

Since this evening is the conclusion of the Spring 2009 “Thursday Evenings with the Schmids”, I thought it appropriate to summarize the series before offering an economic forecast for the future.

When Maryanne first asked me to participate, I saw my contribution as an economic historian simply to point out that, stripped of the sound and fury of a highly complex and computerized economic hyperbole, there was really not much new. As a matter of fact, over the last three and a half centuries our antecedents had been forced to deal with similar absurdities and extravagances.

Furthermore, since mankind had been down this path before—several times—I knew it was possible to eliminate much of the uncertainty that is anathema to markets, and even to make fairly detailed and informed judgments upon which to base business decisions. This much I could do without presuming to tell you how to run your businesses, which would surely have led to your even greater discomfort.

So in the First of Six presentations, I took you back in time to the Place Vendome in Paris in the year 1796 to witness the finale of the Revolutionary government’s experiment with mortgage-backed securities, which were used as money in a vain attempt to restart their collapsed economy. All day before a fascinated crowd, carts loaded with bales of the now discredited notes were driven to the square and burned, which was taken as an official admission of their worthlessness by the citizens, who added their own notes to the fire.

In the Second of Six, we explored the similarities of four preceding historical bubbles by visiting The Dutch Tulip Bubble of 1634-37, the French Mississippi Bubble of 1720, the Weimar German Hyperinflationary Bubble of the early 1920s, and the US Stock Market Bubble of the latter 1920s, the collapse of which led to the Great Depression of the 1930s. I suggested that there would prove a greater similarity between the collapse of our Credit Bubble and Weimar Germany’s than with the Great Depression, as our current bubble would also be capped by an orgy of multiple-trillion unit expansions of the money supply.

In the Third of Six, I explained that more than 77% of American cash circulates offshore, leading to a shortage of money and credit in the US, and suggesting that area businesses may want to market their wares abroad as a single economic unit, called Alta, or Upper California, particularly wines and tourism, in order to earn

some of it back. I cited the grand coup of the Swiss National Tourist Office in attracting generations of English tourists to their mountains by suggesting the Swiss Alps were the only ones that mattered. Similarly Europeans are of the certain opinion that weather in the Golden State is always perfect, therefore California never produces an imperfect vintage.

In the Fourth of Six I felt compelled to warn our audience not to be taken in by false market bottoms, so-called “sucker rallies”, but to be patient and remain as liquid as possible. So that small business owners would be prepared for any eventuality, I set some parameters for a worst-case scenario, which I was gratified to see was accepted without undue alarm. Not a single canister of oxygen was required, though I did notice a slight uptick in traffic at the bar.

Accordingly, I thought it time in the Fifth of Six to lighten the mood and visit classical English economist W. Stanley Jevons for his humorous narratives of barter with three very different characters. One, John Higley of Massachusetts Bay Colony, who minted his own copper three-penny pieces from the family mine in New England in 1737 to satisfy his thirst for Scotch whiskey. The second, French diva Mademoiselle Zèlie, who wrote in her diary at the end of the nineteenth century of her experiences in singing arias for the natives of Tahiti in exchange for farm animals and coconuts. And finally, the adventures of a proper English gentleman named Mr. Wallace and his party in bartering for their dinner on a small island in the Malay Archipelago, providing us with a lesson in the art of bartering first for money substitutes, like bottles of spirits and cutlery, as a way of enhancing liquidity, which could then be exchanged for the items wanted later in a deferred double exchange.

And finally, in this Sixth of Six, I will offer a scenario for the period ahead so that you will not be caught unawares while you are all preoccupied in trying to make the most of the summer tourist season.

First we will begin with the obvious:

The new round of so-called “Alt-A” mortgage defaults, brought on by resets doubling or tripling monthly payments beginning in mid-year, will depress housing further, put a damper on spending and burden commercial real estate. Foreclosures will continue to rise, while statistics hyping increased sales will be misleading, as they will mostly reflect the foreclosure market, so that median home prices will continue to fall, especially in California, Nevada, Arizona and Florida.

The falling home prices and rising unemployment will trap unwary investors and businesses who buy into the early market turnaround hype currently making the rounds but will present opportunities for those who are patient and maintain their liquidity.

After an initial flurry accompanying the initial bailout funds which the markets will hail as the expected “turnaround”, business will begin to falter and it will become obvious that larger bailouts will be necessary.

In response to continuing mega-injections of bailout money, markets will ebb and flow between feverish activity and stagnation, but despite the ongoing hype by the Treasury, and the Fed, serious questions will begin to arise in Congress and on Main Street as to the validity of the bailout strategy as federal deficits rise dramatically . More banks and businesses will fail or be merged as it becomes increasingly clear that the failed Credit Bubble cannot be reinflated.

The dollar will be highly volatile as foreign demand fluctuates. The Treasury and the Fed will monetize the debt on a grand scale, dramatically weakening the dollar and compromising the market in Treasuries. The foreign exchange markets will eclipse stocks and bonds and currency trading will reach \$3 trillion per day, then \$4 trillion or more.

As markets become more unsettled, there will be many business and investment casualties, but among the survivors will be those who will have heeded the ten minute mini-lessons of parts 1 through 6 of this series—a single hour in all—and who come to realize that the “Bailout Bubble” which is just beginning will morph into a “Currency Bubble” and who will take the necessary protective actions.

Finally, the 2 /12 hour drive from San Francisco, long seen as a negative by the counties north of Napa and Sonoma will become a blessing both for local residents and the crowds of economic refugees from the city looking for a less-expensive and quieter lifestyle. They will need everything. That’s where you come in.

Over the summer we will codify this roadmap, which we have come to call the “Blue Lakes Model” and its availability in the fall will be announced at www.thelodgeatbluelakes.com

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