alpha+ capital management

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I had occasion recently to reread some essays written in the mid 1970’s and 80’s by respected economists. They analyzed the troubles of the time, described cause and effect in the overuse of credit and how that drove price inflation, followed by a price reversal which was accompanied by threatened failure of financial institutions. Economic depression was seen as possible though not likely and there was general uncertainty as to what would make the problem go away. A noteworthy thing about the articles is that they read as if they were written recently instead of thirty years ago.

Background conditions varied but the description of excessive leverage, systemic stress, public fear and the resulting reactions and behaviors were pretty much the same. It is good to remember that we have survived such episodes before.

The fear generated by *not knowing* underlies the attitude that is better to overdo a good idea than underdo it. Restoration of liquidity to large institutions is an emergency necessarily met by cash infusion. Then, when the economy begins to revive the liquidity is not retracted for fear of choking off the budding recovery and when the velocity of monetary transactions recovers, it fosters an acceleration of inflation.

That much ineptitude is understandable and forgivable. More worrisome is that the confusion and fear energize those who mistrust the free market capitalism which created what we have and opens the door to policies driven by passionate, wrongheaded ideologues. New rules must evolve to suppress parasitic gaming in a world of networked communication systems and newly contrived securities but there is potential for mischief here too. And the exercise of affecting shock at finding the trait of greed among humans is wearing thin.

This time around, the government is accepting control of finance, autos, energy, education and medical care, and the public does not seem much alarmed at the prospect. The concept of socialism may not carry a negative connotation to the youthful, moderately aware public. For us, however, it is enough to postpone optimism about returning to previous levels of corporate earnings and investment values anytime soon.

The powers that be are willing to modify traditions of ownership, contracts and taxation under the banner of fairness. Recent indicators include the promise to raise income taxes on a minority of taxpayers to transfer cash to others, some control of corporate compensation and the dismissal of the president of General Motors by the president of the USA. The power coalition now includes labor unions, government workers, racial bloc voters, university faculties and students, the traditional communications industries and large corporate supplicants, together with the presidency and both houses of Congress.

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That degree of political imbalance could permit a shift in the relationship between personal independence and government as guide and nurturer and one hopes it will swing back before too much damage gets done. An alternative is to set the arguments out in public and win the socialism/ capitalism debate in that arena.

Under these conditions the breadth of potential is from troublesome deflation all the way to exaggerated inflation. An appropriate response is to improve inflation protection with inflation protection bonds. Some gold bullion is reasonable. Real estate with moderate leverage at low fixed interest rates supported by ample cash flow would be sensible. Stocks remain the basic carrier of future prosperity for the patient investor. The possible entry into a Japan style decade of slow growth no longer seems so bad.

I've been wrong, but it does feel like the *steep* part is over.

John May