

Moral Hazard, Imputed Income and the “Gnab Gib”

By [The Mogambo Guru](#)

05/26/03 The Fed increased raw credit by \$6 billion last week. Unfortunately, this number is not particularly remarkable these days.

(In fact, I figure you are pretty grumpy that I would waste valuable ink to write about it, although I must assume that you are less upset than my wife, who helpfully points out that the lawn needs mowing a hell of a lot more than anybody needs me to point out the humdrum. So we will let it pass without further comment, except for a few muttered expletive-deleted, highly-caustic comments about the Fed and central banks in general, because that is the childish way that I act. But still, so caustic are my disparaging remarks that, in fact, I got blisters on my lips just from uttering them.)

Sauntering over to the banks, we look around the lobby and notice the eerie silence. We hear only our own footsteps going clunk clunk clunk, echoing through empty rooms. The tellers are all looking forlornly at empty tills, and we see that depositors took a chunk of money out. The only activity seems to be in the number of jackasses taking out huge mortgages and loading wheelbarrows full of “re-fi” money into the trunks of their cars.

Now, I don't know where YOU live, and if I really wanted to know I suppose I could ask John Ashcroft because as the head of the new Secret Police State Here In America he knows many secret and shameful things about all of us already, and more and more all the time, but over in this neck of the woods it is Not A Good Sign (NAGS) when the banks can't make loans, or won't make loans, to anybody who wants to finance business activity, assuming that there are some, although for the life of me I can't imagine who in the hell it would be.

Imputed Income: Stupid Loans

Come to think of it? Why would I expect banks to be loaning money, anyway?

Exactly what is it that corporate finance people are dragging into the bank loan department when they apply for a loan? Their income tax returns, all showing falling sales and rising expenses? Records and ledgers and journals showing the same thing? And you think banks are going to be loaning out big money to a business that seems to be spiraling into bankruptcy? To guys who are already over-expanded, over-indebted, and over-leveraged as it is?

And didn't the bank just get off the phone, talking to a long series of people and businesses about why their loans are now overdue? And against this backdrop of gloom, you think banks are looking to make loans that can't pay off? Hahahaha! Okay, okay, you got me there, you little rascal! Of course banks will make stupid loans! That's the whole history of banking crises! And

greed, too, of course. So can I coin the word “stupeed” to mean BOTH stupidity and greed? Sure!

And that is why we got saddled with the Federal Reserve System in the first damn place; so when the next stupeed calamity caused by banking stupeedity hits the fan, the whole system will not freeze up, due to one, or a few banks, going under from the aforementioned stupeedity.

Imputed Income: Ruptured Brain Syndrome

Now, this is usually where I take off on a tangent, usually via Hysteriaville, around the beltway through downtown Panicburg, crossing over to Madnesstown and ending up at the hospital being treated for Ruptured Brain Syndrome (RBS). RBS is where the brain is stressed by too much contradiction, as the cognitive dissonance between sound economics and the lack of horrified reaction in the economics profession concerning the actions of government, including the Fed, are so overwhelming.

This Ruptured Brain Syndrome is the new charity I am setting up to treat the only known sufferer of this rare disease, who is, in fact, me, and who is suffering more than mere words can convey. When I contemplate the fate that is inescapable, the fate that was ordained by the actions of the government and the Fed for all these decades, and now being hurried along by their exponential acceleration since the late 90's, then I end up in places I don't want to ever go. But being a new philanthropic charity, I'll need some celebrity endorsements, too, so if any of you know any famous movie stars who will compete on game shows and donate their winnings to my little charity here, have them give me a jingle.

But getting back to the banks... we note that, looking at the chart of Total Bank Credit since February, it has been about as flat as my average EEG-level of brain activity, which I maintain is a part of Ruptured Brain Syndrome, but everybody else steadfastly avers that it is just my surplus of stupidity made manifest by machines. But if the bank has flat Total Assets, but they own hugely more mortgages and hugely more government securities, then isn't it arithmetically correct that they are making dramatically less loans to businesses?

Last week, Richard Benson of Specialty Finance Group, LLC wrote a real nice piece entitled “The Federal Reserve: Moral Hazard's Best Friend.” And in it I can detect the lingering odor of fear, although he is not panic-stricken and paralyzed with fear like me. He starts right off stating that, “Moral Hazard occurs anytime the system encourages effective fraud or accounting magic that allows those in charge to benefit in the short run, leaving others holding the bag.”

The rest of the article is defining some of the ways that the Fed can keep anyone from getting stuck with the bag, because losses will be financed. He writes, with more than a modicum of sarcasm, or maybe that is just me reading something into his words that I want to see, about what I can describe is the current thinking of the Fed: “Indeed, everything gets financed. There is no need to ration investments to the best projects and credits. Saving is not necessary because there is credit creation. Since credit can be created without limit, credit underwriting is not necessary.”

The result is that “The Fed’s New Economic Model allows the economy and asset prices, like stock and housing, to ‘break free’ and rise without any concept of true value.”

Imputed Income: What Is Imputed Income?

Well, that is the result, all right. And it works like a charm in the beginning. But you can be sure that every buyer had a concept of value when they bought the stock or house, and predicated on an even better concept of what the next buyer would pay when they sold it to them, and thus ended up with this fabulous profit that has dollar-signs dancing in their glazed eyeballs.

“Most people don’t realize,” writes Benson, “that the Bureau of Economic Analysis (BEA) includes around \$750 billion of non-cash ‘Imputed Income’ from Personal Income.” What is this, this ‘Imputed Income’?

Ha, now I’ve gotcha. If you are ever in an idle conversation and it somehow gets around to a point where you want an example of the smug arrogance, overt fraud and outrageous stupeidity of government, I suggest that this is one you can use.

Sit back and relax and I’ll explain. Close your tired eyes for a moment, and imagine that we are in a beautiful, quiet little town, named (insert your name here) Town. There are only two industries in IYNH Town, the mortgage industry and the sex, drug and rock and roll (SD&RR) industry. If I buy a house, then the mortgage people get to spend my money on SD&RR and I get to spend none, but I get to stand on the porch of my house and watch them whooping it up and having a wonderful time with my money.

Then one day, when I pay off my house, I get to start spending the money on SD&RR and the mortgage industry spends none. Hahaha! Now watch ME have a wonderful time, you bastards! Hahahaha! Wheee!

As for the SD&RR industry, they see no change in spending. They only notice the change in WHO is spending the money. Ergo, total income has not changed. Ergo, there is no ‘Imputed Income’ from home ownership. This is just another example of voodoo economics.

Ditto military personnel who get meals and housing provided. The taxpayer paid for them, so there is no imputed income, and in fact there is only depleted income of the taxpayers. It is a income transfer, yes, but the serviceman got what the taxpayer had taken away. Again, there is no Imputed Income.

Ditto banks who provide me with services that I do not pay for. According the government, this is Imputed Income to me. But, whose freaking money do you think that they are using here? Mine! And, so what you are telling me is that they use MY money, so that THEY can loan it to THEIR friends and accomplices, and they make a PROFIT on between what they pay me for the use of my money and what they charge the borrower? And to keep me from withdrawing my money in disgust at being ripped off, they give me “free checking?” And so, because the bank calls it “free,” that the government figures that they are truly giving me something for free, and that it is imputed income to me?

Wow!

And, so, if you are in the military service and you have a checking account and you are not paying a mortgage on a house because you now have to live in your car, then do you have an Imputed Income? Or does it HAVE to be an actual house? Man, ain't voodoo economics wild?

Imputed Income: Enjoy Your Free Lunch

Still, reports Benson, 'Imputed Income' includes "about \$300 billion for supposed bank services that are not charged for, \$90 billion for people who own their own homes, and military personnel who received meals and clothes, etc. Imputed Income is upwards of 15% of Personal Income, but reflects no cash payment."

Let's see now... Personal Income these days is about \$9.2 trillion. Fifteen percent of \$9.2 trillion is about... \$1.4 trillion! And no cash payments...

I may have been willing to go along with the idea of 'Imputed Income' when I thought that the adjustment was some minor amount. But 15%? \$1.4 Trillion! No way!

Okay, now the deal is off, and I will no longer go along with this obvious fraud, and I will state for the record, and let me be totally frank here, and you might want to take notes, There Is No Such Thing As Imputed Income. It is a government- speak fraud. It is the government stating that there IS such a thing as a free lunch!

And not only that, but it amounts to 15% of what your piddly paycheck says you earn! Mr. Benson goes on to say, "The Fed announcing they are coming in with printing presses at full tilt may mean they are close to having their model wobble wildly out of control."

Frankly, this remark sets me off. I say that when the Fed comes in with printing presses blazing it means that things are ALREADY out of control! Why else would they do that, except in response to an emergency?

And I will go farther than that, and say that because the Fed comes in with easy money and credit, that whatever doofus "emergency" you think they see is just a hint of worse things to come, because the history of governments coming to the rescue guarantees that things will get only worse. And since our problems all stem from supreme fiscal and monetary insanity, the cure of providing more fiscal and monetary insanity will only make the problems worse.

Imputed Income: Gib Gnab

The proof of this loudmouth assertion is history itself; more fiscal and monetary insanity is the same course that every other country always took! Always! And here we are, doing it again, right now! And that cowardly course of action never worked for any of them! Not one! Never! And we think that now, in 2003, that things are going to be different? Hahahaha! We don't deserve to have any money, because it is against Nature itself, and completely contrary to The Way Things

Work In The Real World, to think that juicy, dumb pigeons as retarded as we won't get eaten by predators.

And the only thing that will make the Congress or the Fed stop is when the pain of printing money to keep buying more and more debt, to keep interest rates artificially low, in the face of rapidly rising-price inflation and a declining dollar, gets too horrific to bear.

I think the scientific term is the reverse of the "Big Bang." Oh, everybody likes to talk about what happened AFTER the Big Bang, but nobody likes to talk about what happened leading up to it. I, however, easily tread where no man has gone before! I fearlessly travel the Dark Side of the Force!

I am (pause for dramatic effect) Mogambo!

In the usual meaning of the term Big Bang, it means that the universe has collapsed onto itself, and squeezed everything into one tiny, dimensionless dot, and then there was an explosion outward, with glowing bits of burning stuff being hurled willy-nilly into the cosmos, and the sound it makes is a really loud BANG! The primordial matter goes shooting out, cools, gets transformed into planets and people and factories and intangible assets, creating the universe.

In the reverse, which I call the "Gnab Gib," because it literally IS the reverse of Big Bang, prices of stuff, say, oh, over-valued assets, disappear FROM around the cosmos into a single point. I mean, what IS the net present value of a factory that is about to condense into the nothingness of singularity where the Gnab Gib and the Big Bang meet? And since the factory will emerge from the other side of singularity after the Big Bang as dispersed blobs of molten goo, sprayed out into the cosmos, and it will not cool for, let me check my calendar here, oh, say, about a million years, then the future value of the factory must be approaching zero.

Except for those who "think long term." Then it has a P/E of, oh, 34. You know, right around in there someplace.

Regards,

The Mogambo Guru
for The Daily Reckoning
May 26, 2003

P.S. Mogambo Sez: Get away from stocks, and short them if you have the guts. Buy put options. Short futures. Buy gold. The Fabulous Mogambo Indicator has spoken.

Today is Memorial Day... or at least as it's being observed. The markets are closed today, rather than on Friday, as they might rightfully ought to be.

With that in mind, we thought we'd offer a "compte-rendu" (summary) of the markets "Year To Date". The following are the top-ten performing markets in the world circa May 26, 2003... (at least according to a website called: investors-route map.co.uk)

BRAZIL	up 39%
ARGENTINA.....	up 38%
ISRAEL	up 25%
LATIN AMERICA	up 24%
CZECH REPUBLIC	up 22%
CHILE	up 17%
AUSTRIA	up 15%
SPAIN	up 15%
IRELAND	up 14%
SWEDEN	up 12%

The site boasts “This table demonstrates the difference that can be made by successful international asset allocation, between the best at the top and the worst.” We couldn’t agree more, but we find it a difficult task to convey to our mostly US and UK readers.

All the same, you might be interested to know which markets are waiting to be dredged from the bottom of the barrel: our old friend Japan is right down there with a 6% loss YTD; Hong Kong and Taiwan share a similar fate... but India takes the cake, with an 11% drop thus far this year. All in all, not so bad considering the world is on the edge of deflationary abyss, eh?

Eric, how about some insight into these numbers?

(I know you’re dying to find out... so I won’t make you wait: The US, France and Europe are smack dab in the middle with 5% gains; the UK... a bit lower down with a hopeful 1% gain. For weighting techniques, you’ll have to visit their site.)