Hitting the Wall

by Mark G. Brennan

On October 8, Americans awoke to government reports that the domestic economy had shed another 95,000 jobs in September. Despite the billions of dollars mailed to select citizens in the form of stimulus checks and the politicized bailouts of protected industries, U.S. policymakers have failed to resuscitate the moribund economy or coax unemployment down from its ten-percent perch. But Washington's latest strategy for jump-starting business activity—"quantitative easing"—should horrify taxpayers because of its eerie resemblance to the efforts of Dr. Frankenstein.

Compared with this new stimulus effort, Mary Shelley's chilling tale has a relatively happy ending. Dr. Frankenstein's flat-headed ogre murdered only three innocents before fleeing into the arctic snows. By contrast, the viral effects of quantitative easing pose existential risks to the American economy, the U.S. dollar's reserve-currency status, and the global financial system. If you liked the currency policies of Weimar Germany's Reichsbank or Robert Mugabe's monetary skullduggery in Zimbabwe, then you'll love the Federal Reserve Bank's current flirtation with disaster.

The federal government spends more money doing things most Americans don't want done—drone attacks on Afghani weddings, maintaining the domestic sugar price at twice the international market price—than it is able to pay for by extracting tax dollars from those same Americans. As a result, the government must issue Treasury bonds to finance its deficit.

Few investors see any attraction in ten-year U.S. government bonds, which are currently yielding less than 2.5 percent, especially after factoring in the possibility of default. So instead of offering a higher rate to entice the Chinese or other high-savings nations to buy our dicey debt, the government has decided to buy its own bonds.

How can the federal government afford to purchase bonds, when it is already out of cash?

That is where quantitative easing comes in. The mechanics of the process are simple. First, the Federal Reserve creates money *ex nihilo* and credits the new matter to its own account. Then, with its make-believe bankroll, the Federal Reserve uses its electronic funds to purchase U.S. government bonds. (The policy's proponents scoff at those who equate such financial legerdemain with "printing money": Nowadays, money creation happens electronically. Memories of overheated Weimar printing presses only frighten those who are fixated on our benighted financial past.)

The central bank's technocracy believes that by taking money—or, in this case, computer bytes—from the government's left pocket and putting them into its right pocket, economic recovery will ensue. If only it were so simple, or at least not so risky.

Former Fed Chairman Alan Greenspan, whose two-decades-long easy-money regime was responsible for the last real-estate bubble as well as the late-90's stock-market orgy, warned attendees at a foreign-exchange conference about the bogeyman ready to spring from the Fed's computers. Bloomberg News quoted Greenspan as telling the assembled financiers that "We're increasing the debt held by the public at a pace that is closing [the gap between our debt and] any measure of borrowing capacity."

In laymen's terms, Greenspan's warning reflects the law that a borrower can only carry so much debt before lenders declare him bankrupt. Thus, the judgment of one former central-bank demigod not previously known for monetary responsibility: The United States is running headlong into the brick wall known as borrowing capacity.

It will be bad enough when international bond buyers stop purchasing U.S. government debt. But Armageddon will come when those bondholders decide to dump the paper they already own, driving up U.S. interest rates. Imagine how much worse the U.S. economy will perform when adjustable-rate mortgages rise from 8 percent to 14 percent, and credit cards jack up their 1-percent teaser rates to 19.9 percent, overnight. The national funeral for the domestic consumer will have to be canceled, as the only Americans liquid enough to attend will prefer the comfort of their Swiss chalets to lining Connecticut Avenue in the rain.

What will happen in the near future when the Fed unleashes its second round of quantitative easing—inflation—on the global economy?

Capital goes where capital is treated best. And today, the developing world treats capital better than the stagnant developed nations of the north do. The recent inflationary policies of the United States and the European Union have flooded the economies of Brazil and Indonesia with capital looking to exploit the higher interest rates and growth prospects common in developing regions. But this capital has no national loyalty or moral code; it will flee these regional upstarts at the first sign of economic weakness or political instability. Leaders of the developing world have learned through experience that foreign capital drives up the value of local currencies, which then impedes their ability to export.

In their pursuit of higher returns, global financiers arbitrage away the developing country's lower labor and raw-material cost advantages. This process devastates the host country when the parasitical capital reverses course by dumping the local bonds and currency. In the wake of this violent process lie unemployed workers, shuttered factories, and, in some cases, smoldering political unrest. As tempers flare and barricades go up in front of the national palaces straddling the equator, fund managers in New York and London will report successful quarterly results to their deep-pocketed investors, whose loyalty to the fund manager is as illusory as the fund manager's loyalty to the economies in which he invests.

The leaders of developing countries will want to rethink just how well they treat foreign capital, which remains forever free of national, ethnic, or moral attachments. Thailand's Finance Minister Korn Chatikavanji has done just that. On October 11, he proposed a 15-percent withholding tax on interest payments and a capital-gains tax on Thai bonds, all in an effort to temper the recent rise in Thailand's currency, the baht. Other leaders will likely follow.

In October, economist David Carbon of DBS in Singapore told the *Wall Street Journal* that every day another two billion dollars flows from developed countries to East Asian upstarts. Carbon fears that trillions of dollars from the Fed's first quantitative easing—"QE1"—have yet to be spent, even as the Fed has started to test the market's appetite for "QE2." The financial press could do us all a great service by eschewing the monikers proposed by the Fed and naming this ill-fated inflationary vessel Titanic.

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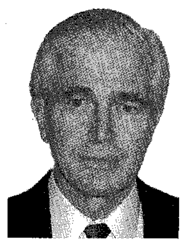

Include Me Out

The Social Network
Produced and distributed by Columbia Pictures ◆
Directed by David Fincher ◆
Screenplay by Aaron Sorkin ◆

THE SOCIAL NETWORK concerns Mark Zuckerberg and his cybercreation, Facebook, the website that now boasts 500 million active users and has made its "inventor" a multi-billionaire. On his site, you're free to divulge your most praiseworthy, intimate, and perverse behaviors to thousands. Merely register, and you instantly become a star, inviting the scrutiny of your "friends," as the site identifies your correspondents. Furthermore, your chosen circle can grow exponentially, since each of your friends has the option of suggesting you to their friends, who can likewise do the same. Should you be up to something sufficiently exceptional or weird or lurid, your circle could possibly rival that of the Almighty's, having a center that's everywhere and a circumference nowhere. Like certain celebrities, you'll taste Lucifer's temptation. Don't you deserve to outshine the Bible's out-of-date deity?

Not that Zuckerberg designed his site with such blasphemy in mind. No, his sinning was far less grand. His enterprise was driven by jealousy and anger. He wanted to strike back at the girl who had dumped him and, while he was at it, all those other girls whom he assumed would be only too glad to snub him in favor of more presentable swains. At least this is the way Aaron Sorkin and David Fincher have dramatized it in *The Social Network*. They've instructed Jesse Eisenberg to play Zuckerberg as a hopelessly gauche young man whose behavior suggests he may be suffering from Asperger syndrome, the form of autism characterized by high intelligence, obsessive focusing, and a striking lack of empathy.

We meet Zuckerberg first in a college bar with Erica (Rooney Mara), a pretty Boston University coed. He's trying to impress her with his Harvard connections and how he intends to make it into one of the school's prestigious Final Clubs. It's important to know the right people, he explains. As he patters on, she becomes increasingly restive and finally excuses herself, saying she has some studying to do. He expresses astonishment. After all, how much study time would anyone need to put in at BU? This is a step too far. Erica takes aim and fires. "You're going to be successful, and rich," she tells him with seeming sweetness. "But you're going to go through life thinking that girls don't like you because you're a nerd. And I want you to know, from the bottom of my heart, that that won't be true. It'll be because you're an asshole."

The rest of the film will confirm her prediction implicitly, while its conclusion will do so explicitly when another young woman observes, "You're not an asshole, Mark; you're just trying too hard to be one."

Stung by Erica's dismissal, Zuckerberg runs to his dorm, where he works through the night hacking into the other dormitories' websites, electronically snatching the profiles of their coeds complete with headshots. With this digital information, he constructs his own website, Facemash. Each page features pictures of two coeds and invites users to choose which is lovelier and make whatever other comments they wish. Facemash, indeed. It's Zuckerberg's kick in the face to the gals who think him unworthy. The girls are outraged, and the boys delighted. Soon Harvard's server is so overloaded with male responses to Zuckerberg's invidious invitation that it crashes. It seems that, despite the *de rigueur* training in tolerance and gender awareness throughout prep school, the Harvard gentlemen are simply raring to demean the ladies.

For this stunt, Zuckerberg is put on probation, but it's no big deal. He's become an overnight campus celebrity. The Winklevoss twins, prominent members of the Porcellian Club, the most exclusive of the Final Clubs, invite him to work with them on their idea for a social website to be called HarvardConnection. It will be exclusive, of course, inviting only the best of the best to participate. Then, as if to signal their devotion to exclusivity, the Winklevi, as Zuckerberg comes to call them, meet him in the bicycle room of their club, a foyer to its inner sanctum to which Zuckerberg cannot be admitted. With gracious *noblesse oblige*, they offer him a sandwich. No wonder the Jewish wunderkind came to betray these handsome WASP scholar-athletes.

Zuckerberg has been described by many commentators as being an outsider's outsider, a young man insulted by the privileged's closed doors. Using the Winklevi's idea, he devises the website that will become Facebook and takes it online without acknowledging their admittedly small role in its inception. From this moment, the war is on. Eventually, the Winklevi bring suit against him, as does Eduardo Saverin, Zuckerberg's classmate and closest friend who put up the money with