

Transcript of J.A. (Tony) Boeckh TV Interview on *Inside Business* - Australian Broadcasting Corporation – Sept 13, 2009

Finance expert discusses where the GFC stands Finance expert discusses where the GFC stands

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ALAN KOHLER, PRESENTER: The Wall Street investment bank, Lehman Brothers collapsed on the night of Sunday 14th of September, 2008, exactly a year ago tonight - triggering a global banking meltdown and a ruinous downturn that was christened the Great Recession.

Why was that event so catastrophic? What have we learnt since then, and where do we stand now after the most forceful and expensive series of government interventions in the market economy that's ever been seen?

One person with a deep knowledge of the disaster is **Tony Boeckh**, the former chief executive and editor of the highly respected **bank credit analyst**, an industry newsletter that delves into the big issues in the US economy and financial markets.

I spoke to **Tony Boeckh** from Montreal where he now runs his own private investment firm.

Well **Tony Boeckh**, we now know with the benefit of hindsight that allowing Lehman Brothers to go bust exactly a year ago this weekend was a very bad idea, but I guess the question is whether the authorities should have known that at the time?

TONY BOECKH, BOECKH INVESTMENT LETTER: Well I don't know. It's one of those things that's easy to make judgements after the fact and I don't think that people behind the scenes were privy to all the facts and the complications of Lehman's operations.

I don't think anybody really understood the full extent of their operations and the complexity - even the people running Lehman.

I think that was the problem with all those investment banks, but it certainly looks to me like as though it was a big mistake but we'll never know whether the crisis would have been a lot more moderated if they had bailed it out or maybe we would have ended up in the same place but my take is that it was a mistake.

ALAN KOHLER: What made it such a catastrophic event?

TONY BOECKH: Well the real source of the magnitude of the problem was the growth of private credit over the previous 25 years.

We use the term 'private sector debt super cycle' to describe it.

It's the biggest expansion of private debt relative to incomes or the growth of GDP that's ever taken place in history.

It lasted 25 years. In the 1920s the only other comparable period only lasted about six or seven years so there was time for these borrowers to get themselves just way way in over their head and it was just an accident waiting to happen.

ALAN KOHLER: And the timing coincides with the transfer of the chairmanship of the Fed, from Paul Volker to Alan Greenspan.

TONY BOECKH: Yeah I think that was a key thing and it's sort of ironic because Volker was your quintessential inflation fighter. He was so disturbed by the inflation that had taken place in the previous 10 or 15 years and he single handedly killed inflation in the United States and it was the decline in inflation and the decline in interest rates that took place after that that allowed this big private sector credit expansion to begin and it was fostered by, my take on it is that the Reagan deficits, the idea that you could have something for nothing and so I think the two combined led to the sort of whole sense of the public not having to take responsibility for themselves, they could get in over their head financially and the government would be there to bail them out.

ALAN KOHLER: And how important was the decision, way back in 1971, for the US to go off the gold standard? I mean, there's a sense that there was discipline on the gold standard, and that was replaced by the Volker discipline, but after he went there was no discipline.

TONY BOECKH: Well I think you raise an excellent point and I feel very strongly about that.

I think you really have to go back to the 1960s to really understand what happened. We had this monetary stability and sort of conservative finance and then what began to happen in the early 60s is that the US Government had trouble maintaining the international integrity of the dollar.

People started converting dollars into gold and there were various attempts through controls to try to prevent the dollar from going down, to prevent the gold price from going up and it was finally in August 1971 when Nixon took the Americans off gold, off the fixed price for gold and said we're all Keynesians now.

And that was the signal to the whole world that the United States would never allow international discipline to affect domestic policy in terms of stimulating prosperity and so on.

They would never allow these external pressures to force them into tightening, when for political reasons domestically they didn't want to do that.

ALAN KOHLER: But now there's the great reckoning isn't there?

TONY BOECKH: Yeah well we got a day of reckoning and going back to your point about going off the gold standard.

Where we are now, we've hit this avalanche of new money that's been created by a combination of fiscal deficits and intense monetary expansion in the United States and other countries as well and we're obviously heading towards very high government debt to GDP ratio in the United States.

Most projections private and public show it heading up towards 100 per cent of GDP, perhaps even higher and we've been there before.

The UK's been there after the Napoleonic War after World War One and Two.

The US has been there after the civil war and again after World War 2 and we managed to get out of that without a huge problem, without a lot of pain.

But the key point is that was there was a key international monetary standard that imposed discipline.

You had this sense that there would be monetary stability so nobody lost confidence in the money because of these high government debt ratios.

Now we're heading towards massive government debt ratios, massive monetary stimulus, I call this the great reflation experiment because it's truly an experiment.

We've never been here before and this is all occurring at a time when there is no international monetary standard, no international discipline.

The basic monetary standard is the floating US dollar which floats downwards, foreigners hold, I'm talking about foreign central banks, hold something like \$2.5 trillion of short-term money and they're watching nervously as the US embarks on this big reflation experiment and nobody knows really where it's going to come out, how it's going to play out in the future and I think that's the great uncertainty.

ALAN KOHLER: Well how do you think it's going to play out?

TONY BOECKH: Well I think in the short run we're ok. I'm bullish in the short run.

I think we're in cyclical bull markets. Stocks, commodities, corporate bonds, because we have this avalanche of money that's hitting a pretty depressed economy.

It's starting to recover but it's still very depressed.

We've got falling inflation, very low short-term interest rates, lots of liquidity in the system so this, we call this the sweet spot for the cycle of riskier assets when money is going into financial markets the money has to go somewhere and people are getting more relaxed about risk in the short-term so I think this is clearly good for markets and it's going to last for six months, 12 months, maybe a couple of years, we don't know.

But out beyond that, you have these big risks that we were talking about earlier and all this uncertainty and how that plays out and I think there's a good chance this will play out ok, but I don't have a high degree of confidence.

The people that are running this system, they totally missed the build-up to the crash, they missed the crash, they didn't understand it until after the fact and I don't think we can count on them not to blow it again.

It's the same people running the game.

ALAN KOHLER: Canada and Australia seem to have gotten off quite lightly because of the better shape of our banks and also because of each country's commodity export base, although Canada suffers a bit from being next door to America.

Do you think that those two lucky countries can continue to prosper in this way?

TONY BOECKH: Canada and Australia are remarkably similar in many ways, you mentioned we happened to live next to door to the United States, sometimes it's a blessing, sometimes it's not such a blessing, you don't have that situation.

Basically we're commodity orientated countries where our currencies are seen as commodity currencies, are banking systems are pretty sound, we've come out of this thing pretty well, we never had to in Canada bail out any of the banks and I think that's true in Australia as far as I know.

But we are faced with a short term problem, our currencies have gone up a lot, I know that in Australia there is a lot of talk about the reserve bank tightening policy which my personal take on

that is it would be crazy, you've had such a strong rise in the currency that that in itself is pretty stiff monetary tightening so I don't think they need to be raising interest rates there especially given the latest figures that came out on employment and unemployment.

ALAN KOHLER: And what's your take on gold at \$1,000 an ounce?

TONY BOECKH: Well that's a good question, I'm pretty neutral on gold in the short term, it's gone up a lot in the last few years relative to other commodities relative to the stock market, I think most of the demand as far as I can see is investment, so-called investment demand, financial demand, it's the final users are the jewellery trade and it's been extremely weak so I don't think it's a sound basis for a sustained bull market at this point in the gold market, so I'm really not that excited about it.

But in the short term if investors really decide they want to throw a lot of money into gold, you know they can push the price up pretty far, but I think you really need a recovery in jewellery demand and the perception that there is going to be a much higher rate of inflation and a falling US dollar to get that gold market really in a sustained new bull market from here and I don't see inflation coming back in the US for a very long time.

And I don't think the dollar, it's weak and vulnerable, but I don't think it's going to fall apart for the next couple of years.

ALAN KOHLER: Well thanks very much **Tony Boeckh**.

TONY BOECKH: Thank you Alan.

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