90]

As of mid-September, 47% of S&P equities were in a bear market.[ref 91] With indices reaching new highs, this looks like the "market narrowing" observed in 2000 and again in 2007. There are planet-wide stretched carry trades—imbalances overtly engineered to generate profits for a select group. I detest the whole notion of carry trades. They are the root cause of many problems. The system is now so leveraged that abrupt moves in *any* direction by *any* market are high risk. Recall that a Russian bond default was the flapping butterfly triggering the market's fall to its knees in 1998 (mixed metaphorically speaking).[ref 92]

> "It is hard to avoid the sense of a puzzling disconnect between the markets' buoyancy and underlying economic developments globally."
>
> ~84th Annual Report of the Bank of International Settlements

> "Please make sure you have made the right decision."
>
> ~Warning on a 110-volt electric bath toy sold on Alibaba

Michael Lewis's interest in the Aleynikov witch trial[ref 93] morphed into a story about high-frequency trading (HFT) that became the bestseller *Flashboys* (see Books). This story is not new: Joe Saluzzi and Sal Arnuk detailed it in *Broken Markets* in 2012, but Lewis's gravitas and the cute subplots gave it legs. Soon it was fight night. Insider Haim Bodek took on HFTer Manoj Narang.[ref 94] Saluzzi took on an exceedingly annoying Irene Aldridge.[ref 95] The Katsuyama–O'Brien brawl on CNBC was the Thrilla in Manila, with Katsuyama landing the haymaker: "I believe the markets are rigged, and I also think you are a part of the rigging."[ref 96] Boom! O'Brien counterpunched, and CNBC bloviated for the remainder of the day that the markets are not rigged (as though they would know). O'Brien's counters were retracted under pressure from the authorities the next day.[ref 97] CNBC bloviation continues to this day.

> "Wall Street at its most socially useless."
>
> ~*The Atlantic* on HFT

This form of digital Marco Polo enabled by the trade routing firms skims money, but I am unconvinced that the retail consumer is paying the rake. What has my undies in a bunch is the role of the "algos" in the legendary flash crash of May 6, 2010 and numerous micro flash crashes documented daily by Eric Hunsader and crew at Nanex. The mouth-breathing regulators completely ignored them, declaring "quote stuffing doesn't exist." The HFTers claim to provide liquidity, but they are destabilizing the system. An 80-car pileup seems inevitable and will elicit endless ineffectual congressional investigations, a few fines, and no convictions. There is no better evidence that the risk–reward of HFT is tapering than Goldman's exit from the game as described in *Flashboys.*

> "I've been pleased with the transparency of the investment banking industry in my lifetime"
>
> ~Senator Ron Johnson during a hearing on HFT

**Precious Metals**

> "If you're capable of understanding the world, you have a moral obligation to become rational. And I don't see how you become rational hoarding gold. Even if it works, you're a jerk."
>
> ~Charlie Munger, 2011

> Andrew Ross Sorkin: Warren Buffet won't touch gold. Do you think he is wrong?
>
> Ray Dalio: I think he is making a big mistake.

> "There is no more important challenge facing us than this issue—the restoration of your freedom to secure gold in exchange for the fruits of your labors."
>
> ~Howard Buffet

As gold appeared to be headed south, I was asked by a prominent Keynesian and money manager, Mark Dow, what gold price would tell me I was wrong. Good question. The price action has made this an unpleasant ride for the last two of my 15 years of ownership, but it is not about price for me. I am a reluctant gold enthusiast and will remain so as long as political and monetary events dictate. In this section, I discuss a few that transpired this year. None has knocked me off my commitment to gold fostered by the folks at the Fed.

The market was not as savage (wildly sold) as it was in 2013, but there was no shortage of volatility. After a strong first-half start, I began to smell possible trouble when Goldman, Bank of America, and the World Gold Council began talking down gold in early summer. Of course, the former two are talking their books. The World Gold Council, despite its name, appears to bash the metal routinely. Soon thereafter, suspiciously large (billion-dollar) trades began appearing in the wee hours of the morning when poor liquidity leaves the market vulnerable.[ref 98] Of course, all of this was accompanied by schadenfreude from those who regret missing the first 10 years of the gold bull market. You could write volumes on the tits for tats between bugs and bears. Many of us simply trying to mitigate the perceived currency risk imparted by central banks find the attacks a little tiring.

> "The idea that the world is ending and the accompanying demand for guns, canned food, bottled water and gold is having difficulty attracting new adherents."
>
> ~Barry Ritholtz in the "Rules of Goldbuggery", *The Big Picture* blog

India was a bit schizophrenic. At first they took their foot off the throats of gold importers by removing 2013 import restrictions imposed ostensibly to control their balance of trade. I asked a prominent economist on the relative impact of importing gold and buying shares of Intel on the trade deficit; there is none. Alas, there were too many smugglers with too many body cavities to control. As the year progressed, however, restrictions reappeared, and smugglers got out the K-Y once again.

Gold repatriation continues to be a hot topic. In 2013 the Germans announced they would repatriate 700 tons of gold, but they retrieved only 5 tons from the US and 32 tons from France.[ref 99] Lo and behold, the Germans decided that they didn't really want it (sour grapes), with a spokesman declaring, "There's no reason for mistrust."[ref 100] Subtle hints to the contrary came from Bundesbank President Jens Weidmann: "[The US] will not transfer gold to Germany because we doubt whether it is really there."[ref 101] Seems clear enough. In a surprise announcement, the Netherlands managed to quietly repatriate 122 tons from the US to safety behind the dikes.[ref 102] France has expressed interest in repatriation now that Germany absconded with theirs.[ref 103] Belgium is pondering a similar move.[ref 104]

> "For central banks [gold] is a reserve of safety; it's viewed by the country as such. In the case of non-dollar countries it gives them value protection against fluctuations with the dollar."
>
> ~Mario Draghi, President of the European Central Bank

The Swiss peasants decided they wanted to take a crack at getting their gold back after the majority was sold off a decade ago under pressure from the IMF. (Pakistan, under similar pressure, told the IMF to لي لدغة, which Google translates to "bite me.") The overt 10% overnight putsch on the Swiss franc last year left a bad taste in their mouths. Thus, a Swiss referendum to mandate gold repatriation, maintain at least 20% of its reserves in gold, and never sell any of it (the latter being decidedly too rigid) loomed large. If passed, the Swiss would be repatriating at least 700 tons back to the Alps. "Not a problem," said an analyst at Deutsche Bank who noted that the Swiss can use gold swaps to move paper gold on and off the balance sheet every month. I'm not sure that's what the Swiss peasants were yodeling about. Of course, the referendum was violently opposed by the Swiss National Bank because it has a currency to debase. The week before the vote, Willem Buiter of Citigroup penned a report describing gold as a ridiculous reserve asset (Figure 7).

26 November 2014 | 14 pages

## Global Economics View

### Gold: a six thousand year-old bubble revisited

- Gold is a fiat commodity currency (with insignificant intrinsic value).
- Bitcoin is a fiat virtual peer-to-peer currency (without intrinsic value).
- Gold and Bitcoin are costly to produce and store.
- Gold as an asset is equivalent to shiny Bitcoin.
- Central bank fiat paper currency and fiat electronic currency are socially superior to gold and Bitcoin as currencies and assets.
- There is no economic or financial case for a central bank to hold any single commodity, even if this commodity had intrinsic value.
- Forbidding a central bank from ever selling any gold it owns reduces the value of those gold holdings to zero.

Figure 7. Screenshot of a Citigroup report on gold days before the Swiss referendum.

Buiter has been critical of the Federal Reserve's reckless policies, so this one came out of the blue for many of us, prompting a brief email exchange ending with this:

> Collum: “Your email box must be filled with detractors.”
>
> Buiter: “It is indeed.”

On the last trading day preceding the referendum—November 28th (Black Friday, ironically)—gold got bonked by 2.5%, silver by 6.5%, and oil by 10%—the Thanksgiving Turkey Massacre. It was a classic “swan dive” chart pattern (Figure 8).


Figure 8. Routine example of price discovery in the gold market.

I topped my personal best that day for “flushing money down a rat hole.” Like the Scottish vote for independence, the Swiss referendum didn't pass. Whether the selloff was in anticipation of a negative vote, engineered to *elicit* a negative vote, or unrelated to the vote is unknowable. Generally, however, voting power away from the powerful will run into opposition. The first trading day after the failed referendum was wild. The night the vote failed, gold tanked almost 4% and silver dropped 10%. Apparently, all that price appreciation before the vote—there was none—was getting unwound. I also didn't realize the Swiss rejected a silver referendum too. (Actually, Brevan Howard announced the closing of its commodity hedge fund that weekend too, possibly liquidating a large silver position.[ref 105]) Regardless of proximate cause, the shorts were putting on a full-court press. Gold investors were seeing nothing but bus axles.

Strange restoring forces were at work, however, causing gold bugs to get a strange feeling (like when climbing the ropes in gym class.) That same weekend—it was a busy weekend—India made a major policy reversal (again), removing mandated gold exports.[ref 106] Also, the gold forward offered rate (GOFO), touted as an indicator of demand for *physical* gold, had gone markedly negative and was now diving,[ref 107] evidencing short supplies of the metal. By the end of trading on Monday, gold and silver had massively reversed, closing with bold gains. Another sure bet bites the dust. By December 3, the grifters at the London Bullion Metals Exchange stopped reporting the GOFO.[ref 108] I'm sure it was for some macroprudential reason.

China and Russia continue to suck up gold by the pallet. Russia was selling treasuries to buy gold (see below).[ref 109] China is rumored to have imported 2,000 tons[ref 110]—the equivalent of 25% of the US's entire unaudited gold stash. The CPM group, another one of those gold-bashing gold organizations, suggested that the Chinese demand for gold is speculative hearsay,[ref 111] but guys like Koos Jansen—a new breed of gold analysts who understand the Asian market—enthusiastically disagree.[ref 112] Both China and South Korea are said to be building new vaults to hold this fictitious gold.[ref 113,114] China's gold demand prompted a shocking article by Alan Greenspan—*that* Alan Greenspan—describing China's motives for buying gold and the *merits* of gold.[ref 115] The man may have a marble or two left and is trying to disembarrass himself. This resurrected version of the much younger Greenspan is, once again, touting the virtues of gold as the only defense against central bankers like, well, Alan Greenspan:

> "If, in the words of the British economist John Maynard Keynes, gold were a 'barbarous relic,' central banks around the world would not have so much of an asset whose rate of return, including storage costs, is negative."
>
> ~Alan Greenspan, *Foreign Affairs*

A lot of guys with suspiciously strong Chinese affiliations and bold resumes are also advocating for gold:

> "China should now rapidly increase its gold reserves, without pushing up prices of the precious metal excessively."

> *~China Times*

> "Currently, there are more and more people recognizing that the 'gold is useless' story contains too many lies. Gold now suffers from a 'smokescreen' designed by the US . . . to maintain the US Dollar hegemony."
>
> ~Sun Zhaoxue, Former President of the China Gold Association

> "China should increase its gold reserves appropriately, and China must take every chance to buy, especially when gold prices fall."
>
> ~Li Yining, a senior economist at Peking University and a member of the Chinese People's Political Consultative Committee

We continued to witness the drop in gold inventories in GLD.[ref 116] Ignore those (of us) who think GLD is fractional reserve gold—rehypothecation at its finest—and ask a simple question: Why would GLD liquidate *any* gold in a sell off? If I owned a housing real estate investment trust, for example, a market selloff would reduce the price of the trust without a requisite liquidation of inventory. Provisions for arbitraging the price of GLD versus the price of physical gold in theory causes some adjustments in GLD around the margins,[ref 117] but the directions of what should be razor-thin adjustments could be up or down. This is amply illustrated by SLV, the analogous silver trust, in which a vicious two-year selloff caused *inflows* of silver.[ref 118] Given that only the multinational investment banks, the TBTF group, can trade GLD shares for physical gold—this *is* true[ref 119]—I've got two theories:

(1) The TBTF banks traded shares for the physical metal, presumably owing to demand for the clinky stuff in Asia.

(2) The collateral underlying the share price of GLD was vaporizing (going to China), causing the share price to drop. This idea is a little kinky but has been lurking on the Internet.[ref 120]

In a sense, the two theories are two sides of a push–pull argument. Either way, bullion rushing out of GLD and shipping off to Asia seems bullish for the future price of the metal. The volume of gold imports relative to the price of GLD shows a nice supply–demand relationship (Figure 9), but a correlation of demand going up with price—a Giffen good[ref 121]—wouldn't be nuts either.

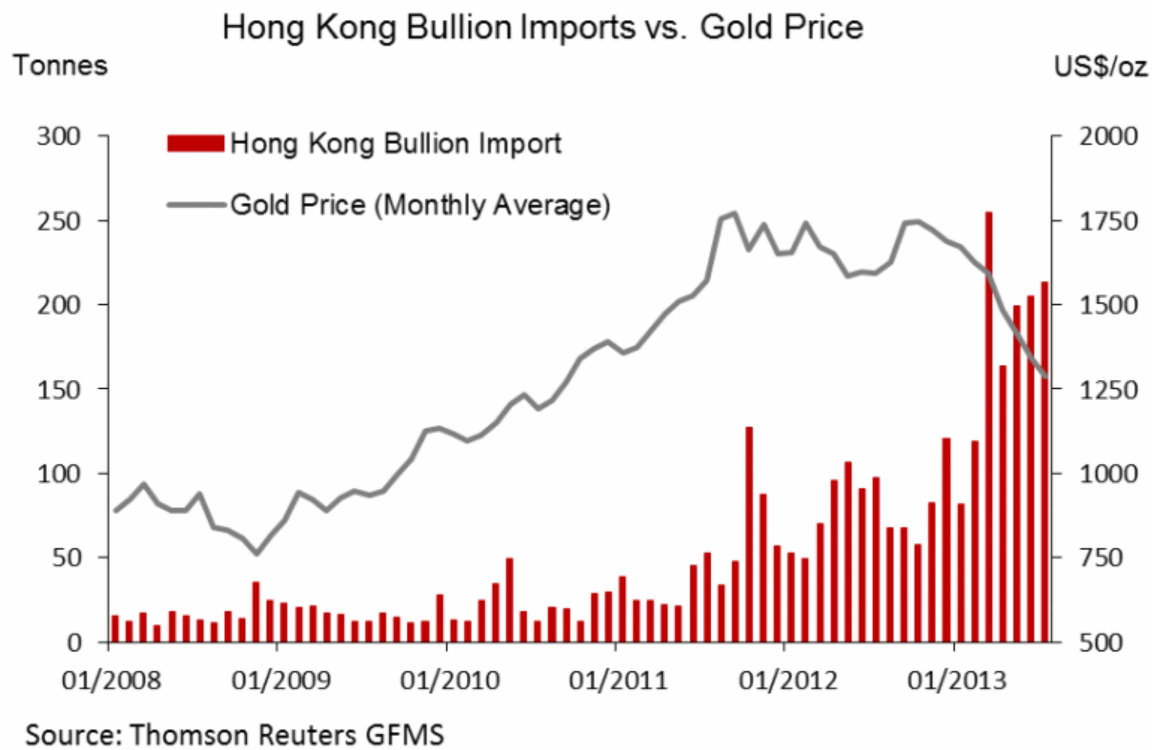



Figure 9. Gold imports through Hong Kong versus gold price.

Those accusing JPM of market rigging got a hoot when the London Gold Fix—the group of bankers that sit around fixing the price of gold each morning (duh)—was shown to be fixing the price of gold.[ref 122] They moved the rigging onto computers this year hoping that we could never imagine rigging a market with a computer.[ref 123] Soon precious metal riggers were jumping ship (from the rigging). The Queen of Darkness, Blythe Masters, resigned from JPM to become a market regulator at the Commodity Futures Trading Commission.[ref 124] No, really! She had claimed that "manipulating the metals market is not part of our business model. It would be wrong, and we don't do it," but nobody believed *that*.[ref 125] Going from rigger to regulator was way too much irony, causing her to reverse course within the week.[ref 126] Soon the five banks overseeing the century-old rig-a-thon—Barclays, Deutsche Bank, Bank of Nova Scotia, HSBC, and Société Générale—were formally accused by authorities of participating in the con.[ref 127] A *Financial Times* article on the scandal claiming the market was crooked as hell got yanked, but it had been saved. E-permanence is a bitch.[ref 128] Barclays offered up a sacrificial lamb, accusing Daniel Plunkett of the early morning spankings designed to make Barclays' customers "puke up their positions."[ref 129] The cockroach model says that Plunkett did not work alone. We are told the silver fix was a fix also.[ref 130]

So where do we stand? Many claim gold and silver inventories are tight, as reflected by backwardation, a linguistic abortion describing greater demand for physical in the near term. Inventories at the Shanghai Metals Exchange have plummeted.[ref 131] Our newest sovereign state, the Islamic State of Iraq and Syria

(ISIS), is about to release a gold currency—the dinar.[ref 132] Kiev (Ukraine) got IMF blood money (a loan) and bought gold with it,[ref 133] but more recent rumors suggest it is gone (*South Park* style).[ref 134] Ecuador pawned its gold to Goldman Sachs for a collateralized loan,[ref 135] which will likely turn into a net purchase at default.

The barbequed relic may have some life left in it. I think we are at the beginning of a seismic change in the global currency system, and gold will move to center stage in the new Bretton Woods Whatever. With other asset classes priced for perfection—all gains pulled forward—there may be serious price risk in gold medium term, but the opportunity costs of owning gold seem modest.

> "I did a lot of things at times with people on Wall Street, and I don't trust them. . . . Gold is always going to have a value and there will always be something there."
>
> ~Michael Franzese, former mafia boss (ba-da-bing)

**Energy**

> "If oil prices stay below $90 per barrel for any length of time, we will witness massive fiscal squeezes and regime changes in one or more of the following countries: Iran, Bahrain, Ecuador, Venezuela, Algeria, Nigeria, Iraq, or Libya. It will be a movie we have seen before."
>
> ~Steve Hanke, Johns Hopkins University and the Cato Institute

At the time of this writing, oil is hovering near $60 (Figure 10). The energy sector took a serious beating in the second half of 2014 owing to geopolitics, not geology. Goldman says the market is saturated (despite the rising price preceding the bloodbath),[ref 136] but interpreting Goldman reports is very difficult because Goldman always has a book being talked up. The CEO of Marathon Oil says he had been seriously underestimating the company's reserves.[ref 137] The CEO of Continental Resources, Harold Hamm, says the notion that the market is in a glut is nuts.[ref 138] He says it's all geopolitical. Others view it as a global economy in stress. Again, it seems likely (to me, at least) the global game of Tetris is accelerating to a finale.

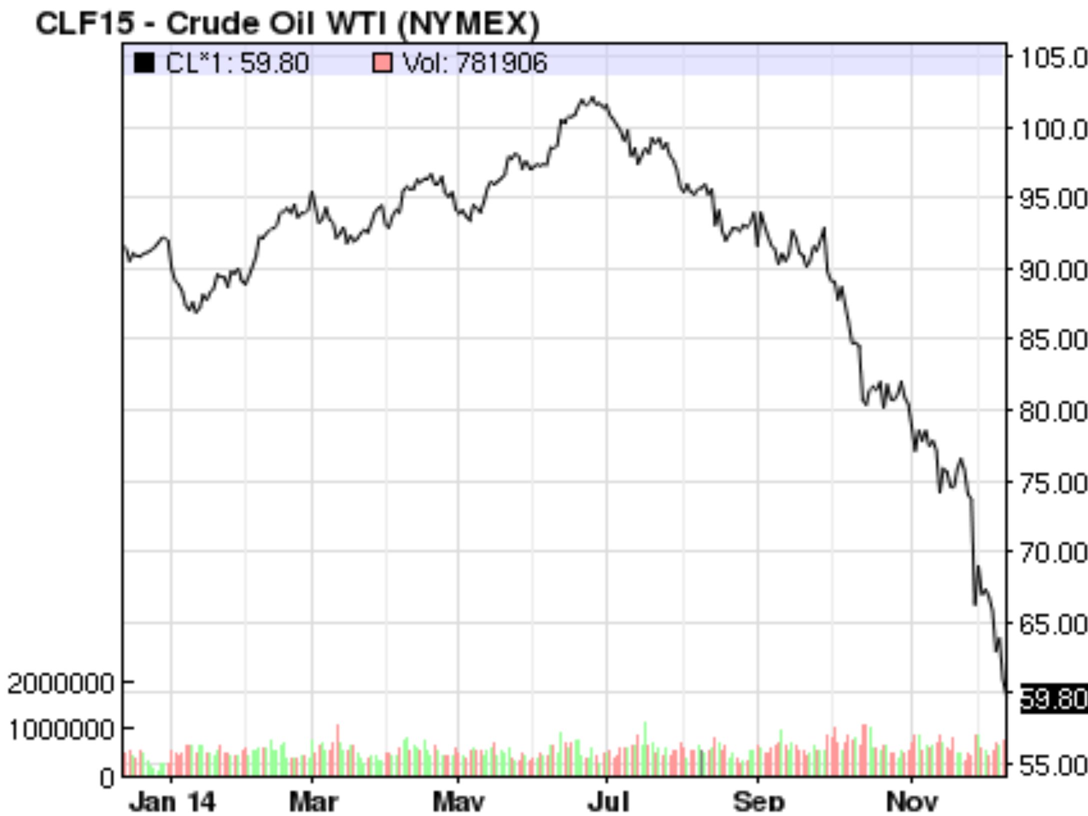



Figure 10. Crude oil price.

Meet the Frackers. The massive (40%) plummet in global crude prices has inflicted carnage on the marginal producers. Most are riddled with junk debt—supposedly over 25% of the entire junk bond market[ref 139]—and likely to serially fail. Before the collapse, the seven major producers were already witnessing falling liquids production.[ref 140] The good news is that once located in a big shale field, the frackers never hit dry wells. The bad news is that fracked wells have the life expectancies of gnats. The increasing output derives from an exponentially growing well count (Figure 11).[ref 141]

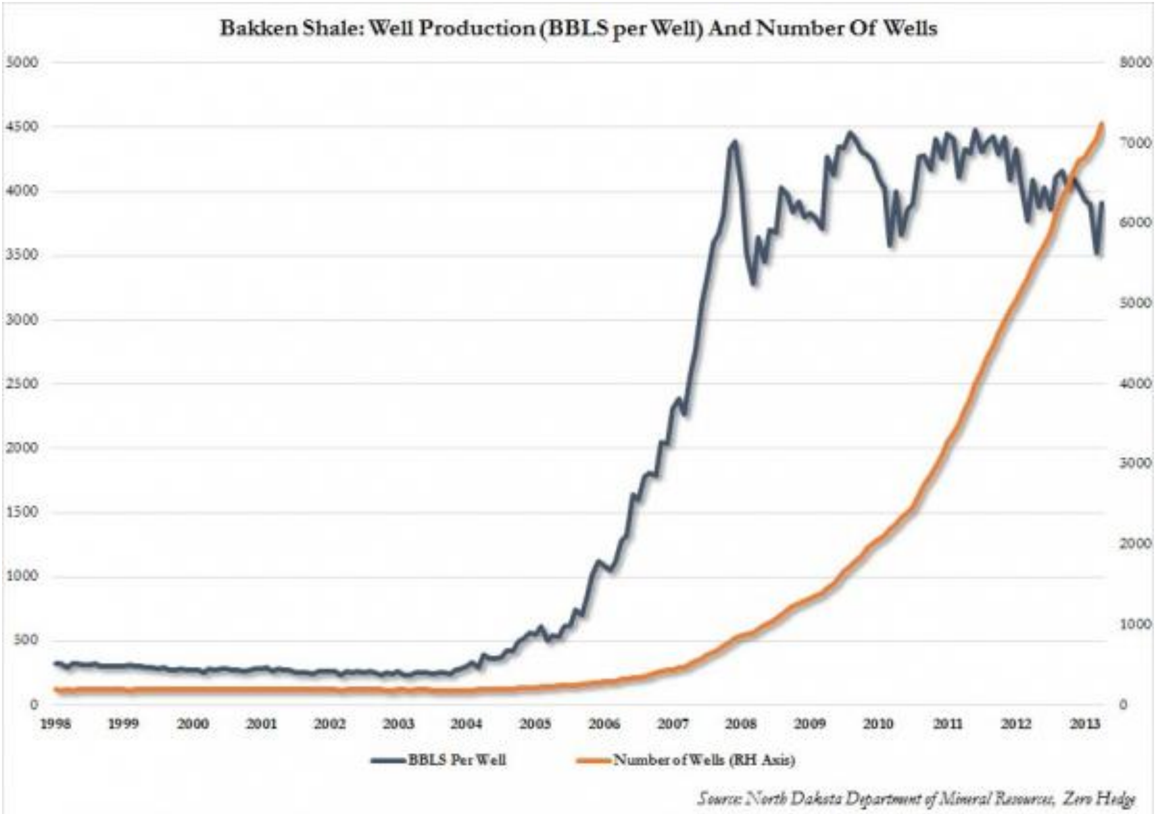



Figure 11 Output versus fracking well count.[ref 141]

I return to the geopolitics of oil in the section on Russia. I suspect, however, that the enthusiasm of the Saudis for low oil prices is temporary. Once they are done fracking my brokerage account, there could be an excellent entry into the energy sector as an investment. I am holding a large and growing position in energy and am tied to the mast. This time next year, I may be writing a lot more about the energy sector. At least we won't be suffering bogus announcements of strategic petroleum releases anytime soon.

**Personal, Savings, and Retirement**

> “[Malls] are trying to change; they’re trying to get different kinds of anchors, discount stores. . . . What’s going on is the customers don’t have the fucking money. That’s it. This isn’t rocket science.”
>
> ~Howard Davidowitz, flamboyant retail analyst

Every year I write about the dire situation in personal savings and retirement. This is as painful as watching a Nicholas Cage movie. I will keep it short this year because nothing has changed, it's not gonna change, and I'm starting to sound like Crazy Eddie. We have a large group of people who will spend their twilight years marinating in a grinding poverty that is altogether unfamiliar. After years of not saving—regardless of why or whose fault it might be—they are heading down the Niagara River in a barrel: *they are going over the falls*. Let's reconsider a few numbers.

The median retirement savings is $2,000.[ref 142] That is not a typo: 200 rolls of quarters. The assets in existing retirement accounts are broken down by age in Figure 12.[ref 143] Charles Schwab's numbers are more dire.[ref 144] One-third of the boomers over 65 still have mortgages.[ref 145] Those with equity in their houses are being pushed into treacherous reverse mortgages.[ref 146] Fidelity estimates that 48% of boomers report that they are not on track to cover the basics in retirement.[ref 146] Most of the others suffer self-delusion. It is said the average retirement age is 62, which is way too low. You eat what you kill. Few have created enough wealth to live another 35 years on the fruits of their labor. Boomers looking to retire early from a good job intending to pick up money on the side should reconsider.

| **Estimated Existing Average 401k Balances As Of March 31, 2013** | |
|---|---|
| **Age Group** | **Amount** |
| Gen Y (22-34) | $16,500 |
| Gen X (35-48) | $63,600 |
| Overall Average (Jan, 2014) | $101,650 |
| Baby Boomers (50-67) | $126,900 |
| All 55 & Over | $150,300 |
| Source: Fidelity and Vanguard | |

Figure 12. Balances of *existing* retirement accounts by age.[ref 143]

Let's take a deep breath and push forward. More than 30% of all new loans are subprime, which suggests that the debtors can't really afford the payments.[ref 147] Credit cards issued to subprime borrowers rose 39% in the first quarter alone.[ref 148] HELOCs are on the rise again.[ref 149] An estimated 60% of working-age Americans have less than $25,000 saved.[ref 150] One in six Americans depends on food stamps.[ref 151]

The self-deception has been institutionalized within the financial industry. Ya know those commercials that ask, "What's your number?" Well, the answer is a lot bigger than the numbers carried around in the commercial. Optimistic returns going forward—returns ignoring Hussman's dire analyses completely—suggest you can remove 4% of your retirement money without serious risk of running out. A million dollars spins out $40K per year. Now go look at what it takes to accrue a million dollars.[ref 152] It's a scary scenario for most. A mathematically challenged pundit rhetorically asked us to "consider a [50-year-old] worker making $50,000 a year, and saving 5 percent of it, with accumulated savings of $500,000."[ref 153] Can somebody tell me where that $500,000 came from?

Those overwhelmed by debt may not have screwed up. Maybe it was odious debt[ref 154]—debt incurred under conditions awful enough to provide a moral backstop to repudiation. Regardless, overwhelmed debtors have a binary choice that is gonna hurt either way: suck it up or default. The free market solution to default would cause the creditors to lose a lot of money. They will call for bailouts, which comes from savers and is most definitely *not* a market solution. I like the idea of branding bankers' foreheads with a $ (*Inglorious Bastards*) and dropping them in the middle of an ISIS stronghold. They would beheaded for trouble. Maybe that's too extreme.

> "You have a 25% chance of living 'til 93 years old, and you're going to need like $3 million to live on. Totally go to Starbucks now, it's fine."
>
> ~Josh Brown (@reformedbroker), CEO of Ritholtz Wealth Management

> "If You Don't Need It, DON'T BUY IT"
>
> ~1943 War Rationing Card

**States and Municipalities**

> "Detroit's industrial ruins are picturesque, like crumbling Rome in an 18th-century etching."
>
> ~P. J. O'Rourke

States and municipalities are still deeply underfunded—the situation will necessarily rectify over the coming years—but there were not many fireworks *this* year. The underfunded pensions continue to make news, with Illinois always at center stage. The Chicago firemen's pension fund is a $50,000 liability per Chicago household—probably far higher for households that are net payers of taxes.[ref 155] Illinois passed a reform bill to ease the state's burden,[ref 156] but who picked up that bar tab? Some of it may have been put back on the pensioners. Kankakee, Illinois, is in dire straights with a pension plan that is only 18% funded.[ref 157]

Michigan's auto woes continue to fester. Flint's pension plan is estimated to consume 32 percent of the $55 million general fund.[ref 158] The ultimate disaster zone—Fallujah on the Lake—is obviously Detroit. The cost to clear Detroit's blight using bulldozers (literally) is said to top $850 million.[ref 159] Even as a small government guy, I could endorse such conversions of crack houses to green space. Montages of Detroit's blight are legion. One shows decay over merely the last half-dozen years.[ref 160] Detroit was planning to shut off water to 150K mostly black residents owing to lack of bill payment.[ref 161] This is a no-win situation. Detroit thought it might pawn its art for $3 billion (below market price),[ref 162] although the legality of doing so while in bankruptcy proceedings is doubtful. I'm sure some wealthy Wall Street folks would gladly sign a rent-to-own agreement using profits from Detroit's debt restructurings. Detroit politicians—on the dole no doubt—tried to sign a crappy debt restructuring deal (again), and a judge said no.[ref 163] People often forget, however, that the primary function of bankruptcy is to distribute assets in cases in which there is simply not enough to go around. Maybe in prospective years Illinois will attack Michigan, eliciting some serious Krugman-esque stimulation of their respective economies.

Defaults on pensioners seem likely to be the horror story of the next decade or two. A Kentucky ruling on whether bankruptcy can negate pensions could change contract law by determining whether pension funds can be elevated to most senior creditors.[ref 164] A judge in the Stockton, California, bankruptcy will rule whether CalPERS is merely a servicing agency (moving it out of harm's way) and whether it can reduce payouts to the pensioners.[ref 165] Precedent is being set while pensioners are possibly being set up.

Sixteen counties in Northern California want to secede from California.[ref 166] Sounds like another brother-against-brother fight brewing. CalPERS is dumping its hedge funds, which made for great headlines.[ref 167] The fine print, however, reveals that hedge funds and private equity moneys constitute only 1% of its portfolio.

**The Bond Caldera**

> "The Fed has somehow managed to take the income out of fixed income and the yield out of high yield. . . . There are no interest rates to observe."
>
> ~Jim Grant, editor of *Grant's Interest Rate Observer*

> "Successful financial repression requires a widespread belief that conventional government bonds are safe."
>
> ~ Peter Warburton, Director at Economic Perspectives Ltd and author of Debt and Delusion

I obsessed over the bond market *all year long*. It appears that central bankers have pumped up a bond bubble—a Bond Caldera™—so hunormous that you can see it only from space. The global bond market is all trade, no investment. Try this exercise: Imagine buying bonds to clip the coupon for the duration of the bond—a real commitment to bonds as an investment. Would you park on treasuries returning 2.0% for 10 years? How about 2.9% for 30 years? Didn't think so. A lot can happen in 30 years.

Let's go way out over our skis: how about reaching for yield? That's always a brilliant idea endorsed by central banks the world over. With a little timing, you could have snarfed up the following portfolio:

| Source | Duration (yrs) | Yield |
|---|---|---|
| Cyprus | 5 | 4.8% |
| France | 10 | 1.3% |
| Germany | 10 | 0.8% |
| Greece | 10 | 6.4% |

| | | |
|---|---|---|
| Ireland | 10 | 3.2% |
| Italy | 10 | 2.3% |
| Kazakhstan | 10 | 4.0% |
| Mexico | 100 | 5.5% |
| Nigeria | 1 | 11% |
| Portugal | 10 | 3.0% |
| Puerto Rico | 10 | 7.0% |
| Rwanda | 10 | 6.0% |
| Spain | 10 | 2.2% |
| Spain | 50 | 4.0% |

*Japanese JGBs at 0.4% for 10 yr were excluded because the market no longer exists; the Bank of Japan buys 100% of the new issue.

Do any of those look good? Most are basket cases. Others are decent credit risks but offer pathetic returns. All are results of unfettered central bank credit. The only high-yield bonds in the bunch—possibly even the most attractive—were email-marketed by Nigerian princes. As Mark Gilbert of Bloomberg says, "You might want to dance near the door." *Everyone* is betting they can top-call this market and get out. I'd rather pick up nickels on the Autobahn. To reiterate Hussman's Truism: "*somebody must* own these assets" as trillions of dollars of risk morph into billions of dollars of detritus.

"Junk bonds have really gone to levels which under our analysis are pretty much the most overvalued in history."

~Jeff Gundlach, *The New Bond King*

"In my 20 years of managing high-yield bond investments, I've never seen so many signals that scream caution.

~Steve Blumenthal in *Forbes*

"For too long, markets failed to raise funding costs for countries with unsustainable policies. "

~Mario Draghi, hours before Portugal defaulted on a bond

China and Russia both backed away from the US treasury market this year: who picked up the slack? The *Belgians!* Yes. Those crazy waffleheads supposedly committed half of their GDP to buy $141 billion of US treasuries, becoming the third largest holder.[ref 168] If Belgium can bail out the US, then why doesn't Possum Trot, Kentucky bail out Detroit? Of course, somebody used Belgium as a proxy buyer because Belgium is also a basket case. I'm guessing the Fed was doing it; some say China. It could be any central bank, given that they are really one gigantic interconnected web of quantitative easing (QE).

2014 was the year of the taper—the Fed's long-awaited exit (Fexit) from grotesque QE monetizations. The bond trade of the century was on: *short US treasuries!* Problem is that somebody forgot to tell the bond market: the taper ended (sort of), treasuries soared, and interest rates went even lower. Excuse me while I kiss the sky. Maybe the Belgians blew through the stops. Or, better yet, maybe it was those two Japanese guys caught carrying $134 billion in bonds over the Italian-Swiss border back in 2009.[ref 169] This one wasn't a dud for those who front-ran the taper by shorting bonds. That'll teach them to bet on a sure thing.

> "If I traded bonds, I'd have been bankrupt seven years in a row. I just don't geddit."
>
> ~Mark Gilbert, *Bloomberg*

How is it possible to pull off the taper without event? I have a theory that is without support—a hunch of the highest order: The Fed was able to decouple *temporally* headline risk—the Fear Factor—from actual liquidity risk. It would require help from other central banks. Curiously, within hours of the US-centric QE coming to a close, Bank of Japan (BOJ) governor Kuroda surprised the markets (and other BOJ governors[ref 170] apparently) by announcing a huge QE. Soon thereafter, Mario Draghi announced the Eurowanker variant.[ref 171]

Bill Gross stunned the world and the bond market when he moved from Pimco to the two-faced Janus.[ref 172] (Nice truth-in-logo, guys.) Apparently, that sweet old man who wrote the folksy monthly reports was actually a bit demonic at the office, noting wryly to Mohamed El-Erian, "I have a 41-year track record of investing excellence. What do you have?"[ref 173] Ouch. I wouldn't be shocked if Gross's divorce from Pimco was akin to Sam Zell marking the top of the real estate market almost to the minute by selling his $38 billion real estate empire. For a while, it looked like Pimco liquidations by Gross's groupies might eviscerate some bond indices, but price-insensitive central banks can buy up any slack.

Corporations continued a record bond-issuing spree. Examples of unappealing offerings include Caterpillar (50 yrs at 4.8%), Hasbro (30 yrs at 5%), and Target (10 yrs at 3.5%). If these and other large-cap companies are such stellar credit risks, why did they need to borrow money? Stock buybacks—almost $1 trillion of stock buybacks![ref 174] This form of bond-denominated stock monetization (BDSM) is a modern day variant of a leveraged buyout. Clearly the equity buyers find per-share rises in earnings well worth rotting their balance sheets. Stock buybacks are the new stock splits.

Telltale signs that the bond market is unglued are legion. State tobacco bonds were used to pull tobacco settlements forward, but buyers failed to anticipate drops in cigarette sales.[ref 175] An index reflecting Mexican corporate junk bonds dipped to a 5.2% annualized rate.[ref 176] How do you pass on those? It appeared as though the junk bond market was about to crack open in the summer, but paroxysms gave way to renewed tranquility. US junk bond indices dropped below 5% yield. As my fingers prepare to release the keys, however, the junk bond market is being crushed by the energy sector. The Fed also wants more high-quality assets for stability in a crisis and has inexplicably excluded munis from that category.[ref 177] Muni crisis in 3...2...1...

The big story receiving no attention is that the Fed is considering exit fees—penalties—for removing assets from bond funds and some money market funds during times of stress.[ref 178] Nobody bought into those funds with that rule in place. You would think that such fees would cause the bond market to collapse. You pass that law, and it will be a time of stress. Restricted withdrawal on just one fund—akin to breaking the buck—could cause a global contagion.

I've run into seemingly savvy investors who swear off bond funds, instead buying the bonds. They defiantly declare that they can't lose principal because they won't sell them. This baffles me to no end: aren't they just failing to mark their portfolios to market, whereas the bond funds have no such luxury? If rates double, dudes, you've lost a lot of principle. You just aren't calculating it. Cliff Asness pointed me toward his comparable analysis.[ref 179]

Why do I think it's a bond bubble—a Bond Caldera? Because short-term interest rates (some now *negative*), quantitative easing, and mountains of affiliated carry trades necessarily inflated it. Normalization of first-world sovereign overnight rates to, say, 4%—not exactly a Volcker-esque nightmare scenario—would demand a stunning reduction in principal.

So how is this going to play out? Jack Bogle says, "The best estimate of returns of bonds going forward is today's interest rate . . . with a 0.91 correlation."[ref 180] Sounds easy enough, but this is the *nominal* return and, as noted above, 2% nominal return on treasuries won't cut it. We have pulled all imaginable returns forward. Is it good news if the bond market holds steady and we earn dismal *nominal* returns for eternity? If so, projected returns on 60:40 equity-bond portfolios will stink unless equities soar, and that is not going to happen with current nosebleed valuations (see *Broken Markets*). The best-case scenario for *future* bond buyers and the worst-case scenario for *current* bondholders is a bond rout—serious repricing and affiliated rising yields. In the event of a bond crisis, equities will not be very perky either. Thus, unlike in '08–'09, when soaring bond funds offset tanking stock funds, the market will experience simultaneous paroxysms. It's unclear whether cow blowing or jawboning by fluffers Draghi, Bullard, Yellen, or Kuroda will put Humpty back together again.

> "The age of getting rich quickly is over as is (most likely) the age of getting rich slowly."
>
> ~Bill Gross, former bond king, Janus

> "We sympathize with traditional stock and bond investors, who are faced with extremely poor choices today."

> ~Paul Singer, Elliot Capital Management

To silence those who will bleat that nobody saw an epic bond crisis coming, I leave you with a few more warnings from some of the old mossbacks of finance:

> "Leveraged loans to private equity are not just flashing red but have a wailing siren."
>
> ~*Financial Times*

> "A skeptic would have to be blind not to see bubbles inflating in junk bond issuance, credit quality, and yields"
>
> ~Seth Klarman, Baupost Group

> "I can't recommend buying any long-term bond as the yields stink relative to inflation."
>
> ~Peter Boockvar, Lindsey Group

> "This is a game we won't even bother playing."
>
> ~Tim Price, PFP Group, on the bond market

> "Most government bondholders are unlikely to achieve a positive real return over the medium-to-long-term from this starting point."
>
> ~Jim Reid, Deutsch Bank

**Argentina Versus the Bond Vultures**

> "The Argentine Republic will meet its obligations, pay off its debts, and honor its commitments."
>
> ~Axel Kicillof, economic minister of Argentina

> "If I were the Argentine government, I would make all participants believe that I was willing to push everyone over the proverbial cliff at the end of July to improve my negotiating position."
>
> ~Kyle Bass, Hayman Capital

There are always nuggets of folly in Argentina. The day the Argentine Central Bank's reserves accounting was questioned publicly, a massive fire destroyed a warehouse archiving documents from the entire banking system.[ref 181] That's funny stuff. Alas, just like Obama's benefactor-turned-ambassador who has never even visited the place,[ref 182] South America doesn't do it for me.

What caught my attention, however, was Paul Singer of Elliot Capital Management and a cadre of "vulture funds" raiding Argentina's debt markets like pox-riddled conquistadors.[ref 183] The media excoriated Singer et al.[ref 184,185] This battle would be the end of capitalism, they decried. How will we ever repeatedly bail out poor third-world countries (read: global banking cartel) ever again? The media was clueless and wrong.

The backstory: Argentina has been defaulting on debts since 1824.[ref 186] Economist Steve Hanke estimates that it has been in default for 35% of its history.[ref 187] A rolling loan gathers no loss. The default in question, however, occurred in 2002 on bonds issued in 2001. Whoever lent them *that* money has the intellectual firepower of an empanada. Singer and the Gouchos bought mucho cheap debt, waited for the banks to restructure it, and then told Argentina no way were they settling for a few pesos on the dollar. Argentina said, "Yes way!" but that didn't work. Normally, a collective action clause allows a majority of creditors—the banks—to force all creditors including the "holdouts" to accept the new terms. Argentina's bonds, however, did not include this clause. Oops. Specifically, the rights upon future offers (RUFO) or "pari passu" clause mandated that Argentina could not settle with the holdouts without paying *all* creditors off at the *same* rate.[ref 188]

So why not just cut the crap and default? It's not like it would tarnish their stellar Fico score. Of course, that's just crazy talk because the banks wouldn't get paid, and the banks bought a lot of politicians to get paid. US courts, however, ruled that *any* form of settlement would be in violation of RUFO. Apparently, the bankers should have budgeted more for the judges (an unforced error). Argentina protested that the court ruling "is merely a sophisticated way of trying to bring us down to our knees before global usurpers."[ref 189] And your point is?

Argentina went jurisdiction shopping. It considered having the investment banks pay Singer, but this was deemed RUFO forbidden.[ref 190] Argentina tried to get the court to order payment so as to claim that such a mandate negated RUFO. The Bitcoin guys were champing at the Bit to offer their services. Alas, payments of any kind in any way would trigger RUFO. Singer bet that the global banking cartel would find a way to pay them: they bet on moral hazard.

Only Hanke seemed to get it right by accusing Argentina of serial defaults and giving a thumbs-up to a default.[ref 191] The upside of a default is that everybody—Argentina, the banks, and Singer—would get schooled on risk. There was no solution, and on July 30th Argentina defaulted.[ref 192] The high-yield bond market at large didn't really like it. The St. Louis Fed (@stlouisfed) tweeted "Why did the Argentine peso fall following Argentina's default?" (They are actually *paid* to say stuff like this?) Meanwhile, the world continued rotating on its axis. Rumor has it that Singer has his sites on some hard assets.

Bottom line: If you lend to countries like Argentina in a *free-market-driven* credit system, you will quite justifiably lose your shirt. Because it's probably not actually *your* shirt, you should also lose your job, your freedom, and possibly your genitalia. Repeatedly lending to third-world countries aided and abetted by bribed third-world politicians destroys more lives than the collective efforts of serial killers. You should probably have your ass colocated with a prison cell.

> “Argentina’s professed willingness to negotiate with its creditors has proven to be just another broken promise.”
>
> ~Jay Newman, spokesman for Elliot Capital Management

**Inflation Versus Deflation**

> “Perhaps it is one secret of their power that, having studied the fluctuations of prices, the [bankers] know that history is inflationary.”
>
> ~Will Durant

I was *positive* a determined central banker could trigger inflation, and contemporary central bankers are a determined bunch. Austrian economists predicting rampant inflation were eviscerated this year, however, as the deflation drumbeat became deafening. Central bankers are wracked with apoplithorismosphobia (irrational fear of deflation). I am still very much afraid of inflation but began to wonder: Can you jam money into the system without triggering serious inflation? Can huge volumes of dormant money with low velocity be sopped up before it becomes high-velocity inflation?

Now for the confession: I don't understand the inflation–deflation debate at the most rudimentary level. How can you describe something so extraordinarily complex using binary language? Try describing the weather or the Great Barrier Reef using only two terms. Not easy, eh? Possibly for this reason, the inflation–deflation debate has elicited some of the most bizarre financial analyses I've ever read. Let's begin with a couple deflationary warnings from two *very* smart and respect-worthy guys:

> “The new reality is that we currently stand face-to-face with the very deflation risk that just about everyone denied could ever happen.”
>
> ~Steen Jakobsen, Saxo Bank

> “The Fed and the ECB have failed to prevent a dreaded replay of Japan’s deflationary template a decade earlier in the West. The Ice Age is once again about to exert its frosty embrace on markets as investors wake up to a new and colder reality.”
>
> ~Albert Edwards, Société Générale

Europe is said to be staring into the abyss occupied by Japan. US central bankers are developing nervous ticks. This all sounds so macroprudential (a content-free Yellen term). The dialog spans the gamut of pensive to inane. Let's begin with some of the Masters of the Universe—mostly central bankers—in their own words.

Bullard is "forecast[ing] rising inflation," which is why he is "concerned about declining inflation expectations." Mmm-kay. Whatever you say, Jim. Kocherlakota tells us we should be concerned about "below-target inflation" without clarifying from what dark place the Fed pulls its target. From recently released Fed minutes, we find that Bernanke thinks "low inflation is generally good" but that a "2% inflation target may be too low." Fed governor Charles Evans declares "2% is not the right number." I agree with Chuck, but I doubt we would agree on why 2% is not *my* number. With deflation risk in mind, a Fed report warned us that "consumers have decided to hoard money," presumably in small banks called "hoardings and loans." Krugman—a central banker in his dreams—warns that "the great danger facing advanced economies is that governments and central banks will do too little," which is a complete 360 for him. He also noted that "inflation redistributes wealth down the scale of both wealth and age, while deflation does the reverse." Poor folks love rising prices at Walmart. Adam Posen, president of the Petersen Institute, explains this odd consumer preference: "Food is one component of consumption. A rise in its cost is not inflation."

Whether journalists are duplicitous or merely duped by macroeconomists is unclear, but they take in these nuggets of ambiguity from the authorities and spit out some seriously content-free content. Let's start with *The Economist*—the gateway to higher economic reasoning—by blowing right through an extraordinary flowing montage of quotes: "the biggest problem facing the rich world's central banks today is that inflation is too low. . . . Politicians and central bankers are not providing the world with the inflation it needs. . . . The perversity of the low-inflation world is shown by the fact that the catalyst for the latest deflation scare is in itself a largely positive development. . . . The belief that goods bought tomorrow will be cheaper than goods bought today chokes consumption." And then there was this little treasure: "You can have too much of a good thing, including low inflation. Very low inflation may benefit important segments of the population, notably net savers." I respectfully suggest you guys step back and take a deep breath or change your name to one that better reflects your content.

Other media outlets had their 10 minutes of glory. The *Financial Times* warned that "it can be extremely difficult to increase the rate at which prices rise." God forbid. *Bloomberg* noted that "an inflation rate approaching zero is bad for the economy because . . . companies' inability to raise prices hurts profits." So if profits need inflation, are they *real?* The *Wall Street Journal* worried that "the recent period of very low inflation could persist longer than first thought and may threaten the currency area's economic recovery." It was a Yahoo Finance headline, however, that captured the weapons-grade stupidity of the discourse on deflation:

> “Golden Years look dark as lower inflation eats into Social Security.”

Wait . . . *what?* Jeepers. It astonishes me that people actually penned these ideas. I know bats spewing shit less crazy than that. I personally don't need any inflation whatsoever. I like dropping prices, living large on less, boosting the GDP like an Italian (blow and hookers). Here's a simple sanity check: name *one* example of a good that fails to sell because it has gotten too cheap (besides equities, that is.) Raoul Paul Ilargi of *Automatic Earth* asserted that real deflation is not about dropping prices but about how much you have to spend. That's a keeper.

Let's bring a single member of the opposing team—the Sultan of Swat—off the bench:

> “I remember sitting in class at Harvard being told by a fiscal policy expert that a little inflation was good for the economy. All I can remember after that was a word flashing in my brain like a yellow caution: bullshit. . . . This kind of stuff that you’re being taught at Princeton disturbs me.”
>
> ~Paul Volcker, former FOMC Chair

Some argue the definitive resolution to the inflation–deflation debate comes from the Billion Price Project (BPP) of Roberto Rigobon and big-brained economists at MIT.[ref 193] By monitoring over a billion prices using NSA-quality robotic software, they amass a sample size on daily price fluctuations so enormous that no sane person could contest the final read on inflation. Not so fast, Bucko. How do they statistically weight the prices? How do you compare the price of toothpicks to college tuition? Soaring toothpick prices are never going to trouble me; I'll use my fingernail. A billion prices need a billion statistical weightings to reflect the magnitude of the prices, the percentage of one's income dedicated to the purchases, and the optionality of the purchases. That is where error and even chicanery could lurk. I asked Rigobon how they weight the prices, and he courteously told me that info is “proprietary,” which is a euphemism for لي لدغة. In chemistry, a manuscript that describes a new method without providing any methodology gets rejected. The Billion Fudge Factor Project (BFFP) is a nonstarter without details.

Curiously, when I posted my concerns about the Billion Price Project online, somebody said the index went live, came in way too hot relative to the consumer price index (CPI), was brought back to the shop for a tune-up, and was re-released in the new CPI-friendly form. This, at present, is an unsubstantiated rumor, but back-testing to the CPI would be *very* tempting and would *completely* negate the basic premise. Also, I can name 50 items whose prices have profoundly influenced my lifetime of consumption; the other 999,999,950 are largely white noise. According to Daniel Kahneman (*Thinking Fast and Slow*), we *must* ignore the white noise.

Consumers deeply understand that which eludes central bankers and maybe even MIT economists: CPI inflation is very real. Prices are going up and package sizes are shrinking. John Williams of Shadowstats would argue that inflation is seriously underestimated.[ref 194] I don't know if he's right, but his methodology is clean and simple. Oddly, even data from the Fed suggest high consumer inflation.[ref 195] Paul Singer of Elliott Asset Management suggests that “the arithmetic of government statistics (jobs, growth, and inflation) is distorted and dishonest almost beyond measure.” Philippa Malmgren, former member of the President's Working Group on Financial Markets, refers to “a growing gap between what central banks are telling us about inflation versus what people are really experiencing.” The technical term for those who doubt government inflation numbers is “inflation truther,” which roughly translates to “ignorant peasant with a walnut-size brain.” Someone who uses “inflation truther” pejoratively is technically referred to as an “asshat.”

Lets call a spade a spade. Contemporary central bankers care deeply about CPI inflation because consumers *must* get less than expected *somehow* to exit this morasse of debt. What the bankers *fear*, however, is the deflation of assets on member banks' balance sheets. They *fear* the bad deflation—the kind that leads to defaults on loans rather than just cheaper goods—because of bank failures and because it shows that the central banks royally screwed the pooch. According to Austrian business cycle theory, the bigger the boom the bigger the bust. We are now at the end of a monumental bank-sponsored credit boom; brace for the Red Bull-sponsored bust. The inflationary credit boom is the disease; deflation is a symptom. We are being relentlessly waterboarded with liquidity by central bankers and fed propaganda with rectal feeding tubes. Charles Kindleberger, the world's expert on bubbles in his day, noted that bubbles arise when excess credit is jammed into a system with decaying fundamentals.[ref 196] Decaying fundamentals? Sound familiar? If somehow all this money hoarded at the Fed escapes into the wild, take cover. Either way, proclamations that “it's a dud” seem premature. I highly recommend *Banking and the Business Cycle* (1937) for a compelling description of what happened the last time we hit this bridge abutment.

**Wealth Disparity**

> “Printing money out of thin air does not increase wealth, it only increases claims on existing wealth.”
>
> ~Charles Hugh Smith

In the olden days, claims that the rich were getting richer and the poor were getting poorer were a thinly veiled rallying cry for class warfare. Thomas Sowell reminds us that a growing economy lifts all boats, *and* those at the bottom strata percolate up generationally from garment worker to bookkeeper to doctors and lawyers (well, maybe just doctors). It feels different now, and the angst over wealth disparity resonates with growing numbers of adherents. It is no longer just the dregs of society but the increasingly struggling middle class, or what I prefer to call "the median class."

> "Only the wealthy can afford a middle-class lifestyle."
>
> ~Zero Hedge

The contrasts are stunning. While 53% of adults earn less than $30,000 per year,[ref 197] the rentier class—big-gun money managers—are muffin topping out at $3 billion.[ref 198,199] David Tepper earned almost $500K per hour. Stevie Cohen ranked second in earnings as a full-time defendant for insider trading. The *median* retirement savings of a working-age adult is $2,000, yet we've got folks with the cash to pay for brain surgery on goldfish,[ref 200] $60 million Steve Martin–like balloon art,[ref 201] $500K watches,[ref 202] and $2,000 glamburgers ("gluttonburgers").[ref 203] A full 47% of millennials are using >50% of their paychecks to pay down debt.[ref 204] Twenty percent of US families have no employed family members.[ref 205] This is a problem demanding solutions for which none are obvious. The elite billionaire society, Beta Kappa Phi,[ref 206] is dominated by the rentiers rather than wealth-creating capitalists. This is not about Bill Gates or Michael Dell. Wealth inequality is about the inordinately high pay for those who don't actually create wealth and the inordinately low pay for those whose toils do. We have reached the apex of another gilded age.

> "It's not just enough to fly in first class; I have to know my friends are flying in coach."
>
> ~Jeremy Frommer, Carlin's chief executive

> Seven Habits of Highly Successful People: skiing, yachting, snorkeling, golf, polo, dinner parties, and shopping.

We will be tempted to redistribute. But ramping up the minimum wage by fiat quickly ushers in the 360-burger-per-hour robot.[ref 207] "Our device isn't meant to make employees more efficient," said Momentum co-founder Alexandros Vardakostas. "It's meant to completely obviate them." (Note the careful use of "obviate" rather than "replace.") Debates about whether we should throw money to the rich or money to the poor, however, beg the key question: why are we throwing money at all?

> "A smoothly operating financial system promotes efficient allocation of saving and investment."
>
> ~Janet Yellen

Killin' it Janet! But then she went on to make some unfortunate comments suggesting that the poor need to own more assets. Oh well. It is ironic that some (including me) attribute the wild disparity squarely on the Fed.

The economy has been financialized to dysfunction, a hallmark of a failing empire according to Kevin Phillips in *American Theocracy*. By flooding the market with capital, central bankers have made it difficult for workers to compete with capital-intensive technology. (I hasten to add that I'm unsure where I stand on this point given that creative destruction is central to growth.) The excess capital, however, also renders our hard-earned savings—our capital—worthless. I *know* where I stand on *this* point. Why pay savers for use of their capital when the Fed hands it out for free? By driving down rates to zero, the Fed is impoverishing savers unwilling to step out on the risk curve. Those of the median class who spent time out on that risk curve have been generationally wounded and, more important, are broke. They lack the capital to close the gap. Despite claims of impending deflation, the spending power of paychecks for the staples—food, energy, health care, and education—has tanked. Alliance Bernstein does a remarkable job of laying out the almost unattainable goal of a stable retirement.[ref 208]

> "I would say [Fed policy] has been in some sense reverse Robin Hood."
>
> ~Kevin Warsh, Stanford University and former Federal Reserve governor

> "Maybe the Fed is delusional about the effects of its policy . . . in widening the gulf between rich and poor in this country."
>
> ~William Cohan

> "Part of the impact of these very, very low interest rates is that we've created this disparity. The wealthy are benefiting from government policy and the non-wealthy aren't. We have a president who says we've got to fight this disparity, and we have a Fed who's encouraging it everyday."
>
> ~Sam Zell, former real estate mogul

History shows that ugly things happen when classes start battling for their share of the pie. A McShitstorm hit the McDonalds annual meeting from clashes of cops and protestors.[ref 209] Ferguson (see below) is not just about a dead black guy. Models show a high correlation of global riots with global food prices.[ref 210] We are there again. Nick Hanauer, a guy who is quite familiar with wealth creation, suggests that the billionaires of the world should be nervous:[ref 211]

> "What everyone wants to believe is that when things reach a tipping point and go from being merely crappy for the masses to dangerous and socially destabilizing, that we're somehow going to know about that shift ahead of time. Any student of history knows that's not the way it happens. Revolutions, like bankruptcies, come gradually, and then suddenly. One day, somebody sets himself on fire, then

> thousands of people are in the streets, and before you know it, the country is burning. And then there's no time for us to get to the airport and jump on our Gulfstream and fly to New Zealand. That's the way it always happens. If inequality keeps rising as it has been, eventually it will happen. We will not be able to predict when, and it will be terrible—for everybody. But especially for us."
>
> ~Nick Hanauer, to his fellow billionaires

Nick sees pitchforks in the future. The Hanauer editorial posted in *Politico* generated upward of 10,000 comments from 10,000 pitchfork wielders. This plotline—a possible Fourth Turning—is just coming into focus.

**Banks and Bankers**

> "The Bank never 'goes broke.' If the Bank runs out of money, the Banker may issue as much more as needed by writing on any ordinary paper."
>
> ~Monopoly board game rule book

Simon Johnson noted that six years after the crisis, the big banks are still only 5% capitalized (20:1 leveraged).[ref 212] Twenty-five European banks failed the stress test, which will force them to recapitalize.[ref 213] The largest banks were mandated by the Dodd–Frank Bill to "put their affairs together" with formal plans to ensure stability: the Federal Reserve and FDIC rejected all of them—a 100% failure rate.[ref 214] JPM has total assets of $2 trillion and a total derivative exposure of $71 trillion.[ref 215] Beware of flappy-winged butterflies. If the Fed taps the brakes, those guys are headed right through the windshield. If we hit a bump in the road, it's out through the moonroof.

> "The tragedy is not that things are broken. The tragedy is that they are not mended again."
>
> ~Alan Paton, *Cry, the Beloved Country*

Let's ignore the awkward question of *why* you recapitalize insolvent banks—you're not supposed to according to Bagehot.[ref 216] *How* do you recapitalize them? Best I can tell, banks clean up their risk (a) through a grinding, multiyear balance sheet rehabilitation (a good ground game), (b) by getting their friends at central banks to engineer highly profitable carry trades, or (c) by simply selling their garbage to taxpayers way above market value. The Fed chose the latter two for US banks. They set up "good" banks and "bad" banks. The good banks hold good assets—heads they win—and the bad banks are like state-run Ebola clinics (tails we lose). The banks are also using more traditional methods; they are stepping away from the mortgage market, leaving it to the shadow banking industry. Get ready for good shadow banks and bad shadow banks.

The banks amassed almost $200 billion in fines,[ref 217] paradoxically without any convictions of major bankers. (Actually, Iceland just hurled a banker in jail.[ref 218] Go Vikings!) There are several nice summaries of JPM's and BofA's illegal activities.[ref 219] The tenacious Matt Taibbi describes how the system was corrupted by backdoor dealings to avoid any jail time in *The Divide* (see *Books*). Taibbi tells us the no-jail policy was indeed a *written policy* by Eric Holder and the Obama DOJ. It is said that as you age you tend toward one of two paths: altruism or narcissism. Holder chose the latter. Barry Ritholtz claims that the fines *are* cleaning up the corporate culture despite the lack of satisfaction.[ref 220] I like Barry but wholly disagree: the bill for this legal and moral lapse has yet to arrive.

> "The behaviour of the financial sector has not changed fundamentally in a number of dimensions since the crisis . . . some prominent firms have even been mired in scandals that violate the most basic ethical norms."
>
> ~Christine Lagarde, managing director of the IMF

Nothing gets through those beer goggles, Columbo. The details of this year's shenanigans warrant some comment. Credit Suisse admitted to helping wealthy US folks evade taxes but claimed that management was unaware they were running a crime syndicate.[ref 221] The Gnomes of Zurich chronically aided and abetted tax evaders. Deutsche Bank and Barclays were in on the scam too.[ref 222] (Don't take me too seriously; I understand arguments for the evasion.) We found that JPM was complicit in the Madoff case, *and the DOJ knew it*.[ref 223] (One should assume the same for Worldcom and Enron.) JPM's Asian CEO was brought up on corruption charges because traders cooked the books to conceal losing trades.[ref 224] Of course, the whistleblower was denied whistleblower status by the regulators because of the DOJ's zero-tolerance whistleblower policy.[ref 225] JPM also helped BNP launder money to sanctioned countries.[ref 226] Preet Bharara, Prosecutor of the Stars and head of his own Rainbow Coalition, went after BNP shareholders for almost $10 billion because you *never* help sanctioned countries. The actual criminals within BNP were left unscathed. JPM paid only $88.3 million to settle similar unlawful dealings with Cuba, Iran, and Sudan.[ref 227] Apparently, you get a two-decimal discount if you are domiciled in the United States. Even Bharara has his tolerance limits; he got majorly pissed at Jamie Dimon for giving himself a 74% raise.[ref 228] I'm guessing it will make Jamie's huge campaign donation to help Preet crowd source his political career harder to explain. I have a suggestion, Preet: Stop fining shareholders and start jailing criminals. Convict somebody—*anybody*. Blythe Masters, after narrowly escaping a prison sentence[ref 229] (not even close), left JPM and accepted a job as *Regulator for a Day* at the CFTC.[ref 230] That's how quickly her detractors processed the absurdity and stopped it.[ref 231] Blythe will be played by Julianne Moore in the sequel to *Catch Me If You Can.*

HSBC overstated its assets by what some might call a rounding error ($92 billion),[ref 232] which forced it to restrict withdrawals by demanding proof that you *need* cash (bank run).[ref 233] Do grocery receipts count? It also recruited the former head of MI5 (British CIA clone) to join its board, which seems oddly consistent with suggestions that HSBC was laundering money to Hezbollah.[ref 234] This also squares nicely with my previous assertion[ref 2] that HSBC is a retread of the profoundly corrupt and now defunct BCCI. After the next bailout—there will be another—Goldman will underwrite the IPO of HSBCCI.

RBS losses since '08 were shown to top £40 billion since '08,[ref 235] an amount oddly comparable to that dumped into it by the taxpayers of one or more countries.[ref 236] Fortunately, RBS managed to scrape together executive bonuses totaling 200% of base pay.[ref 237] CEO Ross McEwan apologized. All was forgiven. . . . at least forgotten.

Citigroup got hit with a $10 billion tax from the DOJ for its role in the crime spree.[ref 238] On a more humorous note, it inadvertently paid out $400 million in fake invoices sent by Banamex (Mexican princes).[ref 239] Trolling for payments using fake invoices to huge corporations is a provocative business model.

> "Regulators are starting to ask: Is there something rotten in bank culture?"
>
> ~*New York Times* news flash

The punitive qualities of all these fines are often muted by their tax deductibility. And, by the way, where does this $200 billion garnered by the Big Shakedown go? State and federal governments have found a number of worthy causes that are also politically expedient[ref 240]—"a wealth redistribution scheme disguised as a lawsuit."[ref 241] Andrew Cuomo threatened to withdraw BNP's license to operate on Wall Street if they didn't up his vig by $1 billion.[ref 242] I can taste vomit in my mouth.

The relief was palpable when MF Global officers and directors were allowed to use insurance money to defend officers and directors rather than give it to creditors.[ref 243] A judge ruled that Goldman's shell game, in which they moved aluminum from warehouse to warehouse, was unintentional.[ref 244] It was just the tip, your honor! It was just the tip! The actor who played McGruff the crime dog got 20 years for pot and weapons charges,[ref 245] the former being legal in some states and the latter a constitutionally protected right. A spoof article describing Holder's departure to JPM was outlandish but so believable that I had to confirm with the source that it was actually satire.[ref 246]

> "When you won, you divided the profits amongst you, and when you lost, you charged it to the [central] bank."
>
> ~Andrew Jackson, former president of the United States

There are a few lawsuits weaving through the courts, and nothing terrifies bankers more than the discovery phase of a trial. Thirteen global banks were sued by Alaska Fund for ISDA fix rigging.[ref 247] I'm not sure how you rig a fix or fix a rig or whatever. The nonprofit *Better Markets* has alleged that the DOJ violated the Constitution (shocking) by acting as the investigator, prosecutor, judge, jury, sentencer, and collector, without any check on its authority or actions.[ref 248] A Freedom of Information Act suit showed that the SEC colluded with banks to ensure that they were prosecuted for only a single credit default obligation (CDO) charge and that the rest were covertly included in the settlement.[ref 249] Barclays' court battles over Libor rigging could produce some interesting discovery about "fantasy rates."[ref 250] The AIG trial seemed sufficiently consequential as a window into this huge heist that it gets its own section.

The charter of the Export-Import Bank (Ex-Im Bank) is up for congressional renewal.[ref 251] Ex-Im bank is, according to Wikipedia, "the official export credit agency of the United States federal government . . . for the purposes of financing and insuring foreign purchases of United States goods for customers unable or unwilling to accept credit risk."[ref 252] It lends money to foreign debtors who cannot get credit through normal channels (credit being so tight and all).[ref 253] Who might they be? Well, sovereigns who buy *lots* of Boeing jets presumably to bomb other countries who also buy *lots* of Boeing jets.[ref 254] Lobbying—quite possibly illegal foreign lobbying—will ensure that the bill is passed. Why not let private banks fund these guys? They've been instigating and then funding foreign wars since antiquity. Congressional opponents risk an airstrike on their next campaign.

Is there any hope that the system will correct itself? In Vietnam, they execute bankers who egregiously screw up by "binding perpetrators to a wooden post, stuffing their mouths with lemons, and calling in a firing squad." That's making lemonade out of lemons. I suspect that the next crisis may see some punishment meted out extralegally in the US. There appears to be some already.

Zero Hedge was the first to pick up on a rash of dead bankers that stopped short of inspiring a Whack-O-Meter based on the bank Implode-O-Meter from 2009.[ref 255] I lost count at about 20 and was shocked to find it is now 36.[ref 256] Unfortunately, the guys most likely to make everybody's short lists are not the ones heading off to the ultimate gated community. It's possible that bankers suffer from the Werther effect—the tendency of suicides to come in waves.[ref 257] It may simply be the Baader–Meinhof phenomenon,[ref 258] or what I've always called the "green van effect"—buy a green van and then notice how many are already on the road. Nassim Taleb would likely tell us we are being fooled by randomness: 36 suicides in the large sample size may be normal . . . but I doubt it. Some of the subplots were curious. One was accidentally shot by two guys on a motorcycle. Another, according to the *Denver Post*, offed himself with eight shots from a pneumatic nail gun.[ref 259] It read like satire given that this Final Exit was likely assisted by the Kevorkian brothers. We know there was *at least* one twisted bastard in the room. One banker went to the light with his whole family, which strikes me as over the top even for a banker. Although JPM's payroll contained several who met untimely deaths, JPM had taken out $680 billion worth of life insurance policies (curtains default swaps) on their employees[ref 260] presumably as a precaution against unfortunate accidents. A Chinese banker both died and fell from a fourth-story window, although the translation is unclear about the order in which the two occurred.[ref 261] Even the head of a Bitcoin exchange cashed out.[ref 262]

> "Perhaps sometimes it is easiest if the weakest links, those whose knowledge can implicate the people all the way at the top, quietly commit suicide in the middle of the night."
>
> ~Zerohedge

**AIG**

Hank Greenberg's lawsuit against the Fed proved the Rosetta Stone of the bailouts. The world was aghast when the Fed bailed out the insurance behemoth to the tune of $187 billion, ostensibly to save AIG but really to save its counterparties (read: Goldman Sachs). The world subsequently blew a collective snot bubble when gazillionaire and former head of AIG, Hank Greenberg, sued the Fed for the bailout.[ref 263] Greenberg's suit asserted that the Fed had no right to confiscate 92% of the company without formal proceedings of any kind. Hmmm. It does sound a little sketchy when put that way.[ref 264] Well, the lawsuit reached the discovery phase this summer, and the media were all over it:

> "The government never sought to couch AIG's lifeline as a way to push money into the hands of Goldman Sachs, Deutsche Bank, Société Générale and the dozens of other banks around the world. . . . The problem is that so many people don't like the answers."
>
> ~Andrew Ross Sorkin, Wall Street darling and putative journalist

Not so fast, Andy. Last year I alluded to David Stockman's assertion that the dominant insurance component of AIG was cordoned off by state insurance statutes—legal tourniquets—from the rotten part of the corpse: the risk of collapse was nil.[ref 2] New York's superintendent of insurance (Dinallo) testified as such in the trial.[ref 265] Tim Geithner, Hank Paulson, Ben Bernanke, and anyone else intimately involved seemed to have truth issues along with *very* bad memories. Matt Stoller wrote some great pieces on the AIG case.[ref 266,267]

> "I would be guessing, but I guess I would guess sometime in '08—but I'm not sure."
>
> ~Timothy Geithner under oath, recalling squat about AIG

That is some seriously evasive mumbling. Bernanke was said to have two moods while on the witness stand with David Boies bearing down on him: "annoyed and really annoyed." Records show he used the pseudonym "Edward Quince" in emails (to Linda Green?) during the crisis,[ref 268] presumably to be secret to all except those with a Jekyll Island decoder ring. Key witness and Fed lawyer Scott Alvarez was clear that Paulson had done some serious fibbing to Congress while pushing the TARP (i.e., AIG bailout) through Congress under false pretenses. Alvarez's use of "I don't know" 36 times and "I don't recall" 17 times *in one day* made for riveting testimony.

> Boies: Would you agree as a general proposition that the market generally considers investment-grade debt securities safer than non-investment-grade debt securities?
>
> Alvarez: I don't know.

Judge Wheeler was smart and easily irritated at Alvarez's bad memory. And unlike Congressional hearings, Boies had all . . . day . . . long.

We heard about the numerous potential suitors wanting to buy up the company as a distressed asset and how Geithner and the gang wanted nothing to do with that: none would pay Goldman back 100 cents on the dollar.

> "...Geithner and company shot AIG in the head, and then let other banks feast on its rotting carcass."
>
> ~Matt Stoller, journalist, channeling Matt Taibbi

Will anything come of this? I don't know. Many prominent journalists wrote scathing indictments of those bringing the suit. Some called it laughable, frivolous, ludicrous, absurd. I, however, am rooting for Kappa Beta Phi alum Hank Greenberg. The Fed should not have commandeered AIG the way it did. It should have let the counterparties eat their mistakes rather than carrion. AIG wasn't the only organization that left the reservation. MF Global is suing Price Waterhouse for the bad accounting that led to its demise.[ref 269] Maybe somebody will yank Corzine from the Hamptons long enough to take the stand. Watch out for guys on motorcycles, Jon.

**The Federal Reserve**

> "I found myself doing extraordinary things that aren't in the textbooks. Then the IMF asked the U.S. to please print money. The whole world is now practicing what they have been saying I should not. I decided that God had been on my side and had come to vindicate me."
>
> ~Gideon Gono, governor of the Reserve Bank of Zimbabwe

> "We have [made] a colossal muddle. . . having blundered in the control of a delicate machine we do not understand."
>
> ~John Maynard Keynes

The Fed's dual mandate as both arsonist and firefighter puts it in the untenable situation of relentlessly fighting blazes it lights. It spent most of 2014 trying to convert one zero-interest-rate policy (ZIRP; Figure 13) via the so-called taper to another (ZIRP-lite), the whole time babbling incoherently to maximize its flexibility to use data of its choosing at times of its choosing. Phrases like "macroprudential" and "central tendency outcomes" are all designed to conceal the real purpose behind their sado-monetary policy.

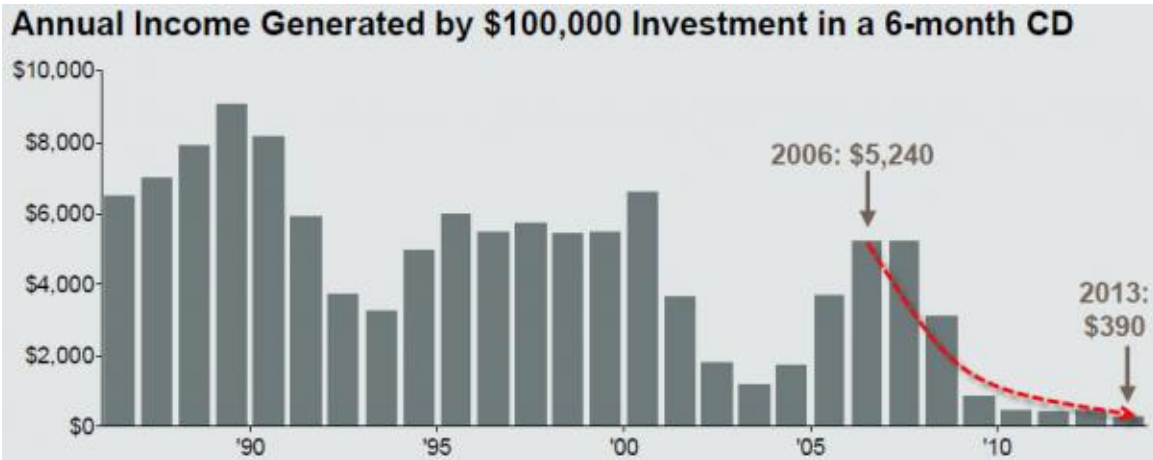



Figure 13. Graphical view of financial repression.

ZIRP is praised by some as a means of providing cheap funding for public and private debt, allowing equity withdrawal from appreciating assets—kind of like an ATM. Hmmm . . . how'd that work for homeowners? The cost of the Fed's No Banker Left Behind financial repression program is estimated by *Bloomberg* at more than $1 trillion to the savers (errata: money hoarders). I know I've been repressed. It takes a balance of $480,000 in my checking account for the interest to pay my $4 monthly account fee.

> "Savers are figuratively on their hands and knees and rooting around in bushes and between sofa seats for loose change on which to sustain themselves."
>
> ~James Grant, editor of *Grant's Interest Rate Observer*

The Fed's primary justification for the risk and high cost of their Iatrogenic ZIRP, however, is to jack up asset markets to all-time highs. Yellen noted that "the channels by which monetary policy works is asset prices . . . I think it is fair to say that our monetary policy has had an effect of boosting asset prices." Richard Fisher concurred: "We juiced the trading and risk markets so extensively that they became somewhat addicted to our accommodation."

> "We make money the old-fashioned way. We print it."
>
> ~Art Rolnick, chief economist for the Minneapolis Fed

Life According to ZIRP seemed pretty good, but $4 trillion is a lotta scratch. A less aggressive approach would have been to monetize it more gradually at, say, $5 million of debt per day, but that would have required starting at the birth of Christ to hit the $4 trillion target. In the midst of the '09 crisis, the Fed needed it fast—Damn the Torpedoes . . . Shock and Awe . . . Surge! Unfortunately, the notion that you cannot print your way to prosperity is gaining traction.

There was a lot of chatter about the Fed scarfing up all the high-quality collateral, causing stress in the repo market.[ref 270] Anyone professing to understand the repo market is smarter or more dishonest than I. What I do know is that if the Fed buys up the good stuff—relatively speaking, of course—that leaves only the riskier crap for the rest of the fixed-income buyers, which seems to be the Fed's motive. There's also endless debate about the size and quality of the Fed's balance sheet. Some say it doesn't matter if their balance sheet looks like a yard sale (worthless shit everywhere). The Fed is even talking about an expanded balance sheet in perpetuity. Benn Steil, author of *Battle of Bretton Woods* and a fellow at the CFR, noted that the Fed *must* have quality assets in case it ever needs to fight inflation.[ref 271] In short, you cannot sop up inflationary liquidity by selling CPDOs and credit default swaps into the market. I am a Benn groupie, but there is no evidence whatsoever that this Fed gives a hoot about inflation.

> "But why do I care about some archaic money-market malarkey? Simple. Without collateral to fund repo, there is no repo; without repo, there is no leveraged positioning in financial markets; without leverage and the constant hypothecation there is nothing to maintain the stock market's exuberance."
>
> ~James Bullard, president of the St. Louis Fed, on the role of the repo markets in blowing bubbles

The media got aroused by the Segarra Sex Tapes,[ref 272] in which a former regulator-turned-whistleblower recorded more than 40 hours of royal screwing she received trying to uncover nefarious activities at Goldman. At some level, they weren't very salacious in the context of the triple-X performance by the banks and regulators over the years, but this one still left a bad taste. The judge's insensitivity to Segarra's claims weren't so shocking given that Mr. Judge (the judge's husband) had previously consulted with Goldman.[ref 273] All of this occurred under the watchful eyes of the Federal Reserve[ref 274] but was promptly forgotten until a ProPublica story shoved it back in the public's eye.[ref 275] Of course, that was several months ago, and nobody cares now.

The recently released 2008 Fed minutes[ref 276] offered another window into the crisis. The Fed clearly understood that the banks were rigging the credit markets . . . but so was the Fed. In 2008 Yellen was "worried about the possibility of a credit crunch if higher job losses begin to make lenders pull back credit." I started writing to folks about it in '02, Dudette, while you guys were making forts out of pillows and blankets.[ref 277] Fisher noted, "None of the 30 CEOs to whom I talked, outside of housing, see the economy trending into negative territory.” Bernanke suggested that “one of the lessons is that we [may] need to take the accommodation back.” We're still waiting for that one. Fisher also expressed stress over the “rising cost of hops and barley . . . I am a beer lover.” (The Fed humor was roundly criticized, but that is neuropsychologically sound behavior under stress.) The most contentious part was probably Kevin Warsh declaring, “We are not clueless.” Some would disagree.

I suspect the Fed orchestrates public debate like a comedy improv group. The result is entertaining and, at times, rather garbled. Let's look at some temporally separate quotes that I've reattached with the ol' “. . .” thingie:

> “More jobs have now been created in the recovery than were lost in the downturn. . . . Five years after the end of the recession, the labor market has yet to fully recover.”
>
> ~Janet Yellen

> “The FED needs to be clear; rates will be low for a long time. . . . We need to let the market work.”
>
> ~Charles Evans, president of the Chicago Fed

> “Inflation expectations are dropping in the U.S., and that is something that a central bank cannot abide. . . . Without leverage and the constant hypothecation there is nothing to maintain the stock market's exuberance. . . . I think you should quit numbering the QEs.”
>
> ~James Bullard, president of the St. Louis Fed

The Fed's second tactic was to feign concern that moral hazard (over-reliance on backstops) had fostered too many animal spirits. Are you kidding me? The *Fed* is admonishing *us* for going out on the risk curve? Now whose fault is *that*? As Mark Gilbert of *Bloomberg* noted, “It's an odd world indeed where the major central banks have all adopted the mantra of 'lower for longer' on interest rates, and are now berating the financial community for listening.” Some compare QE to alcoholism, but that is not really valid: One is a terrible addiction with devastating withdrawal symptoms, the other is merely a drinking problem.

> “There is some evidence of reach for yield behavior.”
>
> ~Janet Yellen, June 18, 2014

I think they dropped Janet on her head when they were competing to see who could throw the Fed chair the furthest. (Hey. Back off! At least I laid off the “flat head” joke. *That* would have been tasteless.)

As Caligula once said, every orgy must end and always with a bang. It seemed to be time. The Fed began to foam the runway for a decrease in QE, even possibly raising Fed funds rates (albeit much later than any rational person could imagine.) The Fed seemed to believe that if it hiked rates with ample warning—if it pulled the trigger *really, really, really slowly*—it wouldn't blow the global economy's head off. The Fed began the Green Mile toward the dreaded taper. As described and critiqued in the section on bonds (see above), not much happened. It began coercing credit-addicted investors into rehab, but the stay at the Betty Ford Clinic was short-lived. In the fall, a 10% drop in equity markets spread fear in the Fed—*OMG!*—prompting Bullard to declare, "We could go on pause . . . and wait until we see how the data shakes out." An ensuing immaculate rally was dubbed the Bullard Rally (Fed cat bounce). Damn, another dud.

Careful Red. The Fed may have kept rates too low for too long (again), causing serious malinvestment (again). Loose credit has kept the losers in the game (again), causing the economy to rot (some more). The Fed suffers acute Hayekian Fatal Conceit—the belief that a committee of a dozen mid-level bureaucrats of moderate intelligence can control something as unimaginably complex as the global economy better than Darwinian selection and the Wisdom of Crowds (free markets). If the Soviets were still around—they went broke trying to control markets—I think they would agree. Let's listen to the voices of just a few more detractors with serious gravitas before moving on:

> "The number of times that the Federal Reserve has hiked interest rates without a negative economic or market impact has been exactly zero."
>
> ~Lance Roberts, STA Wealth Management

> "This time is different . . . because the Federal Reserve's zero-interest rate policy has starved investors of all sources of safe return, forcing them to accept risk at increasingly higher prices and progressively dismal long-term prospective returns."
>
> ~John Hussman

> "There is agreement in the Fed that QE is about the worst thing you can do. . . . These guys are painting themselves into a corner . . . with great, great negative possibilities. . . . The Fed wants to get out of the QE business because it has brought no success and a great deal of criticism."
>
> ~Art Cashin

> "I don't really like the Fed very much . . . I wish the Fed were not manipulating the market the way it is."
>
> ~Jeffrey E. Gundlach, Doubleline Capital

> "A key flaw in US policy is the Fed's linear thinking—believing that the shock therapy of QE could not only save the patient in the depths of crisis but also foster sustained recovery."
>
> ~Stephen Roach, Yale University and former Morgan Stanley chief economist

> "[Yellen] won't raise rates to fight incipient bubbles. For all of our sakes, we really wish she would."
>
> ~Seth Klarman, Baupost Group

> "Where does their confidence come from?"
>
> ~Stan Druckenmiller, legendary hedge fund manager, on central bankers

> "No one has ever seen anything like this . . . if you look at the details of what these central banks are doing, it's all very experimental. . . . There is something fundamentally wrong."
>
> ~William White, former chief economist of the Bank for International Settlements

> "You will see a system primed for a rerun of 2008, perhaps even faster and more intense this time."
>
> ~Paul Singer, Elliot Management

> "We don't understand fully how large-scale asset purchase programs work to ease financial market conditions."
>
> ~Bill Dudley, president of the New York Fed

**Baptists**

> "Sell everything and run for your lives."
>
> ~Albert Edwards, Société Générale

Every year I include collections of comments that seem prescient (Baptists) or off-kilter (Bootleggers)—always in their own voices (quotes) and often suffering well-reasoned paranoia. This year I even have a couple who switched teams or showed bi-curiosity. I begin with the Baptists.

> "We're in a world where there are very few unambiguously cheap assets."

~Russ Koesterich, chief investment strategist at BlackRock

In all likelihood, this manipulation will fail as every attempt at price manipulation since Diocletian's Edict on Maximum Prices in the 3rd century. The only outstanding question is one of timing."

~Louis-Vincent Gave, CIO of Gavekal

"Living in a largely peaceful world with 2% GDP growth has some big advantages that you don't get with 4% growth and many more war deaths."

~Tyler Cowen after discussing the stimulative effect of war

"The stock market does not reflect what's going on in the economy. . . . Holding cash is a better than investing in an over-valued stock market."

~Sam Zell, largest real estate tycoon in the universe

"On almost any metric the US equity market is historically quite expensive. . . . Can we say when it will end? No. Can we say that it will end? Yes. And when it ends and the trend reverses, here is what we can say for sure. Few will be ready. Few will be prepared."

~Seth Klarman, Baupost Group

"Collapses of even advanced civilizations have occurred many times in the past five thousand years, and they were frequently followed by centuries of population and cultural decline and economic regression."

~NASA scientists channeling Joseph Tainter

"Our tinkering artificially short-circuits the fundamental capacity of the system to allocate its limited resources, correct its errors, and find its own balance through the internal communication of information that no forestry manager could ever possibly possess . . . homeostasis ultimately wins through a raging inferno."

~Mark Spitznagel, Founder Universa Investments

"It takes character to sit there with all that cash and do nothing. I didn't get to where I am today by going after mediocre opportunities."

~Charlie T. Munger, Berkshire Hathaway

"You're screwed and even though they say it's in your best interest because zero rates and money printing will help the economy, don't believe them anymore because the strategy has failed."

~Peter Boockvar in an open letter to savers

"This market intervention and manipulation has fostered the greatest-ever speculation in global securities markets, which has motivated only greater central control . . . central bankers believe that they have no choice but to dominate markets—to dominate seemingly everything."

~Doug Noland, Federated Investors

"There's no argument—you have to worry about the excessive printing of money!"

~George Soros, Soros Fund Management

"Today's levels of interest rates and stock prices offer a historically unacceptable level of risk relative to return unless the policy rate is kept low—now and in the future."

~Bill Gross, manger at Janus and founder of Pimco

"What we have never had before, at least in my reading of financial history, is governmentally sponsored bull markets superimposed on a structure of low interest rates."

~James Grant

"Advanced economies with financial markets at risk for runs and fire sales may need to put in place mechanisms to unwind funds should they come under substantial pressure that threatens wider financial stability."

~IMF

"...when it changes it does so quickly, and the impossible becomes the inevitable without ever having been probable."

~Bill Fleckenstein, Fleckenstein Capital

"Paul [Krugman] will continue to be mostly wrong, mostly dishonest about it, incredibly rude, and in a crass class by himself."

~Cliff Asness, founder of AQR Capital

"QE hasn't been a success in the demand side because the [banks] just let it sit. . . . When that starts, all things can happen, and not all of them are good."

~Alan Greenspan (post-baptism)

**Bootleggers**

"I barely made it from the desk to the bed, where I lay curled up in a hallucinatory state for the next eight hours. I was thirsty but couldn't move to get water. Or even turn off the lights. I was panting and paranoid, sure that when the room-service waiter knocked and I didn't answer, he'd call the police and have me arrested for being unable to handle my candy."

~Timothy Geithner, former head of the New York Federal Reserve, after consuming pot during the financial crisis

"I'm going to test your numerology skills by asking you to think about the magic seven. Most of you will know that seven is quite a number in all sorts of themes, religions. If we think about 2014—alright I'm just giving you 2014—you drop the zero, fourteen . . . two times seven!"

~Christine Lagarde, former head of the IMF, unaltered by pot

The bootleggers are an eclectic mix. Some are reasonable souls saying what I think are unreasonable things. Others seem less benign, espousing stunted and vapid ideas. They share the common trait that what they say seems so unmemorable, yet I'm driven to archive it. The bootleggers are, unlike Geithner and Lagarde, more than capable of expressing what is going on in their skulls. Last year I gave Krugman his own section, so I went light this year.

"This is when you're supposed to think about preserving some of your money. I am nervous. I think it's nervous time [5/15/14] . . . all of those things [that made me nervous] alleviated, one by one [6/1/14]."

~David Tepper, May 15, 2014

"When the Austrian brain-worm invades, you start believing things like: (1) Federal Reserve money-printing is a government plot to boost big banks, (2) prices are rising much faster than anyone thinks, (3) real 'inflation' means money-printing, not an increase in prices, (4) printing money can never boost the economy, (5) academic economics is a plot to use mathematical mumbo-jumbo to cover up government giveaways to big banks, etc., etc."

> ~Noah Smith on Austrian economics[ref 278]

> "Noah Smith should really be getting out his papers instead of blogging. I think my career choice would be for him to publish."
>
> ~Paul Krugman

> "But insiders also understand one unbreakable rule: they don't criticize other insiders."
>
> ~Larry Summers, former president of Harvard and former secretary of the Treasury, to Elizabeth Warren

> "Future profitability is better than what we were expecting."
>
> ~Analysts at Citigroup in the Crystal Ball Division

> "The cyclically adjusted P/E ratio suggests S&P 500 is now 30%–45% overvalued compared with the average since 1928 . . . we lift our year-end 2014 S&P 500 price target to 2050 (from 1900) and 12-month target to 2075."
>
> ~David Kostin, Goldman Sachs

**Europe**

> "I say to all those who bet against Greece and against Europe: You lost and Greece won. You lost and Europe won."
>
> ~Jean-Claude Juncker

> "I (and others I talk to) are having an ever-harder time seeing how this ends—or rather, how it ends non-catastrophically."
>
> ~Paul Krugman, *that* Paul Krugman, on Europe

I submitted last year that Cyprus—a clunky beta test for bank "bail-ins"—would "eventually become part of a huge story," and I stand by that. The bail-ins involve shareholders and creditors—creditors including depositors (aka you)—bailing out banks instead of taxpayers (aka you). Not to worry, Yanks. This is a European story. (Just kidding; it's global.) You should read GoldCore's *superior* discussion of the bank bail-in,[ref 279] which is a euphemism for good ole-fashioned bank failure (but without the lines at teller windows). Don't have time to read it? Hooey. You've obviously run out of valid reading materials. The message is clear: choose your bank carefully, diversify by institution, keep balances low, choose carefully the sovereigns in which your banks are domiciled, and quite possibly put your head between your knees. Some are predicting a pan-European bail-in.[ref 280] Germany proposes a wealth tax on southern Europe—Club Med countries.[ref 281] It has been suggested that "the savings of the European Union's 500 million citizens could be used to fund long-term investments to boost the economy and help plug the gap left by banks since the financial crisis."

On the confiscation front this year, the Austrians passed legislation for a bail-in of Hypo Alpe Adria bank that *does not exempt the first 100K euros on deposit*.[ref 282] In short, they whacked the proletariat, prompting one bank analyst to call it "a really stupid idea." It was also a retrospective bail-in involving events before the legislative acts—a claw back—suggesting that expropriations were coming. Spain imposed a "state tax on bank deposits." The accounts were said to be sacred—wrong religion I guess. Catalonia voted overwhelmingly to secede from Spain.[ref 283] I can't imagine why (and all I hear are spanish crickets.) Confiscations took on a new-era flair with a negative interest rate policy. In this world you pay to keep your money in those pillars of stability, the European banks, which were said to be *way* under-capitalized owing to $800 billion[ref 284] to $2 trillion[ref 285] of unwritten-down bad debt. I have mixed emotions on whether slow recapitalization is good or bad because of the wealth transfers associated with flash recapitalizations (see *Banks*).

As though on queue, twenty-five European banks failed the highly handicapped stress tests, prompting immediate questioning of the veracity of the tests.[ref 286] (I suspect they are worthless.) Bulgaria had to seize one of its biggest banks to "avoid" a bankruptcy (whatever that means).[ref 287] Austria's Erste Bank took a 40% write-down because of legislation in Hungary forcing transparency.[ref 288] Portuguese Banco Espirito Santo hit the rocks and was forced to use its own finance arm to lend itself money—liquefying by drinking its own urine.[ref 289] Other attempts to save it included banning short sellers. *Always* blame the short sellers. Of course, the shares eventually found their equilibrium price of zero—Banco Espiece O' Shito. Saxo Bank's Peter Garnry says the "event has hit European financials like a torpedo and has revived investors' darkest nightmares about Europe." During a garbage strike, the fun-loving Portuguese left their garbage at banks.

On the economic front, Europe is a basket case. They talk about austerity like it's some bad thing, like the ice bucket challenge. Austerity is an effect not a cause, and it is transitory only if you get on it early. *Austerity can't wake a cadaver.* Germany looks to be OK because it's vendor financing Club Med to buy German goods. In the 17th century, Europe vendor-financed Spain as Spain ran out of New World gold. That didn't work either. For every 100 residents of Belgium, 28 are working in the private sector.[ref 290] European unemployment is soaring, especially among youth (who are notorious for not being that emotionally resilient.)[ref 291] Household debt in England is 170% of disposable income, while the Great Danes are at 265%.[ref 292] Italy is insolvent to the point of not paying suppliers,[ref 293] and Greece's 2,000-year lost decade continues unabated.[ref 294]

While the Euromess was playing out, equities soared and the bond yields plumbed century lows (see The Bond Caldera) owing to the subversion of price discovery by Mario "Whatever It Takes" Draghi and European central bankers. Meanwhile, those charged with pumping asset prices to maintain world peace continued to chastise investors for chasing risk:

> "Asset values [are] at their highest ever . . . at the other end, we see a real economy where recovery is not really strong . . . that discrepancy between the two is quite worrying."
>
> ~Christine Lagarde, head of the IMF

When credit spreads began to widen and price discovery loomed, the unholy trinity—the so-called Troika (EC, IMF, and ECB)—began passing pickles. The G20 announced it wanted $2 trillion in increased economic activity (and a pony). But as one *Bloomberg* reporter noted by email, "There's a real sense of revenge running thru Europe's apparatchiks presently. Not helpful." The Hessians were stirring:

> "The ECB has reached the limit in helping the Euro Area."
>
> ~Wolfgang Schäuble, German minister of finance

Enter Mario Draghi with guns blazing, locking and loading a weaponized printing press, to create hundred of billions of euros designed to blow up on impact. In a sneak attack, Draghi dragged Europe into the global currency wars.[ref 295] For those hoping to invest in the Europe's future at fair prices, Mario's coin in the fuse box was a donkey punch.

> "The fundamental problems are not solved and everybody knows it . . . the euro crisis is not over."
>
> ~Maximilian Zimmerer, CIO of Allianz SE

In other news, Europe is also hanging on the precipice of global energy shortages if Russia decides to play the energy card—and looking at something even worse if Russia pulls the military card. Venice voted to secede from Italy by refusing to send taxes to Rome.[ref 296] Spanish planes illegally challenged a British airliner in a fight over . . . fish.[ref 297] The UK is close to full energy dependence as North Sea oil falters.[ref 298] It seems likely to me that energy dependence eventually leads to debt crises. Scotland voted *not* to secede from Great Britain (or England or whatever). But as Stalin wryly noted, "People who cast the votes decide nothing. The people who count the votes decide everything." A few hanging chads maybe? And if all that weren't enough, somebody leaked embarrassing nude photos of a young Angela Merkel.[ref 299]

In a world of perfectly efficient stock, bond, and housing markets, investors seem to be yelling, "Hey Guys: it's a dud!"

> "It isn't our job to go out hunting for rigging of markets."

> ~Governor Mark Carney, Bank of England

> "People usually get angry when they are afraid, and Mario looked furious yesterday."
>
> ~Mark Gilbert, *Bloomberg*, email

**Asia**

> "Asia is in a holding pattern with troubles in the queue waiting to make headlines."
>
> ~David B. Collum, 2013 Year in Review

Once I figured out which countries are actually parts of Asia, I was feeling prophetic. We've got pro-democracy riots in Hong Kong and martial law in Thailand. The action, however, was in China, Japan, Russia, and the Middle East. We have some seriously existential risk brewing in these regions, so let's reverse-crack our knuckles and get into it before somebody releases the launch codes.

**China**

> China is starting to crash
> Building ghost-cities was rash
> So now they must pay
> For debt gone astray
> The assets they built are now trash
>
> ~@TheLimerickKing

As economic tensions mount, so do political tensions. The big issue looks to be a battle royale brewing between the US and China. China warned the US against a "Crimea-style land grab," although I'm not sure what that would entail.[ref 300] Our DOJ has accused China of cyberspying.[ref 301] Shocking.

The real clashes will be economic and monetary. The early battles are fought using bilateral trade agreements. China is setting up direct deals that explicitly exclude the US dollar. They have signed bilateral trade agreements with the UK;[ref 301] currency swaps with Switzerland,[ref 303] Singapore,[ref 304] and Canada;[ref 305] direct trade of energy for yen with Gazprom and Qatar;[ref 306] and yuan-clearing banks in Luxembourg and Paris.[ref 307] All of these arrangements chip away at dollar hegemony, although I wouldn't call them causal; a dollar demise finds its roots in US policy. Triffin's dilemma says that a reserve currency fails owing to a ballooning trade deficit.

One could be forgiven thinking that the Chinese variant of state capitalism somehow makes the country less sensitive to credit busts. However, the housing market is said to have 50 million unoccupied houses and 70 million unoccupied apartments.[ref 308] Maybe building unoccupied “ghost cities” equivalent to 50 Manhattans between 2008 and 2012 is OK.[ref 309]

Alas, China *is* vulnerable to the vicissitudes of the credit markets just like everybody else. The bust has begun, and with debt estimated at 250% of GDP, this landing will be tough to stick.[ref 310] The banks are beginning to falter. Famed short seller and China bear Jim Chanos notes that “the Chinese banking system is built on quicksand.” Lack of deposit insurance adds a special flare to bank runs. Gazillions of yuan in loans have turned out to be backed by relentlessly rehypothecated physical collateral (industrial metals).[ref 311] These guys really *are* fast learners. Loan guarantors appear to be totally insolvent.[ref 312] Companies are finding that payments from their counterparties are taking longer to arrive,[ref 313] prompting one businessman to note: “If you don't pay me and I pay others, aren't I just a sucker? I'm not that stupid.” Counterparty risk is a bitch, ain't it?

Of course, these nouveau capitalists with Western PhDs have discovered the miraculous cures available from bailouts. China Development Bank lent 2 billion yuan to coal company Shanxi Liansheng.[ref 314] The People's Bank of China cut rates to 5.6% on November 21.[ref 315] China displays a notable difference in its response to bank crises, however, compared with that of the Western world: they hang bankers.[ref 316] There is a second difference: their one-child policy has left them with millions of single—presumably sex-crazed—young men that can be recruited by General Tsao for when the Szechuan hits the fan. This plot is just beginning to thicken.

> “While we believe Chinese banks’ credit woes will unfold gradually, the disturbing thing is that the end is nowhere in sight.”
>
> ~Liao Qiang, Beijing-based director at Standard & Poor’s.

**Japan**

> “I've never really wanted to go to Japan, simply because I don't like eating fish, and I know that's very popular out there in Africa.”
>
> ~Britney Spears

Fukushima continues to smolder. Be wary of the news reports, however. Becquerels are tiny units so the radiation leakage is easy to state hyperbolically, and reports of cancer clusters are notoriously dubious, as outlined in *The Drunkard's Walk* (see Books). Meanwhile, Japan's economy is about to go critical, as summarized masterfully by Grant Williams.[ref 317] In short, their sovereign debt has soared, the personal savings rate is plumbing post-war lows, the current account balance has tanked in the face of unstimulating Abenomics (monetary camel toe), and the population will continue to age for decades.

The basic premise of Abenomics—the seemingly cockeyed Keynesian construct that has failed for 25 years now (always because it was not enough)—seems to be based on the idea that one can bid up the price of assets and declare enhanced wealth regardless of per-capita output. It didn't work during the pre-bust '80s. It didn't work during the subsequent 25 years. It seems unlikely to work now. Almost 50% of Japan's tax revenues go to paying debt service at interest rates that are at record lows. Rising rates would crush them; monetization will continue. Kuroda's latest announced QE was shocking in its magnitude, timing, and dubious support (ministers voted 5 to 4). The market went on a 'roid rage, but that won't last. The yen was crushed so much and so fast that it spooked the BOJ into jawboning the decay rate.

> "There are no limits to our policy tools . . . to completely overcome the chronic disease of deflation, you need to take all your medicine. Half-baked medical treatment will only worsen the symptoms."
>
> ~Haruhiko Kuroda, governor of the BOJ on QE

A little odd that Kuroda thinks that is how you "take all your medicine." Japan's Bugger Thy Neighbor monetary policy—a currency war—includes seriously dubious interventions into the equity market. The BOJ is now going to pile monetized Japanese equities on top of Japanese pensions loaded with horrifically dubious Japanese debt. The serpent is eating its tail. Abe is working on a plan to give everybody gift cards to spur spending (no joke).[ref 318]

The justification for Japan's monetary policy is that Japan is said to be in the throes of a deflation despite a steadily growing money supply[ref 319] and rising prices of goods and services.[ref 320] Japan is in a depression—a very long one. Depressions are simply serial recessions, the latest starting in October. The pessimists say that it is already game over; demographics and foolhardy malinvestment are so deep-seated that a catharsis is in the future. Kyle Bass is still predicting a bloodbath, a "transformative" moment.[ref 321]

> "Kuroda knows when to go *all* in. The BOJ is basically declaring that Japan will need to fix its long-term problems by 2018, or risk becoming a failed nation."
>
> Takuji Okubo, chief economist at Japan Macro Advisors

Speculation that the Japanese have developed a process to convert sewage into food[ref 322] sounded "transformative", but the suspicion that sewage has been depleted of nutrients is correct; the technology is Internet legend. What a shame. I was really looking forward to a Sewage Burger™ and some Sewshi™.

**ISIS**

> "If a jayvee team puts on Lakers uniforms that doesn't make them Kobe Bryant."
>
> ~Barack Obama on ISIS

> "They are as sophisticated and well-funded as any group that we have seen. They're beyond just a terrorist group . . . an imminent threat to every interest we have."
>
> ~Robert Gates, former Director of Central Intelligence, on ISIS

> "ISIS is not Islamic."
>
> ~Barack Obama imitating George W. Bush

This plotline goes disturbingly far back. Eleventh- and 12th-century crusaders went looking for salvation and found little. Twentieth-century imperialists went looking for oil and hit the jackpot. But what an incredible mess. *Frontline* offered an excellent overview;[ref 323] the explanation in Figure 14 is even better.

## Clear as mud

ARE you confused by what is going on in the Middle East? Let me explain.

We support the Iraqi government in the fight against Islamic State. We don't like IS, but IS is supported by Saudi Arabia, whom we do like.

We don't like President Assad in Syria. We support the fight against him, but not IS, which is also fighting against him.

We don't like Iran, but Iran supports the Iraqi government against IS. So, some of our friends support our enemies and some of our enemies are our friends, and some of our enemies are fighting against our other enemies, whom we want to lose, but we don't want our enemies who are fighting our enemies to win.

If the people we want to defeat are defeated, they might be replaced by people we like even less. And all this was started by us invading a country to drive out terrorists who weren't actually there until we went in to drive them out. Do you understand now?

*AUBREY BAILEY, Fleet, Hants.*

Figure 14. Concise explanation of US Middle East policy.

"That child should be playing with other kids, not holding a severed head."

~Senator John Kerry, master of the obvious

There were some extraordinary moments during this Clash of Civilizations (Miracle on ISIS). In a Middle East version of a wilding, the reconstituted Iraqi army ripped through serious desert real estate, replacing their Black and Decker drills with guns, ammo, troops, Apache helicopters, stinger missiles, 88 pounds of uranium, and $400 million in beer money. (Goldman was planning an IPO for some serious petrodollar-denominated fees; they even had the Nasdaq symbol picked out.) As night follows day, genitals got mutilated, and heads began to roll. Stratfor's George Friedman warned us in *America's Secret War* not to underestimate any of the players in these global chess matches. Gladwell further reminds us in *David and Goliath* (see Books) that the obvious underdogs often win these fights.

> "Once you got to Iraq and took it over, took down Saddam Hussein's government, then what are you going to put in its place? That's a very volatile part of the world, and if you take down the central government of Iraq, you could very easily end up seeing pieces of Iraq fly off: part of it, the Syrians would like to have to the west, part of it—eastern Iraq—the Iranians would like to claim; they fought over it for eight years. In the north you've got the Kurds, and if the Kurds spin loose and join with the Kurds in Turkey, then you threaten the territorial integrity of Turkey."
>
> ~Dick Cheney, 1994

It's always fun until someone loses an eye! That happened when ISIS began slobbering over the Saudi oil fields and, presumably, the whole Saudi regime.[ref 324] The United States had to start building a case to attack. The humanitarian mission is always a strong opening play: do it for the children (the ones who are left). Soon an enemy laptop was discovered with plans by ISIS to use bio-weapons. Sure. I believe that. Must have been found by the informant named Q-Ball. (Oops. Wrong war.) We began discovering old—very old—chemical weapons dumps posing risks akin to those at Love Canal and started pushing that angle again. *Fox News* kept claiming that ISIS was amassing troops on the Mexican border, apparently in alliance with drug lords, illegal aliens, democratic voters, and Ebola carriers, for the final battle in *Lord of the Rings*. Shockingly, the Republicans wanted to build a big fence. The Turks got caught on tape planning a false-flag attack, but they were still smarting from the Erdogan tapes revealing the previous botched variant.[ref 325,326]

The US administration faced a quandary. Bombing ISIS strongholds would inadvertently give Syria an advantage. The solution? Bomb them both just to be fair.[ref 327] Who thinks up this stuff? The administration finally settled on the general strategy of arming everybody, hoping that everybody would get killed. God or some other deity can sort them out. Estimates of 10:1 civilian-to-militant kill ratios[ref 328] have been reported for US drone attacks. The United States put together a massive coalition that included the Bloods and Crips, Klingons, and Girl Scout Troop 539 and began Operation Iraq Liberation (OIL).

Meanwhile, ISIS seems to be positioning to reestablish Syria—the old Syria with seriously expanded borders. Was this all a black swan event? Listen to this interview of Wesley Clark from 2007 in which he says half a dozen countries would be taken out over the next five years.[ref 329] One Nobel Prize and seven bombed Muslim countries later, one begins to wonder.[ref 330]

> "Note to Self: Next time, no Middle East."
>
> ~@TheTweetofGod

**Russia**

> "After the Russian army invaded the nation of Georgia, Senator Obama's reaction was one of indecision and moral equivalence, the kind of response that would only encourage Russia's Putin to invade Ukraine next."
>
> ~Sarah Palin, 2008

> "I can see Alaska from my front porch."
>
> ~Vladimir Putin

OK. I made that last one up, but it's official: Cold War 2.0 has started. Putin is a popular guy in Russia. He's sporting an 83% approval rating (almost as high as Obama's.) The Russians are tired of being famous for dash-cam videos on YouTube. The year started innocuously enough with the $50 billion Sochi Olympic fails live-tweeted by unhappy reporters:

> "My hotel has no water. If restored, the front desk says, 'do not use on your face because it contains something very dangerous.'"

There was a lot of cackling when the Olympic logo failed. Putin's agitation watching the Olympics, wrongly attributed to a punk performance by his commie-dog athletes, was because he was anxious for the real games to begin.

The brawl started almost immediately after the closing ceremonies. We had already toppled Ukraine's democratically elected leadership to install a more Western-pliable variant.[ref 331] The mistake we made has been described in an incisive article by John Mearsheimer in *Foreign Affairs*:[ref 332] we *wanted* the Ukraine and Crimea to satisfy our whims. Russia *had* to have the Ukraine to satisfy its needs.

> "Obama, however, has only tenuous control over the policymakers in his administration—who, sadly, lack much sense of history, know little of war, and substitute anti-Russian invective for a policy."

> ~Letter to Angela Merkel from US intelligence wonks

Who could have guessed what would happen next? While we blathered on about the whereabouts of Malaysia Airlines Flight 370, Russian-speaking troops dressed as Maytag repairmen filled the power vacuum in Crimea. The missing flight had more oddities than a state fair midway.[ref 333,334,335] Nobody wants to admit that a missing flight makes for a much more prolonged distraction than a downed flight. *That* would make you a conspiracy theorist.

Obama and Putin immediately started trading tits for tats. Obama teed off with Harvardian rhetoric. Putin responded using air jerks with full eyeball rolls. Intimidating a guy who rides horses, sharks, and grizzlies shirtless was not easy. We began pressuring Mother Russia with sanctions.

> “Negotiating with Obama is like playing chess with a pigeon. The pigeon knocks over all the pieces, shits on the board, and then struts around like it won the game.”
>
> ~Vladimir Putin

> “I sometimes get the feeling that somewhere across that huge puddle, in America, people sit in a lab and conduct experiments, as if with rats, without actually understanding the consequences of what they are doing.”
>
> ~Vladimir Putin

The European allies cooperated reluctantly. Germany was remarkably cozy with Russia for a while, although the Putin–Merkel romance went frigid when we threatened to strap on some sanctions against Deutsche Bank.[ref 336] We grabbed up another Cypriot bank supposedly containing Russian oligarch money,[ref 337] forgetting that we stole every euro from them last year. The Polish foreign minister expressed angst over the fact that “we gave the Americans a blow job” and then called us “losers. Complete losers.”[ref 338] Apparently, he took one on the chin at some point. (Sorry. Gratuitous sex joke.) It got a little embarrassing and diplomatically tricky when a top US State Department diplomat told the US ambassador to Ukraine that we should “Fuck the EU,” which led to a “sorry—my bad” apology.[ref 339] The Ukraine banned exports of military hardware to Russia as Russia was importing Ukraine.

> “What we've done over the past 10 years is to create a new method of projecting U.S. power . . . a growing arsenal of financial weaponry aimed at hitting foreign adversaries.”
>
> ~David Cohen, undersecretary for terrorism and financial intelligence, US Treasury

Soon the Europeans agreed to ban the buying of Russian bonds.[ref 340] Quite the sacrifice. Standard and Poor's downgraded Russian debt by a notch.[ref 341] The Moscow stock exchange seized up.[ref 342] Visa and MasterCard suspended service.[ref 343] One Russian oligarch noted that the new Chinese credit card was attractive because "at least the Americans can't reach it." JPM, spotting opportunity, blocked money transfers of Russian money back to Russia without authorization by the administration.[ref 344] Really? They kept somebody's money? This is my shocked face: :<O. (In *All the Presidents Bankers*, Nomi Prins describes how the banks prolonged Carter's Iran hostage crisis by doing the same thing.) The international court at The Hague fined Russia for a decade-old whompin' of oil giant Yukos,[ref 345] prompting a somewhat eerie response:

> "There is a war coming in Europe. Do you really think this matters?"
>
> ~Putin confidant on The Hague verdict

Unsurprisingly, Russian energy giants were handled with kid gloves by the Europeans in this Game of Thrones. Winter was coming. China and Russia began setting up a pile of bilateral trade deals including a 30-year, $400 billion energy agreement.[ref 346] I use dollars only for the reader's convenience 'cause it certainly ain't gonna be denominated in dollars. All the while we scratch our heads over the interests of Joe Biden's son in Crimean gas companies.[ref 347]

> "Any fourth-grade history student knows socialism has failed in every country, at every time in history."
>
> ~Vladimir Putin

The US grabbed control of the global energy market to put the serious hurt on Putin. The Saudis started talking about how they were comfortable with oil below $80 per barrel.[ref 348] Some claimed it was to push the marginal frackers in the US out of the game,[ref 349] but it's not obvious why they would bother since prices were rising at the time. More likely, the Saudis did it as part of a US-engineered collapse of the oil price.[ref 350] We got to inflict discomfort on Putin, and in return, the Saudis got military support against ISIS fighters heading for their oil fields.[ref 351] Our primal urge to fight Putin, however, nuked the US energy industry, the junk bond market, and possibly a few sovereign states (see Energy). The consequences of this will be clearer next December.

Cold War 2.0 was looking a little dicey militarily too. Another Malaysia Airlines flight bought the collective farm. (That pun's just plane wrong!) The Swedes undertook a massive search for a rogue Russian sub (Red October).[ref 352] Russian fighters have been buzzing the coast of California.[ref 353] One is rumored to have passed over a US destroyer a dozen times and, if you believe it, jammed the ship's radar and detection systems.[ref 354] Russians, we are told, hacked the White House and a bunch of megabanks.[ref 355,356] Russia's bilateral trade arrangements all appear targeted toward dethroning the dollar. The so-called petrodollar is at risk. I wouldn't underestimate the probability and consequences of an eventual dollar demise. For now, however, it is the ruble and the rubes who have leveraged long positions in it running laps around the drain.

The idea of pressuring Russia with the vicissitudes in the marketplace strikes me as silly. I've watched the dash-cams; those guys are tough. Russians survived cannibalism in the Siege of Leningrad (1941–44). Our idea of suffering is camping out overnight at Target for iPhones, which are for some reason perceived to be in life-altering short supply. The investor lobe in my brain tells me to get ready for a geopolitically induced buying opportunity in the energy sector. My dark-horse economic winner of the 21st century—admittedly a long time—is Russia. Oddly enough, all this may be Kabuki theater (a dud). Catch this exchange between Obama and Medvedev, who were unaware of the directional microphone.[ref 357]

> Obama: This is my last election. After my election I have more flexibility.
>
> Medvedev: I understand. I will transmit this information to Vladimir.

**Ebola**

> "This is not an African disease. This is a virus that is a threat to all humanity."
>
> ~Gayle Smith, senior director at the National Security Council

> "Ebola was unreal and a gimmick aimed at carrying out cannibalistic rituals."
>
> ~Former Nigerian nurse

Years ago I read *The Hot Zone* and *Demon in the Freezer*, but it was *The Great Influenza*, the story of the 1918 flu pandemic costing 100 million lives, that piqued my interest in Ebola. It turns out Ebola and the flu have a common feature: the body's immune response in the form of a "cytokine storm" poses great risk.[ref 361] With numbers still in the hundreds but evidence that Ebola had entered African cities, I did a back-of-the-envelope calculation of a three-week doubling time. Bingo! Ten thousand cases later, it proved spot on. Ebola was undeniably existential risk of an unknown probability. Vice President Biden thought we should send troops to fight Ebola until he found out it wasn't a country. It wreaked havoc on West Africa, where annual per-capita healthcare expenses measure in double digits. Gunmen looting Ebola clinics, families defying government orders and simply dragging bodies to the street, and the generalized breakdown of the healthcare systems in affected countries painted a horrific picture of human suffering.[ref 362]

Ebola was considered a distant problem to many sitting cloistered in the protective warmth of Obamacare. It finally caught the collective attention, however, when it found its way to Dallas and then spread just a little bit.[ref 363] I can't say I panicked, but I understood the concern. Speculation that it might be transmitted sexually—*of course it is*—gave way to the realization that Ebola lasts 90 days in semen.[ref 364] This prompted authorities to urge users to stop turning their condoms inside out and reusing them. How about just throttling some poultry for a couple of months? The fear that bushmeat was infectious sent shudders through the high command of Taco Bell. Obama, although slow to react overtly to avoid panic, appointed a large campaign donor, lawyer Ron Klain, to be his Ebola czar,[ref 365] prompting Bill Bennett to note, “I was a czar. This ain't no czar.” For a country professing allegiance to democracy, we sure appoint a lot of Czars. In any case, Czar Ron went into exhile the day he was appointed.

The more sanguine began comparing the total number of Ebola cases to Derek Jeter's strikeouts and Oscar Pistorius's ex-girl friends. Countless declarations that “more people have died from [fill in the blank] than from Ebola” made me yearn for a swift demise. The glib intellectuals were crystal clear: only peasants worry about such silly things as a 60% fatality rate on an exponentially growing pool of patients. An excellent lecture by Berkeley physics professor Albert Bartlett on our collective ignorance about exponential functions[ref 366] might prove enlightening for the editorial staff of the *New Yorker*:

> “Study: Fear of Ebola Highest Among People Who Did Not Pay Attention During Math and Science Classes”
>
> ~*New Yorker* headline

It has been a dud so far (except in West Africa). There were some odd moments like this 1971 Holiday Inn ad featuring Ebola.[ref 367] A chap named Clipboard Idiot—armed with only a clipboard to protect himself from an infected patient—underscored the risks of inadequate response.[ref 368] As the disease may be heading into quiescence, however, I remind the reader that glib dismissals of existential risk will, on very rare occasions, prove fatal.

> “Bring out your dead.”
>
> ~Monty Python

**Government**

> "It is terrible to contemplate how few politicians are hanged."
>
> ~Gilbert Keith Chesterton (1874–1936), British writer

> "Our own government did more harm to the liberties of the American people than bin Laden did."
>
> ~Ron Paul

Anarcho-libertarians decry the need for *any* government, ignoring the fact that *all* civilizations since the dawn of civilization have voted yes. Government appears to be a necessary evil, but evil it certainly is sometimes. This is a place where "bipartisan" means some larger-than-usual deception is being carried out. This is an organization that is still compensating Irene Triplett, a very elderly lady, for her father's military service . . . in the Civil War.[ref 369] Let's take a quick peek at why confidence in Congress has dropped to an astounding 7% (astounding that it's not 0%).

The capital of crony capitalism, of course, is Washington DC. The geniuses in Congress pushed the Access to Affordable Mortgages Act —a new wave of liar loans—because 4% interest rates are simply too high.[ref 370] The Postal Service is losing billions and maxed out its available credit lines (but otherwise runs pretty well in my opinion), prompting Congress to vote a stay of execution on *all* post offices.[ref 371] Congress pondered a new form of state-sponsored bank—the United States Employee Ownership Bank Act—funded by the taxpayers to loan money to American workers so that they can . . . wait for it . . . "form collectives and buy the companies they work for." Hmmm...collectives. GovTrack says the chance of enactment is 0%.[ref 372] Phew!

The EPA recruits earthy employees who defecate in its hallways.[ref 373] A presidential wannabe (Rick Perry) was indicted by a grand jury on two felony counts of blackmail.[ref 374] A lobbyist got sent to prison for bribing Harry Reid, who was not indicted, fired, or quite possibly even asked to give the money back.[ref 375] Tom Delay's conviction for money laundering, the only conviction of substance of an elected official in recent years, was reversed.[ref 376] Phew again! In the category of criminal stupidity, Nancy Pelosi asserted that "every dollar of unemployment insurance benefits increases America's GDP by as much as $1.90 and could lead to 200,000 new jobs." It would be safe to say that she ain't gonna be splittin' any atoms.

Away from the hallowed halls of Congress and the Senate, the Veterans Administration had some 'splainin' to do. It seemed to have falsified data to hide healthcare delays for veterans.[ref 377] We've been sending our kids to foreign wars and completely failing to patch them up when they return home shot to pieces. An estimated 64,000 vets signed into the VA system during the last decade and never got a first appointment.[ref 378] One who had a leg amputated owing to incompetence suggested wryly, “I feel the VA owes me a leg.” Indeed it does. Obama took the heat on the scandal, but this was a bipartisan effort spanning many years.

> “All we have of freedom, all we use or know—this our fathers bought for us long and long ago.”
>
> ~Rudyard Kipling, “The Old Issue,” 1899

The DOJ spent millions to cover up a clerical error that caused an innocent, wheelchair-bound citizen to be handcuffed as a terrorist.[ref 379] Hundreds of millions worth of cargo planes to reinforce the Afghan Air Force were turned to $32K worth of scrap instead.[ref 380] Eric Holder could have used a few of 'em: he took 27 personal trips on DOJ planes.[ref 381] Elon Musk lost a multi-billion dollar contract when he didn't give a public official a job at SpaceX.[ref 382] A sergeant was convicted of accepting $250K in bribes from local Afghan contractors,[ref 383] which makes you wonder where those crazy Afghans get their money. Maybe a brisk rug market? David Brat knocked off Eric Canter (figuratively). The big losers are all those folks who've been bribing Canter who now get zip. They will have to continue paying to ensure promises of bribes after leaving office will be taken at face value. The Lannisters always pay their debts. Leaving no issue untainted, the feds cancelled the Washington Redskins trademark.[ref 384] It's not the office’s job to do this, but it does prompt some thoughts on a new mascot: the Washington Lobbyists, Criminals, Lightweights, Elites, Kickbacks (which has a nice football ring to it), or, taking a cue from the Miami Heat, the Washington Douche.

The once-reputable SEC continues to underwhelm. Former SEC lawyer James Kidney's farewell letter suggested that his superiors were more focused on getting high-paying jobs after their government service than on bringing difficult cases.[ref 385] Ya think? The agency’s penalties, Kidney said, have become “at most a tollbooth on the bankster turnpike” and that the SEC had become “a cancer.” A Zero Hedge poster called it “Kidney Failure.”

The SEC awarded a whistleblower of a big Wall Street bank $14K hush money for his info; they fined the bank without naming it.[ref 386] Luis Aguilar noted, “I am concerned that the commission is entering into a practice of accepting settlements without appropriately charging fraud and imposing suspensions.” This statement was prompted by a punishment meted out for a banking fraud case that entailed giving back half a million in bonuses.[ref 387] As part of the Dodd–Frank financial overhaul, the Financial Stability Oversight Council was created and was soon in a turf war with the SEC over who is in charge of ignoring financial crimes.[ref 388] Jesse Eisinger noted that Mary Jo “MoJo” White was “supposed to turn around the SEC. She hasn’t.”[ref 389] MoJo's honor was defended by Yves Smith, who pointed out that “Mary Jo White is no doubt doing her job. It’s simply, as with Obama, not the job the public was led to think she’d do.”[ref 390] Maybe the next president—possibly a wizard at trading cattle futures—will bring honor back to the SEC.

Not to be outdone by the SEC, the commissioner of the Chicago Futures Trading Commission, vigilant defender of Wall Street, Scott O'Malia, left the commission to head the International Swaps and Derivatives Association, an enormous lobbying group for the banks.[ref 391] This so-called soft corruption—corruption that is real and really hard to convict—continues unabated.

The hilarious stuff occurred at the state level, and the great state of New Jersey, home of buried bodies and Hoboken, took a leadership role. The big one was Bridgegate, wherein a need for political retribution prompted one of Governor Chris Christie's aides to note, "Time for some traffic problems in Fort Lee."[ref 392] Bridges were artificially jammed up for a few days. Commuters did not get the joke, especially the guy who died in the traffic jam. As expected for any presidential hopeful, Christie just couldn't catch a break. The big guy got caught cutting pension contributions by 60% to close a budget gap[ref 393] while allocating $200 million to a hedge fund that, by chance, had given him a $250K campaign donation.[ref 394] All told, the state's taxpayers lost an estimated $3.8 billion to the governor's largesse[ref 395] (presumably including some portfolio losses). The Wall Street boys and girls garnered $938 million in fees alone.[ref 396] Alas, the statute of limitations on such vente larceny is 10 minutes.

A number of other state civil servants won participation awards. Former New Orleans Mayor Ray Nagin of Katrina fame was sentenced to a decade in prison (or until a last-minute pardon from Obama) for bribery.[ref 397] Rahm Emanuel got $100K from Comcast and then, shockingly, supported its merger with Time-Warner.[ref 398] Governor Andrew Cuomo announced he would disband the Moreland Commission formed to investigate corruption in Albany.[ref 399] Nixon rolled in his grave. By this standard, he was not a criminal.

General Motors (aka Government Motors) was the victim—yes *victim*—of government bailouts. For 50 years they made payroll but no profits, operating at a massive loss when you account for unfunded pension liabilities. What is such a company worth to investors? Salvage rights? Had they been allowed to restructure properly, the pieces would have been auctioned off free of liabilities at prices that would allow industrialists to begin making quality cars at a profit.

But wait a minute there: GM is now profitable, right? The bailouts came at enormous cost (estimated $17–20 billion).[ref 400] Claims that the government made its money back are fibs when you track *all* costs, including bailouts of Ally Bank (former GMAC).[ref 401] This year reminded us about what happens in the absence of real restructuring. GM recalled more vehicles by May 2014 than it had sold in five years.[ref 402] Preventable fatalities (negligent homicides) were traced to bad management. GM is a rotting corpse that should have been feasted on like AIG.

> "Remember when if nobody bought the cars, we let the company fail?"
>
> ~@PoliticalLaughs

**The Clintons**

> "We can't afford to have that money go to the private sector. The money has to go to the federal government because the federal government will spend that money better than the private sector will spend it."
>
> ~Hillary Clinton

That is some industrial-strength stupidity. To bipartisan horror, 2016 could be a dynastic showdown between the Clintons and Bushes. Although Jeb is lying low, the Clintons reminded us why dynasties are dubious. Leaving aside the Benghazi Defense League, the Clinton's image problems began with an interview in which Hillary declared they were "dead broke" upon departing the White House and later suggested they are "not truly well-off." A net worth exceeding $50 million and an estimated $100 million in speaking fees for Bill buys a lot of cigars and pizzas. Hillary accepted a $225,000 speaking engagement at UNLV to discuss the horrors of rising tuition, prompting students to send her a letter asking for the money back.[ref 403] I'm sure the money went to what Hillary believes is a good cause.

> "Don't let anybody tell you it's corporations and businesses that create jobs."
>
> ~Hillary Clinton

Showing that the Acorn doesn't fall far from the tree, Chelsea Clinton gets $75,000 per speech[ref 404] and worked part time at NBC for a $600,000 annual salary.[ref 405] Calling an audible that would impress Eli Manning, she said, "I was curious if I could care about money on some fundamental level, and I couldn't." That's OK. She married a hedge fund manager who *does* care about money and bought her a $10 million condo.[ref 406] When Bill was asked about the fairness of the discussions of Clinton wealth, he ironically noted that "someone is always trying to change the subject." Laws prohibiting flows from foreign sources as part of the Buy American campaign seem to be loose guidelines. Warren Buffett said, "Hillary is going to win. I will bet money on it." I bet you have, Warren.

> "Under no circumstance is there ever a justification for the pre-emptive deployment of Hillary Clinton anywhere by any country."
>
> *~The Onion*

**Barack Obama**

> "You just don't in the 21st century behave . . .by invading another country on [a] completely trumped-up pretext."
>
> ~John Kerry, secretary of state

> "Don't do stupid shit."
>
> ~Barack Obama at a particularly introspective moment

By way of disclosure, I am a right-hemisphere libertarian, but I was OK with Obama for a few years. Yes, he was a liberal democrat with all the apparent trappings (golf pun: #drink), but I snapped a few years back after realizing that even the stronger ideas of liberalism—I believe there are some—are lost on this guy. It is not his liberalism that drives me nuts but his views of the Constitution, civil liberties, and democracy. His presidency was to be defined by how he would resolve a massive financial crisis and corporate white-collar crime wave. He defined it alright, which will be the proximate cause of the next ones. But this section is about the other stuff.

I begin with the obvious. Obama would not be the first president to hit the links a few too many times for quality optics. Those keeping score (#drink) claim that Shankopotomous has had several hundred tee times during his presidency (of the US, not the USGA).[ref 407] The total greens fees (including all the protective accoutrements) for a two-month period are estimated at $3 million.[ref 408] Playing a couple of rounds on courses in Arizona that consume a million gallons of water a year is OK, but doing so on a speaking tour related to the ills of the drought and water shortage?[ref 408] A round immediately after the Foley beheading prompted his aides to note that "the golf game did not reflect the depth of his grief over Mr. Foley."[ref 409] Of course (#drink), these were working foursomes that included the likes of a Bain Capital lobbyist,[ref 410] prompting Jay Carney to note that "Mr. Obama is still dedicated to fighting corruption and influence peddling within the administration." *Still*? Odd choice of words.

> "I do think at a certain point you've made enough money."
>
> ~Barack Obama

> "I do think at a certain point you've played enough golf."
>
> ~A tweeter

Let's listen to some of his detractors. We'll skip "The Cheeto" (Boehner) and the blond-haired Republican hatchet women at *Fox News* and ponder more interesting perspectives, including some from former supporters:

"A more shameless, reprehensible display of buck-passing it would be hard to find from a sitting president."

~Piers Morgan

"I found that you had become exactly like the George Bush that I used to vitriolically hate."

~Obama girl having second thoughts (and a killer bod')

"President Obama's neo-Cold War is not about ideology or respect for borders. It is about money and global power."

~Nomi Prins, author of *All the Presidents Bankers*

"The Obama White House responds to news cycles and how to get past them, not with actual solutions to real problems."

~Ron Fournier, former Washington bureau chief at the Associated Press

"Obama protected Wall Street . . . not people who lost their jobs. . . . He picked his economic team, and when the going got tough, his economic team picked Wall Street."

~Elizabeth Warren

Obamacare, known by few as the Affordable Care Act, continues to elicit chuckles. The website cost $1.7 billion dollars.[ref 411] Come again? Really? Give me a couple of teenagers from the Bronx High School of Science, some Adderal, and a couple ounces of pot—these kids don't work for free—and I could've had it up and running in a month. Rumors that there was some browbeating to get 'er done conflict with reports that the contract went to one of Michelle's college BFFs.[ref 412]

I'll have civil liberties for $500, Alex. The administration's plan to track all license plates to "catch illegal aliens" was canceled owing to the Gestapo optics.[ref 413] The irony is that Obama deemed it a lot easier to give illegals amnesty via executive order (head slap).[ref 414] Embedding government workers in media organizations to make sure reporters were doing their jobs also seems a little dubious.[ref 415] A tepid response from the media confirmed that they were not.

Then we get Grubergate. As the story goes, a guy named Rich Weinstein, who literally lives on a couch in his parents' basement—he's a benefactor of the recovery—discovered a video of Jonathan Gruber,[ref 416] an MIT economist prominent in the Obamacare debate:

> "This bill was written in a tortured way to make sure CBO did not score the mandate as taxes. . . . Lack of transparency is a huge political advantage. And basically, call it the stupidity of the American voter or whatever, but basically that was really, really critical for the thing to pass."
>
> ~Jonathan "The Grubster" Gruber, MIT

Our intrepid sofa surfer tweeted the video to his two-dozen followers, and the power of social media took it from there: Grubergate had begun. Here is an entertaining two-minute synopsis.[ref 417] With ample funding from the Obama administration,[ref 418] The Grubster concluded in copious scholarly works that Obamacare would be a wondrous thing. Soon The Grubster was demoted by Obama from "trusted advisor" to an advisor "who never worked on our staff," which became "who?" for short. Of course, embarrassment and hashtags are the highest form of punishment meted out to wayward politicians these days. The Grubster, however, may be held to a different standard. The failure to disclose conflicts of interest of such magnitudes is a serious ethics violation where I come from;[ref 418] it could get fugly. Not to worry: I hear there are distinguished-scholar openings at CUNY for polarizing and misguided macroeconomists.

> "It's terrifying that a guy in his mom's basement is finding his stuff, and nobody else is."
>
> ~Rich Weinstein, couch potato and Grubergate whistle-blower

Obama introduced—via a vote-bypassing executive order—a new IRA called My IRA or MyRA for short (by one letter).[ref 419] Some feared it would morph into a TriRa (Trimester IRA) owing to mandated investing in government savings bonds currently returning zippo on an inflation-adjusted basis. One supporter warned that investors "shouldn't expect big returns" (at least not with a positive sign.) I can't find evidence (not even a Wikipedia page) that this lead trial balloon launched. The algos loved it, however. The previously delisted microcap Myriad Entertainment & Resorts (symbol: MYRA) was ramped 900% by news-trolling algos.[ref 420]

Other assorted items caught the attention of Obama's detractors. The White House tried to juke the job stats for "factoryless goods" but had to kill the idea.[ref 421] The Potus's retrieval of Bowe Bergdahl meant as a whole new diversionary strategy—a *positive* diversion—failed to elicit euphoria when evidence surfaced that Bowe had actually defected to the other team.[ref 422] By the way, everybody knows the preferred currency in hostage negotiations is arms, not prisoners. Obama wore a beige suit, triggering the dumbest goddamned chatter—Taupegate. You'd think he'd ridden around in the Choomwagon dressed like Sly Stone. The Secret Service had its troubles,[ref 423] and somehow the Fox Blonds pushed that one back on the administration.

> "The United States is and will remain the one indispensable nation in the world."
>
> ~Barack Obama

> "This is what a successful presidency looks like."
>
> ~Paul Krugman, distinguished scholar, CUNY

**IRS Scandal Part Deux**

> "[Holder] has put politics above the enforcement of the law on numerous occasions and unfortunately that is likely to occur again."
>
> ~American Center for Law and Justice on IRS-gate

> Internal Revenue Service Information Technologies: "The IRS does not routinely save chat communications."
>
> Lois Lerner: "Perfect."

This scandal, big in 2013, was buried in a shallow grave but wouldn't die. Recall that Lois Lerner, director of the Exempt Organizations Unit of the IRS, made more than 150 trips to the White House (probably more than Biden) to discuss what appeared to be Stasi tactics against tea party Republicans.[ref 424] Elijah Cummins apparently helped compile the preferred-audit list.[ref 425] The investigation continued in 2014, causing an epidemic of computer crashes and hard drive failures.[ref 426] "Hard drive crashes continue as we speak," admitted John Koskinen a House Oversight and Government Reform subcommittee. Of course, the claim was that *none* was backed up and that they would be too onerous to search anyway.[ref 427] Oops: Sonasoft had them all backed up, but their contract may have included a "lose the backup" clause.[ref 428] The federal law mandating the reporting of lost data got downgraded to a guideline. Holder promised a special prosecutor.[ref 429] Right. That will happen contemporaneously with the release of Tarek Aziz's autobiography. During congressional investigations Representative Darrell Issa grilled IRS Commissioner John Koskinen:[ref 430]

> "For too long, the IRS has promised to produce requested—and later subpoenaed—documents, only to respond later with excuses and inaction. Despite your empty promises and broken commitments to cooperation, the IRS still insists on flouting Constitutional congressional oversight."
>
> ~Darrell Issa

For those with short memories, Koskinen was charged with overseeing the government's Y2K remediation,[ref 431] so broken computers are his forte. A released email from Lerner conveyed an acute interest in whether emails could be searched and noted with irony that “we need to be cautious about what we say in emails.” The district judge demanded that somebody from the IRS show up and, under oath, start 'splainin' the lost emails.[ref 432] That spokesperson admitted that Lerner's Blackberry was “wiped clean of any sensitive or proprietary information and removed as scrap for disposal in June 2012,” well after the investigation began.[ref 433] Nothing *ever* comes of these scandals.

**Bundy Ranch and Ferguson**

> “If someone comes out of a liquor store with a weapon and fifty dollars in cash, I don’t care if a drone kills him or a policeman kills him.”
>
> ~Senator Rand Paul

The highlights of socially important events for me were the battles of the masses versus the State exemplified by conflicts on the Bundy Ranch in Nevada and in Ferguson, Missouri. In both cases, ambiguities exist as to what happened and who is in the wrong. That really isn't the point. These two events dovetail with wealth inequality and police militarization, which are setting off some spectacular fireworks as my fingers hit the keys and will continue to do so in the future. I begin with the Bundy Ranch.

As the story goes, some years ago a rancher named Cliven Bundy decided that paying the feds to graze his cattle on federal lands was not of interest to him (the paying part, that is). There may have also been some large-money interests pining for them thar hills.[ref 434] The battle festered and finally spewed forth when the feds decided to confiscate and execute Cliven's herd. Oh boy. The feds gathered the troops, and the Bundys rounded up a gang that eventually included militias from across the country[ref 435] hankerin' for a fight. For days the two sides squared off in full eyeball-to-eyeball contact. The standoff was reminiscent of the Army versus WWI vets showdown that led to hundreds of deaths.[ref 436] The feds blinked and went home. (Hats off to them.) Powerful imagery shows the ranchers saddled up against the militarized police (Figure 15).

Figure 15. Range war at Bundy Ranch

Pan the camera to Ferguson, Missouri—a ‘hood of St. Louis. Michael Brown, a black male of considerable girth reputedly robbed a store and was gunned down. Some evidence says he was gunned down from behind; leaked autopsy reports indicate he had lurched for the gun as the police claim. That is not the point either. A garden-variety example of an inner-city kid getting whacked by the cops that wouldn't normally make it above the fold in the *Ferguson Gazette* went full Rodney King. The riots stayed out of the green zones (affluent neighborhoods) but lingered for a very long time, as nicely summarized here.[ref 437] Why the fuss? There are as many as 40 shootings in Chicago every night. (For the hopelessly clueless or politically too correct, the glibness in that last sentence is a literary device.)

Ferguson *may* suffer from a new-era form of policing that has been growing for decades and is described in lurid detail by Matt Taibbi in *The Divide* (see Books). Police tactics are mutating from Norman Rockwellian to Orwellian during the last few decades. As Taibbi tells it, potential criminals are identified using methods that the affluent cannot fathom—you are in the wrong place at the wrong time and look suspicious. Large paddy wagons drop dozens of putative criminals at the precinct. The serious criminals are sorted from the mistakes. The latter—schoolteachers picked up on hooker charges, for example—plead down their cases to misdemeanors to avoid the hassle, pay their fines, and return to their daily struggles both poorer and angrier. Those unable to make bail, even those charged with nonviolent offenses, spend days, weeks, and even months in the hoosegow awaiting trial. A kid charged with stealing a backpack was held for three years at Rikers Island *before his trial*, only to have his case dismissed.

Why doesn't the cost of incarceration break the cycle? Oh, that's the money shot: federal subsidies make these all-expense-paid stays profitable for the state. And if that weren't enough, a Clinton-era law mandates that a conviction on *any* drug offense—zero tolerance—results in eviction from federally sponsored housing. (I generally find "zero tolerance" to be too, well, intolerant.) Even those with militant opposition to subsidized federal housing can probably imagine the sense of violation inherent in a fabricated drug offense leaving you broke and homeless. When some random kid named Michael Brown gets shot, you might be inspired to hit the streets with 'tude too and more than just a can of spray paint.

These bouts of civil unrest and disobedience may be the stories of the decade. I try to drive this idea to the hoop in the conclusion, but let's press on.

> "Police Department Reduces Costs by Using Same Evidence For Every Investigation"
>
> ~*The Onion* headline

**Police Militarization**

> "We get up early to beat the crowds."
>
> ~Catch phrase on T-shirts of police charged with crowd control

So where is all this leading? With the advent of smartphones, most debates over paranormal phenomena and almond-eyed aliens have been put to rest, but evidence of police brutality is epidemic. I could link to dozens of YouTube videos but choose only three—a homeless woman getting the crapped kicked out of her,[ref 438] a horrifying montage,[ref 439] and a homeless, mentally ill guy getting gunned down.[ref 440] The last one looks like murder in the first to me. Police tased an 8-year-old girl.[ref 441] A military-style SWAT—Special Weapons and Tactics—raid cracked down on a farmer trafficking in unpasteurized milk.[ref 442] SWAT raided a guy known for trolling the mayor on Twitter.[ref 443] The executive producer of Tosh.0 intervened in a crime as a Good Samaritan and got shot while the crooks got cuffed.[ref 444] Police emptied 600 rounds into a vehicle, killing both bank robbers and a hostage,[ref 445] apparently accepting limited collateral damage. I could go on and on and on . . . but that would be overkill.

The Fourth Amendment delineates castle doctrine—people's houses are their castles. Posse comitatus, passed in 1878 and updated in 1981,[ref 446] provides safeguards against military intervention in civilian affairs. No problemo.

Authorities end run laws prohibiting the use of the military as police by converting local police forces into military units with flexible guidelines brought to you by Homeland Security. We are witnessing what Radley Balko's must-read—*must-read*—book refers to as *The Rise of the Warrior Cop* (see Books). SWAT teams, originally invented by Los Angeles police chief Daryl Gates—yes, *that* Daryl Gates—to intervene in the most severe situations, are now routine participants in drug busts and arrests for a host of *nonviolent* crimes. In conjunction with no-knock warrants, military raids on private residences have increased 10-fold since the late '90s. Federal grants are placing billions of dollars worth of heavy artillery—machine guns, armored vehicles, flack jackets, grenade launchers—in the most unlikely places. The Department of Agriculture ordered submachine guns with 30-round magazines to fight the War on Fruit.[ref 447] Brevard County received eight Apache helicopters.[ref 448] The University of Maryland obtained an armored vehicle fitted with a grenade launcher.[ref 449] "It's never been deployed against our students, nor could I ever envision it being deployed against our students," the police chief says. Campus police prefer pepper spray. Representative Hank Johnson wryly noted that "apparently, college kids are getting too rowdy." A town in Iowa with 7,000 people and a San Diego *school district* both got armored vehicles.[ref 450]

> "If I had a rocket launcher some son-of-a-bitch would pay."
>
> ~Bruce Cockburn

The scary part is that these SWAT guys can be really nuts. In a large police force, you can select carefully (if you wish). Small-town SWAT teams are picked like teams in sandlot Wiffle ball—you get some real losers. Here is a video of one of the A-teamers:[ref 451] do you want this guy bashing in doors in your hometown? Even worse, the feds offered grants for police to hire veterans. Sounds logical given that vets need jobs, but some of these guys are pretty comfortable splattering skulls like cantaloupes. Sprinkle in a little PTSD, and you've got a problem.

So why are Mayberry and Hooterville arming themselves to the teeth with military gear? The simple explanation is that the arms dealers are pocketing billions. A more insidious possibility is that municipal police forces are preparing for tough times ahead. I spoke with a prominent defense lawyer in Ithaca—*Ithaca, New York!*—who says "we've already lost the fight: they own us."

**Civil Forfeiture**

> "Normal people do not carry that kind of cash."
>
> ~Police officer justifying a civil forfeiture

Of course, the police have plenty of nonviolent tactics. Enter the notion of civil forfeiture. It takes on a multitude of forms, all sharing the common theme of authorities confiscating money and goods when they suspect nefarious activity.[ref]

[452] You read that right: *suspect.* Laws changed markedly after 9/11 under the Patriot Act. Police can now legally confiscate money before trial and . . . wait for it . . . keep it as a slush fund.[ref 453] Years ago, California got into a pickle when authorities got caught confiscating the contents of dormant safe deposit boxes that weren't dormant and whose contents were sold off without an inventory.[ref 454] We now have traffic violations leading to the confiscation of cash because its quantities are deemed suspiciously large. A federal judge called authorities' attempt to conceal $13 million from a gambler as "abhorrent."[ref 453]

If you think these are urban legends, think again. *Forbes* published a story about 639 civil forfeitures.[ref 455] In only 20% of the cases was there *any* evidence of possibly illegal activity. The majority, however, went unchallenged because of the court costs and sense of futility. In instances in which there was no evidence of crime committed, the authorities rarely offered to give the money back. A must-see John Oliver rant does a fine job of defining the problem.[ref 456] I suspect that those failing to achieve satisfaction in the courts might have some pretty dark thoughts. This video of a prosecutor gleefully describing how to maximize the take from civil forfeiture generates them in me.[ref 457] I better stop here.

**Civil Liberties**

> "That is exactly why Edward Snowden felt compelled to whistle-blow. He understood what was at stake: Everything."
>
> ~Mike Krieger (@libertyblitz)

> "Why don't we use the American Constitution? It was written by really smart guys, it has worked for over 200 years, and they're not using it anymore."
>
> ~Newspaper in Kiev

Every year it feels like the battle for our civil liberties is slipping away from us one liberty at a time. *Frontline* brought us the must-see documentary *The United States of Secrets.*[ref 458] Gizmodo provided a nice listicle titled, *65 Things We Know about NSA Surveillance We Didn't Know a Year Ago*.[ref 459] The fact that such stinging indictments are still available is an encouraging sign. Another Snowden interview, by contrast, was widely broadcast . . . except in the US.[ref 460]

> "When our engineers work tirelessly to improve security, we imagine we're protecting you against criminals, not our own government."
>
> ~Mark Zuckerberg, CEO and founder of Facebook

The ultimate struggle of good versus evil appears to be the battle for the tech world, in which the power of social media and remarkable global dissemination of information have squared off against authorities showing increasingly fascist tendencies, often under the guise of protecting democracy and freedom. We were warned by Scott McNealy of Sun Microsystems years ago[ref 461] that the tech world has been commandeered by those interested in peering into every aspect of our private lives. Jim Farley, the vice president of Ford said, "We know everyone who breaks the law, [and] we know when you're doing it.[ref 462] Catchy, but I would go back to "Ford—Quality is job one." The NSA intercepts online laptop purchases to install spyware.[ref 463] Tech companies are forced to cooperate. Failure to do so leads to secret trials by secret courts accompanied by secret fines.[ref 464] Attempts to add encryption files to smartphones are being opposed by the FBI[ref 465] because they would "hurt law enforcement efforts to crack homicide and child-exploitation cases." Yes, Joe Friday: Do it for the children.

> "Concentrated power is not rendered harmless by the good intentions of those who create it."
>
> ~Milton Friedman

Payments to tech companies are suggested to be salve for the wounds of cooperation. RSA, a subsidiary of EMC, was paid $10 million to provide backdoor entry for the NSA.[ref 466] RSA touted its "high-security data storage." Apparently it's not the highest security. Yahoo's fight against the government's pressure to cooperate led to a modest fine but also forced cooperation.[ref 467] Whistle-blower William Binney says the fight to keep 80% of fiber-optic cable traffic routing through the United States is motivated by the authorities' desire to have full access to the content.[ref 468] US authorities bitch about Chinese-made routers as insecure, but Glenn Greenwald tells us that US-made routers are *very* NSA friendly.[ref 469] Germany booted Verizon in fear of its relationship with the NSA.[ref 470] (This is probably pandering by politicians.) Civil rights battler Michael Krieger takes on the Cyber Information Sharing Act's attempt to commandeer all our digital privacy.[ref 471] (Michael has been tirelessly bringing these stories into the light of day.) A scandal involving a cooperative effort among the NSA, Facebook, and one of my colleagues at Cornell (Professor Jeffrey Hancock) involved a study in which Facebook altered individuals' newsfeeds to see how social media influenced their responses to key issues.[ref 472,473] I'm told that Hancock is a sincere guy, but the motives of the NSA are in doubt. Attempts by the FCC to regulate the Internet are exceedingly dangerous.[ref 474]

*Congress does not support the NSA; it is held captive by it and terrified of its power.* Russell Tice, yet another NSA whistle-blower, notes the massive blackmail of politicians.[ref 475] Of course, some members of Congress are sociopaths, willing to endorse any bad idea (for a price, of course). There is plenty of evidence, however, that the battle of good versus evil has been lost in the halls of power as well. Jon Stewart hammered Diane Feinstein for her hypocrisy on NSA after the agency stole documents from her computer.[ref 476] Given that she was one of the most ardent supporters of the NSA, ya gotta wonder what the agency had on her to win her support. Feinstein declared that "our oversight role will prevail" in the context of the CIA spying on the Senate Intelligence Committee[ref 477] (as well as all of Congress).[ref 478] Do we look that stupid? It has already failed. On a bright note, the CIA apologized and promised to never do it again. Obama announced no plans to curtail the agency's aggressive global surveillance, prompting General Hayden, head of the NSA, to declare this a "vote of confidence" for the NSA and its staff.[ref 479] Maybe Hayden is confident that their spying program on Obama beginning in 2004[ref 480] had collected enough dirt? This is J. Edgar Hoover on 'roids.

> "This is kind of death of the republic kind of stuff."
>
> ~Rachel Maddow on CIA spying on politicians

And don't think we will be saved by the FBI; it has switched from crime-fighting to national security: facial recognition software, and license plate tracking. They also go after rogue journalists to make the world a safer place.[ref 481] I feel *so* safe.

> "It is not the responsibility of the government or the legal system to protect a citizen from himself."
>
> ~Justice Casey Percell

The security agencies have their own revolving door. I'm sure Stratfor buys a few, but it has become an arm of the government, so it's really just a reassignment. As noted above, an MI5 agent went to HSBC, but I would make the same argument on that one too. Some would say Edward Snowden took the revolving door to work for the Russians, but that would be a reach. Michael Krieger told us that ex-NSA head Keith Alexander sold his insights to Wall Street's largest lobbying group, the Securities Industry and Financial Markets Association, for $600K per month via his new venture IronNet Cybersecurity Inc.[ref 482] NSA's chief technical officer, Patrick Dowd, is allowed to work up to 20 hours a week at IronNet Cybersecurity Inc.[ref 482] Why leave the NSA when you're more valuable moonlighting while on the NSA payroll? Theresa Shea is the director of the NSA's Signals Intelligence, which refers to all electronic eavesdropping and interception.[ref 483] Her husband works in the private sector of the profitable Signals Intelligence industry at Telic Networks and DRS Signal Solutions Inc.[ref 484] The NSA turned down a Freedom of Information Act request to probe Shea's finances,[ref 485] referencing a "1959 law that allows it to keep almost everything secret." Shea resigned to pursue outside interests.

How about the mid-level stuff? A federal whistle-blower got his email account hacked and four years worth of damning evidence deleted.[ref 486] I hear Sonasoft backs that stuff up. A CIA operative used correct channels to divulge key info and got fired.[ref 487] The War against Whistle-Blowers is a major plank of this administration. The NSA sends out malware to infect computers, take screen shots, and record audios.[ref 488] A program called DROPOUTJEEP allows the NSA to pull essentially anything from your smartphone.[ref 489] NSA says that it is simply too big—too much of a burden—to comply with court orders involving saving and providing evidence.[ref 490]

And in the category of “thinking you're safe ‘cause you have nothing to hide” I bring you just a couple of anecdotes. A woman was charged with a crime for leaving her 11-year-old waiting in a car.[ref 491] Another woman got five days in jail for not following a town ordinance on lawn mowing.[ref 492] In the Justina Pelletier case, the state took custody of a 15-year-old over disagreement with a hospital's treatment.[ref 493] A Pennsylvania woman had her house auctioned by authorities because of a $6 overdue tax bill.[ref 494] One woman received massive fines and a jail sentence over school truancy.[ref 495] We can't tolerate kids missing such a bushmeat-laden curriculum that includes Common Core mathematics[ref 496] mandated by state education interventionists. Cecily McMillan of Occupy Wall Street was convicted of assaulting a cop—elbowed him in a scuffle—and faces seven years in prison.[ref 497] Probably won't get that, but . . .

This is not just a War on Women. One poor gent got it right up the butt—a triple-enema-to-find-drugs without a reach-around.[ref 498] I sure hope they fed him a snack while they were up there. No drugs were found, and he got a court-ordered $1.6 million settlement and an endorsement deal as pitchman for the colonoscopy lobby. A hacker from Anonymous is looking at 440 years in prison.[ref 499] Barrett Brown is facing more than 100 years in prison for trying to organize a Wiki-affiliated database to archive hacked materials.[ref 500] He’s spent more than a year in prison, and some consider him a political prisoner. Here's the perfect defense: hack into a bank’s computers, put yourself on their payroll, and declare immunity from all prosecutions.

We now have drones with 4,000 rounds of pepper spray pellets.[ref 501] Fortunately, it would *never* be used on US citizens. After a three-year fight, a court released a “drone memo” outlining arguments for killing US citizens.[ref 502] I guess I'll take the pepper spray. The feds did a smash and grab on computer data in an investigation, grabbed too much, held onto it despite a court order to get rid of it, and then passed it to the IRS.[ref 503] Nice. Orlando used eminent domain to take land from a church to build a soccer stadium,[ref 504] attesting to the rising popularity of soccer. Rumors of such land grabs date back to the ‘60's when Walt Disney was positioning to change Orlando from a small town into a gigantic cesspool. General Mills claims that the simple act of purchasing a product may subject you to non-class-action status and restriction to arbitration.[ref 505] Caveat emptor.

> “Now—as the nature of the threat we face evolves to include the possibility of individual radicalization via the Internet—it is critical that we return our focus to potential extremists here at home.”
>
> ~Eric Holder

Let me close this discussion of civil liberties by taking on a very charged topic. Universities are under increased pressure to deal with sexual misconduct ranging from inappropriate behavior to full-blown rape. Keeping students safe by keeping predators off campus is admirable, but university staffs currently seem ill-equipped, especially for cases that should be handled in criminal courts.

(Those who say university police should play a central role have never seen university police in action.) Women *must* feel safe on campus, but this safety should not come with no attention to the rights—quite possibly the Constitutionally granted rights—of men. An active debate about when no means no has now mutated into a debate about when yes means no. Oberlin administrators have declared, for example, that intoxicated women—not obliterated, merely intoxicated—are no longer considered capable of saying yes.[ref 506] By proxy, Oberlin men are being converted by policy to sexual predators. California's legislature enacted the "affirmative consent" law,[ref 507] in which silence is not implicit consent. The students must use "affirmative, conscious, and voluntary agreement" that is "ongoing throughout a sexual activity." [Insert patently obvious joke here if you dare.]

I don't have the wisdom of Solomon to know where the happy medium is, but this ain't it. Federal probes of college sexual harassment practices are soaring.[ref 508] Lawsuits by the accused are piling up. The system is under stress. An open letter from 28 Harvard Law School faculty is a worthy read.[ref 509,510]

> "We find the new sexual harassment policy inconsistent with many of the most basic principles we teach."
>
> ~28 Harvard Law School professors

We should be careful not to push the system to the point where parents sending their boys off to college have to remind them to videotape their sex to defend against an accusation. As I am on the final edits, the *Rolling Stone* scandal involving false accusations of gang rape at the University of Virginia is just hitting the press.[ref 511] Oh dear. On second thought, skip college and take Father Guido Sarducci's *Five Minute University.*[ref 512]

**Conclusion**

> "I'm tired of being outraged"
>
> ~Ben Hunt, Salient Partners

I envision German Jews sitting around the dinner table in the 1930's discussing risk. Among those who had the opportunity to mitigate the risk—certainly many did not—some chose to do so, and others bet that the threat would pass. It didn't, and they paid dearly. Next time you hear a glib intellectual dismissing risk-averse peasants—intellectual children—because the risk is low or because the worst case scenario failed to materialize, I would understand if you planted one right in their chops and muttered "you smug bastard."

There is no "risk" of a 10% stock market correction because there are no consequences except to the blokes who live (and die) by leverage. Risk is not about what happens but what *could* happen and what the consequences *could* be. Russian Roulette is statistically a 6:1 winner . . . until you lose.

In 2002 I wrote a close friend at Goldman (Rick Sherlund) of the risk of a banking collapse.[ref 277] I described the risk of subprime mortgages and possible collapse of Fannie Mae, Freddie Mac, GE Capital, and the entire banking system. Yes. It *did* collapse, only to be resurrected by central bankers willing to do things to sheep (us) that would make Romans blush. Some, central bankers included, say nobody saw it coming, which is obviously wrong because I was merely parotting what I had read. *Thousands saw it coming, and billions didn't.* Some would say I was dead wrong in my warning to Rick because my call was too early. Bullshit. It was a great call given the consequences of the collapse.

This year has been all about risk—existential risk. Some of it seemed to dissipate and some lingers. Ebola was mathematically *very* serious—Russian Roulette—but western civilization has dodged that bullet for now. Market valuations remain risky—regression to the mean could easily provide a 50% haircut and more if we observe regression *through* the mean. This has not come to pass, but the risk is *very* real. Those who seek risk in markets will eventually find it.

I avoided ranting too much about unfunded liabilities and pension stresses this year not because the risks have dissipated—they have not—but because nothing has happened *yet*. I seriously doubt, however, that the pension problem will be a dud. Whether we witness a massive corrective action—a come-to-Zeus moment—or rot spread over decades does not dissuade me from believing we will experience an historic purging of debt and unfullfillable commitments.

Cold War 2.0 came out of nowhere and has the potential of, at a minimum, rotting our national balance sheet and, in the worst case scenario, turning into a conflagration of a higher order. Oh surely *that* would never happen again, right? The House of Commons met 14 days before World War I broke out. There is no mention in the minutes discussing the risk of armed conflict. The history books are littered with destructive human folly—men (and now women) attempting to be important—and such folly will continue unabated. Folks like Niall Ferguson who study empires in decline think the US Empire is waning. This essay by Soviet dissident Dmitry Orlov is a particularly harsh view.[ref 488] A common theme in these discourses is that declining empires tend to respond violently at home and abroad.

We can see it already. Loss of civil liberties, militarization of the police force, and civil forfeiture are *profound* concerns to me. I get a little over-protective of what's mine. Can you recall an instance in which such a path was taken and then society backed out uneventfully? I can't. Richard Clarke, Bush's National Coordinator for Security, closed his tell-all book *Against All Enemies* by suggesting that the enemy is within.

Ferguson, Missouri is emblematic of both hope and risk. I see the Ferguson unrest as an outgrowth of Occupy Wall Street. The folks on the street are getting madder at the current imbalances. Their lot in life is getting worse for reasons that are too complex for me to fully grasp. What they have figured out, however, is that *they have power.* "Hands up" and "Can't breath" have become rallying cries for pissed off folks and not just inner city dwellers. With the advent of social media and cell phones, a group of people who have never met can assemble spontaneously to shut down the system. Society is developing unprecedented collective neural pathways to express discontent. Don't underestimate the intensity and frequency of such events going forward, because there are a lot of people with a lot of things to be pissed at.

Of course, despite the authorities' best efforts to keep everything orderly, we know how this global Game of Tetris ends:

> "Players lose a typical game of *Tetris* when they can no longer keep up with the increasing speed, and the Tetriminos stack up to the top of the playing field. This is commonly referred to as *topping out*."
>
> ~Wikipedia on Tetris

**Books**

> "I cannot remember the books I've read any more than the meals I have eaten; even so, they have made me."
>
> ~Ralph Waldo Emerson

I rehypothecated that quote from last year's review, but it brilliantly captures my frustration of not remembering in detail what I've read but sensing enrichment nonetheless. I summarize all the books I've read during the year. Owing to limited bandwidth, I try to choose carefully. Audiobooks help: I am an audiophile. Books sent by authors are appreciated but engender a sense of obligation and potential conflict. I have flagged those books. The topics wander but are always reputedly nonfiction: why waste my time on fiction?

*Flashboys* by Michael Lewis

Michael set out to write a horror story about Sergey Aleynikov (highlighted in previous reviews[ref 2]), but the book morphed into a tell-all exposé on high frequency traders. I am a huge Michael Lewis fan; I read everything he writes for his prose, humor, and capacity to find the story within the story. The narrative may have some minor flaws, but *Flashboys* is classic Lewis prose and very entertaining.

*The Great Degeneration: How Institutions Decay and Economies Die* by Niall Ferguson

This is a short, easy read in which Ferguson articulates his views on why and how the West is in decline. He documents the political and economic decay foreshadowing the demise of Western civilization and submits that it could cascade rather quickly. He won't swing opponents (not even former economist Krugman), but it provides for some great confirmation bias.

*Human Action* by Ludwig von Mises

This is a very scholarly work by the legendary godfather of Austrian economics. Those who profess to be Austrian economists view this as one of the bibles. In my humble opinion, this book is not for the faint of heart. I found it to be a bitch to get through. Although ignorance is at play, the prose is also so bloated (early 20th-century Austrian) as to make it difficult for all but the most dedicated reader. The man needed a copy editor. With that said, the ideas are seminal.

*The Death of Money: The Coming Collapse of the International Monetary System* by James Rickards

Rickards is a publishing dynamo. His books are global, his resume impeccable. In this follow-up to *Currency Wars*, Jim describes the battle of central bankers against the forces of the free market, the essence of the inflation–deflation battle. This is an entertaining view of global currencies that I found reminiscent of George Friedman's *America's Secret War*. Those who have read Hayek's *Fatal Conceit* will confidently join Jim in predicting that the central bankers are going to lose: they are fatally conceited.

*Volcker: The Triumph of Persistence* by William L. Silber

The top-seeded Amazon review hammers this book, citing superior treatises (*Secrets of the Temple*, for example) that I have also read. The critic completely missed the point. This book is not about monetary policy; it's a *biography* of Volcker and his relationship to the banks and bankers. I really enjoyed the book and now have a much better understanding of the man called Volcker.

*Rise of the Warrior Cop: The Militarization of America's Police Forces* by Radley Balko

This was, quite possibly, the most disturbing book I've ever read. I moved it to the top of a huge list when Ferguson broke out. Balko documents the slow, methodical militarization of the police force and the accompanying risk to our civil liberties and liberty itself. It could have been hyperbolic, but it was not. I had to complete it in small doses owing to relentless agitation, but it gets my highest recommendation. It also dovetails nicely with Matt Taibbi's *The Divide* (see below).

*The Divide: American Injustice in the Age of the Wealth Gap* by Matt Taibbi and Molly Crabapple

This book is two stories combined like two decks of cards shuffled together. The first is the story of the failure to prosecute Wall Street crimes. Taibbi does a good job of revealing in disgusting detail how and why the judicial system failed. (Plot spoiler: Holder sucks.) It was nauseating. The second is a story of the wholesale roundup and prosecution of impoverished city dwellers with minimum regard for the rules of law and maximum regard for profit motive. You read that right:

profit motive. I am no putty-headed liberal, but this story is lurid and grotesque. This book is not fun, but it puts some of the emergent civil unrest into context.

*What It Means to Be a Libertarian* by Robert Murray

An easy-to-read treatise by one of the more vocal supporters of libertarianism. It is a pragmatic approach to deconstructing many ham-fisted government interventions in our private and economic lives. Murray explains how interventions fail to optimize outcomes as the paternalistic types convince themselves their motives are pure.

*The Deep Dark: Disaster and Redemption in America's Richest Silver Mine* by Greg Olsen.

Olsen describes the harrowing tale of the fire in the Sunshine silver mine in 1972—the largest mining disaster in US history—that killed hundreds. It's not about silver but rather human tragedy. I enjoyed it, but it is unlikely to climb to the top of many readers' lists of must-read books.

*The Fifties* by David Halberstam

David is one of the great narrators of easy-read modern history. He describes all aspects of postwar America in a decade viewed by many as the fundamental linchpin of the tumultuous decades to come. The social, cultural, and geopolitical events will be particularly interesting to boomers reaching back to their childhoods. It was a nice follow-up to *Cronkite*.

*New York Burning: Liberty, Slavery, and Conspiracy in Eighteenth-Century Manhattan* by Jill Lepore

The book introduces the slave rebellion of 1741. The frustrating part of the story is that the rebellion may have been real, or the hunt for a conspiracy may have been New York's comeback to the Salem witch trials. Historians will never know. What's clear is that a lot of slaves were crucified in one of the darker periods of US history. The positive side of the book is that you get a great look at slavery in Manhattan, which was a very different beast than its variant on Southern plantations. It's a niche read.

*Pam, Sam, and the Paper Money Sham* by Bill Borden

The author sent me this charming children's tale of how inflation is a destructive force. Given the topic, I think he did a good job, and the book certainly has little or no competition. In some sense he is channeling Dr. Seuss's morality theme. On the contrary, I was left with the sense that the topic is pretty edgy. A small cadre of Amazon evaluators loved it. Paul Krugman is unlikely to read it to his grandchildren.

*The Drunkard's Walk: How Randomness Rules Our Lives* by Leonard Mlodinow

I love this book genre. This example is on par with Daniel Kahneman's *Thinking Fast and Slow* and better than Nassim Taleb's *Fooled by Randomness* (which I still like, I hasten to add). Mlodinow wanders through the role of random patterns in our lives that are sometimes stunningly difficult to understand in depth. He develops statistical thinking methodically with very clever vignettes and good prose. This is a classic must read.

*Influence: Science and Practice* by Robert B. Cialdini

This book came massively praised by Charlie Munger in a stupendous 1995 interview at Harvard Law School.[ref 489] It's another from the neuropsychology genre. The updated fifth edition describes the half-dozen categories of manipulation that we are subjected to throughout our daily lives. The ideas are presented as vignettes, and they are entertaining and very thoughtful.

*Unbalanced: The Codependency of America and China* by Stephen Roach

With the perspective of a Wall Street economist, Stephen has become a leading expert on the relationship between China and the United States. I sense that this book has not been widely read, quite possibly because of the complexity of the topic or the public's failure to understand how China–US relations will define us for decades to come. The author's past writings reveal him to be bullish on China. His careful analysis of the codependency shows that this position is not held without serious concern. China's newfound enthusiasm for capitalism is likely to be seriously challenged in the next few years. The US's unsustainable consumption of Chinese goods will be a very tough nut to crack. Disclosure: Stephen provided a copy of his book.

*The Golden Revolution: How to Prepare for the Coming Global Gold Standard* by John Butler

As one of the more prominent gold enthusiasts, the author methodically walks us through the history of gold-backed currencies, the rise of fiat currencies, and the case for why we will be returning to a gold-backed global currency regime at some point, a premise I have begun to endorse. The book sprinkles in a solid dose of Austrian business cycle theory. I'm not sure it will sway any die-hard Keynesians to see the light—a high bar—but those whose interests in gold have been piqued will find this a highly readable and useful treatise.

*David and Goliath* by Malcolm Gladwell

Bashing Gladwell has become a bit chic. I could really care less if he lacks rigor. The man can tell a story. *David and Goliath* uses Gladwellian anecdotes to illustrate that asymmetries in power struggles are often not what they appear to be. The superior force (Goliath) never had a prayer against the underdog (David). The origins and historical examples of these asymmetries are very entertaining, but apparently only if you are a Luddite.

*All the Presidents' Bankers: The Hidden Alliances That Drive American Power* by Nomi Prins

Nomi goes through the history of the 20th and 21st centuries looking at the relationships of half a dozen bankers with US presidents. The story is about how a system depending on powerful men (Morgan, Baker, Lamont, etc.) and functioning as the fourth branch of government mutated into a multi-headed hydra in which the prominent bankers—we all know their names—are running organizations more akin to the Borg. The relentless push for deregulation, backstopping of dubious practices, and amassing of political influence is presented with shockingly limited hyperbole. Nomi's tale of horror is not as nauseating as I expected it to be, but the rot of the banking system is inescapable.

*Global Pension Crisis: Unfunded Liabilities and How We Can Fill the Gap* by Richard A. Marin

Rich is the former CEO of Bear Stearns Asset Management and currently a colleague at Cornell. He provided a copy of the book, which examines the coming pension crisis with a global view similar to that of Laurence Kotlikoff's domestic one (*The Coming Generational Storm*). Both of these books tell harrowing tales of underfunding that will define our lives for decades. Both grope for solutions that, quite frankly, I don't buy. Their original assertions are correct: we're screwed.

*The History of Science: 1700–1900* by Frederick Gregory

The Teaching Company offers stupendous trimester-length, college-level courses on CD (usually about 20 CDs). This one is a follow up to *The History of Science: Antiquity to 1700*. As expected, the quality is high. I recommend hitting the website and browsing the topics. *Never pay the list price.* They are often on sale for $50–$70 (80% discount). I have listened to more than 20 of these courses on CD to date.

*The Brain That Changes Itself: Stories of Personal Triumph from the Frontiers of Brain Science* by Norman Doidge

The topic of neural plasticity—the capacity of the brain to rewire itself—is fantastically interesting, which is reason enough to read the book. The stories of the manifestation of this plasticity are often incredible. That said, the book has two weaknesses: (1) as it proceeds, the scientific rigor of the narrative seems to be lost, and (2) one gets a bit of an infomercial feel as though the author is a tad overly attached to the players. Overall, I learned a ton.

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