WHAT PERIOD DOES THIS DESCRIBE?
1/29/07

1. Investment in capital goods increased over 60%.
2. Personal consumption was even greater than 60%.
3. The purchase of new electronic items increased 300%.
4. Worker productivity increased 43%.
5. Overall credit grew 61% in less than 10 years.
6. Consumer credit expanded even more.
7. Wages did not increase as fast as profits.
8. There was little to no inflation (cost of living).

No, it is not 1997 through 2006; it is a business profile of the 1920’s. It was a “new era”. John Maynard Keynes hailed the period as a triumph of the Federal Reserve Board. He also said recessions were a thing of the past. Irving Fisher, the leading economist at the time, said the stock market was at a permanent, new high level. As a matter of fact, Fisher later lost his entire investment portfolio in the stock market during the 1930’s.

There were a few lonely voices that sounded the alarm in the late 1920’s. Roger Babson was one, but more importantly from our view, were the warnings of F.A. Hayek, the leading Austrian economist at the time. He and the other Austrians understood the problem: too much credit along with asset inflation. As fate would have it, Keynes, although completely wrong, became a hero. Hayek, although right, was nearly lost in obscurity. This is a prime example of the fickleness of politics and public perception. It seems as if Washington and public policy are usually populated and executed by the least common denominator when it comes to people.

It seems to us that the end of a period similar to the 1920’s is at hand. Again, the Keynesians say no, and the Austrians say yes. Probably the most reliable of the economic indicators that point downward is the chart below. This chart is quite bearish; however, the announcement of the plus .03% December indicator sparked a rally in the stock market. Go figure.

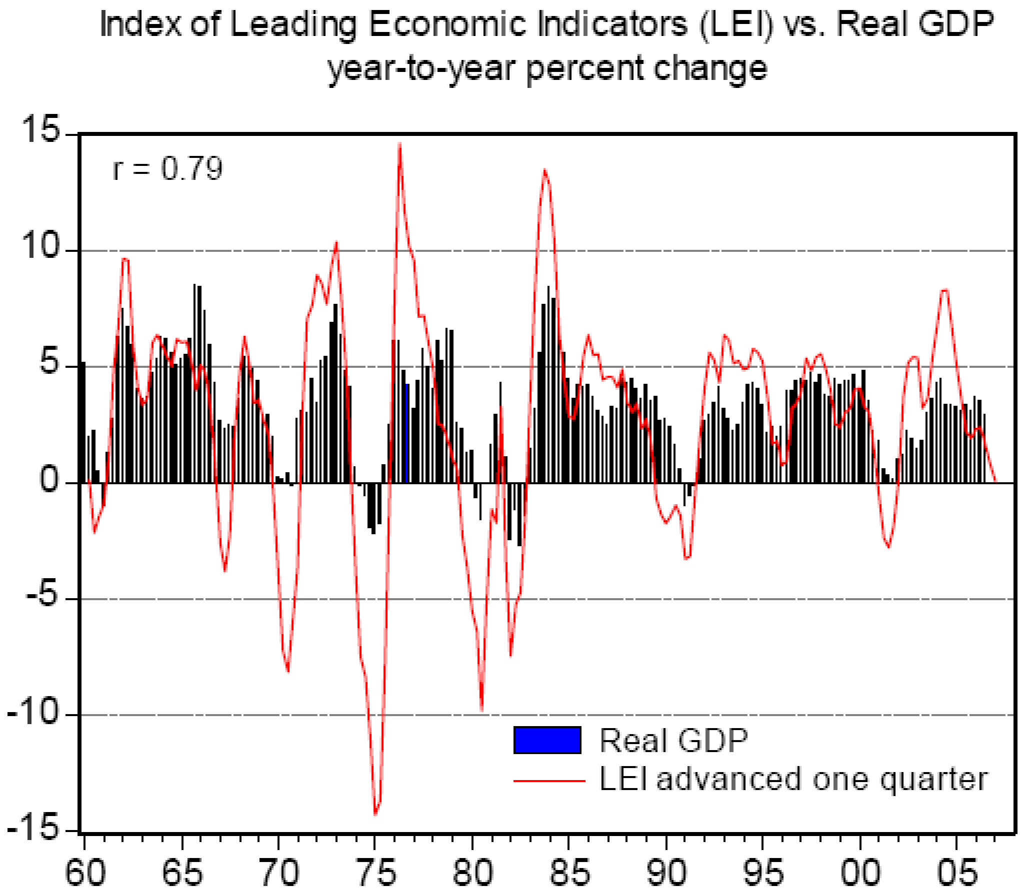

Chart taken from NorthernTrust.com

Yes, we have said this before. In June of 2000, we advised our clients to either sell their stocks or find a way to stop their losses. We think that time may have come again. Isn't it better to leave some money on the table as opposed to losing it and maybe the table also?