



Macbeth and the Economy

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Shakespeare's Macbeth is a tale of deceit and intrigue, but also a path from what was, what is, and what will be.

It strikes me that Shakespeare was also commenting upon the economic problems of today, a backward time machine if you will.

In Act IV, Scene 1 of Macbeth, the three weird sisters* are stirring the cauldron into which they have cast unspeakable animals and chant, "double double, toil and trouble, fire burn and cauldron bubble". And at a later point "Fair is Foul and Foul is Fair." Hecate (Queen of the witches) enters and says "O well done! I commend your pains; and everyone shall share in the gains".

How timely this play is.

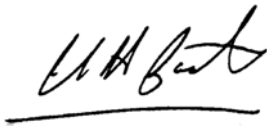
Past: While falling home prices and fear of mortgage default pressured the value of mortgage backed securities, Wall Street wrote their own tale of deceit and intrigue through the creation and touting of complex financial instruments that ostensibly reduced risk, yet multiplied risk beyond comprehension. One of the operative rules was "the more complicated the better". Credit Default Swaps ("CDS") were initially created to insure creditors against bond default. Instead, issuance multiplied far beyond insurance and turned into gambling opportunities for hedge funds and others to speculate upon default without having economic risk. Warren Buffett used the example of a million dollars of fire insurance on a one hundred thousand dollar home to describe the amount of Credit Default Swaps outstanding vs. the risks that were to be insured against. In the chase for high returns, many firms used exorbitant amounts of leverage that proved difficult to unwind. The financial crises caused Congress to pass the Troubled Asset Relief Program ("TARP").

Present: TARP has recapitalized the banking system, not removed troubled assets from the balance sheets of financial institutions. Investment Banks have either morphed into commercial banks or been acquired by commercial banks with a continuing set of financial and fear based problems. The Federal Reserve and the Treasury are throwing a myriad of rescue packages into the economic cauldron. There are strings attached to the receipt of Federal aid, yet the rules are either non-existent or vague, and change daily. The long-term consequence of stimulus injections has not been well thought out. The

Fed's action to lower interest rates to near zero allows the Treasury to print trillions of dollars on an "interest free" basis to consume the unsavory species in the pot such as consumer loans, car loans, sub prime, Alt- A, and whatever debt it can find to suck up all the risk assets of the financial industry. The lingering problem of how to unwind outstanding CDS paper remains.

Future: Troubled assets will be purchased ("Bad Bank" concept) hopefully at market-based (i.e. low) prices not book value. Mortgage and other debt will be restructured at the expense of creditors; fairness will not govern. Sufficient funds will be injected into the financial system to stabilize the banking system and avoid collapse. We will see more "nationalization" of banks and the system until bank balance sheets are cleansed. The Federal Reserve will ultimately repurchase debt created to stabilize the system to avert secular dollar depreciation.** Housing will recover as employment rises with Government sponsored job creation and qualified homeowners take advantage of lowered mortgage rates. A national clearinghouse for CDS will settle the values of good paper vs. bad. Financial markets will anticipate economic recovery and those who persevere shall share in the resulting gains.

The similarities between Macbeth and today occur throughout the play. For our friends that are interested, I will happily provide a copy of the play upon request.



Joel H. Jastromb
Chairman

*The word "Weird" first appeared in Macbeth, but a variant, "wyrd" was the name of an Old Norse Goddess of Fate.

** "Fiat Money Inflation in France" by Andrew Dickson White is another good read that has a tinge of today in it. The National Assembly of France issued money well in excess of the "Gross National Product" during the French Revolution, sending sponsors to the guillotine.