Central Bankers Take Note: The Numbers Just Don’t Add Up

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Disrespectful.

Harsh.

line grabbing.

These were the responses to my ‘central bankers are clueless’ remarks in [last Friday’s *Markets %26 Money*].

Everyone is entitled to their opinion.

Tomorrow night, Port Phillip Publishing is hosting an invite-only event…the ‘Doomers’ Ball’.

And for the record, I had no involvement in the naming of the function.

The depth of feeling behind the ‘clueless’ statement was a result of the content compiled for my presentation.

How could the central bankers be so oblivious to the numbers?

When you see the facts and figures, there are only two conclusions to draw.

Either the central bankers — controlling the destiny of the global financial system — are genuinely clueless, or they’re deliberately re

Clueless was the ‘kinder’ of the two.

It’s simply unfathomable to contemplate the ‘reckless’ alternative…that they are deliberately pursuing a course of action to ruin millio lives.

Hyperbolic? Over-egging?

Not when you look at the numbers.

In the US, RealtyTrac did the numbers on the fallout from the subprime lending debacle:

> ‘*From January 2007 to December 2011 there were more than four million completed foreclosures and more than 8.2 million fore starts…*’

That was in the US alone. When you add in the foreclosures in Portugal, Ireland, Italy, Greece and Spain, the figure is north of 10 m foreclosures. And when you consider that each home has, on average, three people residing in it, we’re talking tens of millions of liv

The root cause of this misery?

Greenspan’s decision to keep US rates too low for too long.

Yes, people and banks got greedy. And yes, they deserve some of the blame.

However, the emotional trigger to chase a quick buck would not have been pulled if the Fed had acted responsibly. Obviously, Gree was clueless to the effect ‘dollar signs in the eye’ can have on people’s behaviour.

> ‘*The notion of a bubble bursting and the whole price level* [of the housing market] *coming down seems to me, as far as a nationw phenomenon, is really quite unlikely.*’

> Alan Greenspan, 27 February 2003

Dr Greenspan’s eyes were opened wide when, in October 2008, he gave testimony to a US congressional committee hearing into th subprime lending fiasco:

> ‘*I made a mistake in presuming that the self-interests of organisations, specifically banks and others, were such that they were b capable of protecting their own shareholders and their equity in the firms…*’

Greenspan’s mistake cost people more than just their homes.

Brad Pitt’s character in *The Big Short* nailed the maths when he said:

> ‘*If we’re right, people lose homes. People lose jobs. People lose retirement savings, people lose pensions. You know what I hat f**king banking? It reduces people to numbers — every 1% unemployment goes up, 40,000 people die, did you know that?*’

Analysts can quantify the financial cost of the crisis…Bank of America wrote off many billions.

But what number can you put on the human cost?

For some, there’s no dollar amount that would be adequate compensation.

These so-called prudent bankers are acting out their ‘tried and failed’ theories with people’s lives. All in the name of ‘growth’.

When I say ‘clueless’, it really is being kind.

Here’s another number for you: US$60 trillion. That’s the amount of <u>new</u> debt that’s been added to the global financial system since

More debt to solve a debt crisis?

Could you be any more stupid?

In last Friday’s *The Australian*, there was this little line: ‘Housing fall to “shock” economy’.

The first two paragraphs give us a clue as to what the RBA is thinking:

> ‘*A sharp drop in house prices would not trouble “resilient” banks but would cause home owners to rein in spending and produce significant economic shockwaves, Reserve Bank Governor Philip Lowe has warned.*

> ‘*Dr Lowe also pushed back against criticism that ultra-low interest rates were to blame for lack of affordable housing in Sydney a Melbourne.*’

I’ve heard that ‘resilient banks’ comment before. That’s right…

> ‘*Not only have individual financial institutions become less vulnerable to shocks from underlying risk factors, but also the financia system as a whole has become more resilient.*’

> Alan Greenspan, 8 May 2003

What's the test for 'resilience'? Is it based on the same modelling as 'property prices have never fallen on a nationwide basis' premise? Until real and unpredictable forces place stress on the system, we have no clue how resilient a financial system may or may not be.

The reverse wealth effect would cause homeowners to rein in spending. And what's so bad about that? Save more, pay down debt, and spend less. Sounds like responsible money management to me. It's just a shame that it takes a 'shock' to bring people to their senses.

And finally, historically-low interest rates have played no part in enabling people to borrow ridiculously large sums of money. Definitely not. Don't blame us…there are other factors at play.

Really?

Please answer me this simple question: Can you borrow more money when interest rates are at 3% or 9%?

Just to make it easy for academic economists, this is not a trick question.

In addition to making debt more affordable, QE made it even more accessible.

Another question: Do you think all the trillions of newly-minted currencies (courtesy of central banks) had an impact on asset prices?

That money had to go somewhere.

Capital moves around the world looking for mispriced opportunities. The RBA must have known that Australia would attract its share of these crisp new greenbacks, pounds, euros, yen and yuan.

It is disingenuous of the RBA to say the housing bubble is not their fault.

Dr Greenspan *presumed* people would act out of a desire to protect the greater good. Wrong. The only self-interest they had was their own.

People inherently want more. If you have the capacity to borrow $1 million (thanks to low rates), then guess what? 11 out of 10 people take the maximum on offer.

It's a very simple equation: The more you borrow = the more you bid up property prices.

And the more you bid up property prices, the more people try to borrow.

The Australian, 4 May 2017:

> '*The nation's largest mortgage insurer* [Genworth Mortgage Insurance] *has warned that borrowers are scraping together deposit* *credit card debt, parental loans and other forms of risky "unsecured debt" as tougher regulations force lenders to require larger d*
> '

You just know this is not going to end well.

Groundhog Day is written all over this.

An engineer builds a bridge and it collapses, resulting in casualties and fatalities.

Would you expect the authorities to let the same engineer build a replacement bridge using the same blueprint and specifications?

No. Lessons are learned; better, stronger bridges are built.

Yet this logic is abandoned when it comes to the economy.

The system collapses, and the people who were instrumental in building the flawed structure are allowed to do it all over again…using the same debt-funded consumption model to achieve ‘growth’.

How many times does the system need to collapse before someone says ‘We need a better way’?

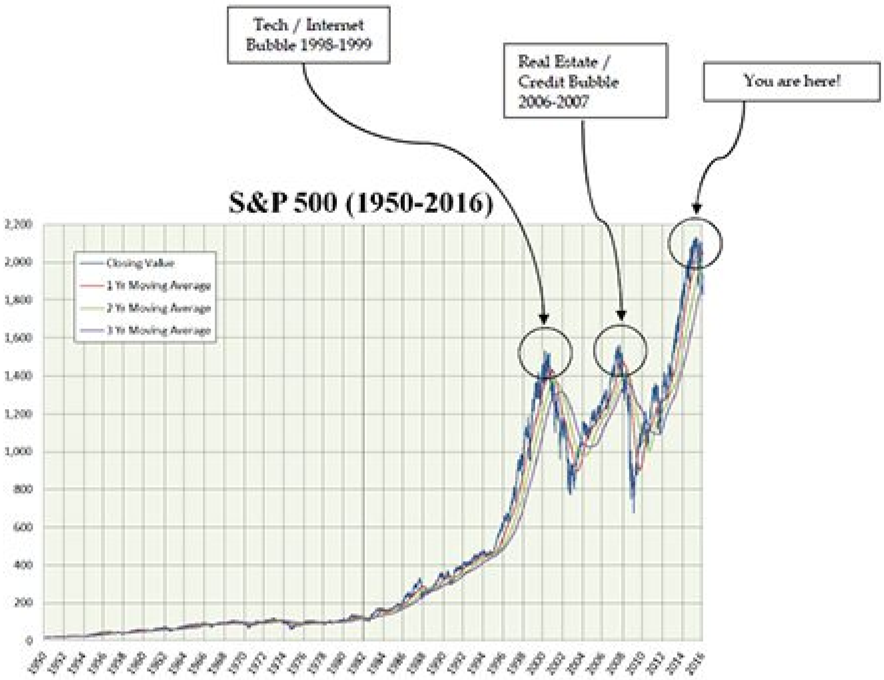
I did say there are only two conclusions to draw.

But there’s actually a third.

‘*Insanity: Doing the same thing over and over again and expecting different results.*’

Albert Einstein was a mathematical genius. He knew when the numbers didn’t add up.

For those who get a little confused by percentages, ratios, algorithms and the like, this chart of the S%26P 500 index should tell you all you need to know.



Source: Value Walk
[Click to enlarge]

We could change the captions on each peak to ‘clueless’, ‘reckless’ and, finally, ‘insane’.

These three market peaks all add up to one thing…capital destruction.

Cheers,

Vern Gowdie,
For *Markets %26 Money*

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Vern Gowdie

Vern Gowdie has been involved in **financial planning** in Australia since 1986. In 1999, *Personal Investor* magazine ranked Vern a
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