OPINION

Welcome to the bubble economy

Dean Rohrer

The market has shown what goes up comes down

By George Mullen and Tom Mullen

The vast majority of so-called experts issuing warnings about the real estate bubble have been missing a far more ominous danger, and it is one few mavens on Wall Street wish to publicize. Not only are we facing an enormous real estate bubble, we in reality are facing a series of growing asset bubbles all spawning from the same mother-bubble. If this mother-bubble begins deflating (due to its own weight or triggered by a catalyst), we can expect all the asset bubbles and our economy to be dragged down in short order. As such, the danger is acute.

Let's reflect on how we got to this point: From 2000 to 2002, the United States economy suffered the enormous shocks of the collapsing equity markets (NASDAQ, down 75 percent, S&P 500 down 38 percent) along with the Sept. 11, 2001, terrorist attacks. Nearly $7 trillion of U.S. investor wealth was wiped out. Sensing that political talk was not enough to avert a financial disaster, the Federal Reserve took the unprecedented action of reducing the fed funds rate from 6.50 percent in January 2001 to 1 percent by June 2003 — the idea being to keep the consumer purchasing at all costs in order to prop up the economy.

This easy money policy, which in turn propelled extraordinary appreciation in highly leveraged real estate, unintentionally gave birth to the mother of all bubbles, the ***liquidity bubble.*** This bubble is akin to the Death Star in the original "Star Wars" movie in that it can attack and overwhelm any target in its sites. However, this liquidity death star is not commanded by a Darth Vader with the intent to kill. It instead is commanded by millions of investors awash in excess cash and who are competing on the world stage for financial returns. These investors include national governments, pension funds, hedge funds, private equity funds, endowments, mutual funds, money managers and individual investors.

As any identifiable market, asset, sector or stock begins showing strong fundamentals and price appreciation, the millions of money commanders within the liquidity bubble begin pouring money on the targeted investment and ride herd on it until its valuation reaches the stratosphere. Simply put, it is investment asset inflation: too much money chasing too few perceived worthwhile investments. As such, this liquidity bubble has metastasized into a series of asset bubbles throughout the economy:

- U.S. real estate bubble: Since 2001, real estate appreciation nationwide has averaged 50 percent, but on the coasts and highly populated areas it has been far higher.
- Global real estate bubble: Since 2001, from Cabo San Lucas to London to Dubai to Shanghai — and most places in between — real estate appreciation has skyrocketed.
- Commodity bubble: Since 2001, the Dow Jones AIG Commodity Index has gone from 85 to 180, a jump of over 110 percent.
- Oil bubble — Since 2001, the price of oil per barrel has gone from $20 to nearly $70, a jump of over 245 percent.
- Gold bubble: Since 2001, the price of gold per ounce has gone from $260 to $570, a jump of over 115 percent.
- China bubble: With GDP growth of 9 percent to 10 percent, China has become the No. 1 destination for direct foreign investment. In both 2004 and 2005 over $60 billion was invested by foreigners.
- India bubble: With GDP growth of 6 percent to 7 percent, India has become the No. 3 destination for direct foreign investment. In both 2004 and 2005 over $5 billion was invested by foreigners. In tandem, Indian equity markets jumped 39 percent in 2005.
- Japan bubble — A rather modest upturn in Japan's economy translated into a 40 percent jump in the Nikkei Index in 2005.
- Corporate earnings and equity market bubble: Corporate earnings growth has been impressive, but is it based on bubble-laced revenue? If so, what does that say for stock valuations?
- Google bubble: Google went public in August 2004 at a price of $85 and has recently reached $475. A jump of over 450 percent in less than a year and a half.

Though we might like to think these returns represent normal and healthy market behavior, they do ***not*** — especially not in the wake of the equity market collapse of 2000 to 2002 and its destruction of $7 trillion of investor wealth, the Sept. 11 attacks and an economy of late that has produced meager wage growth, the smallest job growth in the private sector of any economic recovery since the 1930s, few new products and zero new industries. (That is, unless the development of China as the low-cost producer of all our material desires is considered a new industry.)

We have experienced many bubbles and their subsequent collapses over the decades. They are a natural part of the investment landscape and investor psychology: the Nifty Fifty stocks of the late '60s and early '70s, gold and silver in the late '70s, oil and real estate in the mid-'80s, U.S. stocks in 1987, Japanese stocks and real estate in the late '80s, and technology and dot-com stocks in the late 90s. However, we have never experienced so many bubbles at one time as we have today.

The markets have repeatedly proven that, sooner or later, all asset bubbles collapse. It is only a matter of time. Will the liquidity bubble and its offspring collapse under their own weight as the NASDAQ did in 2000 to 2002, or will it take a catalyst such as Iran going nuclear to initiate their descent? This remains to be seen. However, the risk of a massive destruction of capital followed by a gut wrenching global economic downturn should not be dismissed.

With the risks now properly illuminated, Johnny Nash's song lyrics come to mind: "I can see clearly now, the rain is gone, I can see all obstacles in my way

Gone are the dark clouds that had me blind. ... "

George Mullen and his father, **Tom**, have been in the investment management business in San Diego since 1987 and 1958 respectively. They can be reached via e-mail at gdmullen@gmail.com.

Battling the childhood obesity epidemic

By Philip R. Nader

You have to be living under a rock not to have heard of the "epidemic" of obesity that is apparent not only among adults in this country, but also affecting nearly a third of our youth.

Unless this epidemic is derailed:

- Our children and grandchildren will have *shorter* life expectancies than we do.
- Health costs will continue to catapult even more than the estimated increase from 2 percent in 1987 to almost 12 percent in 2005 — almost 70 billion — and we will *all* have to pay.
- We will see continued health effects of obesity, which are equal to about 20 years of aging. Diabetes rates will continue to rise among younger people with complications of heart and kidney disease. Teasing, bullying and stigmatizing of overweight youth spells out more youth with poor self image, depression and suicidal thinking.

If you are like many, you have heard of this growing health crisis, but probably think it is something for health care providers and individuals to handle. Just eat properly and get more exercise, right? It is easy to state this individual goal, but it is very complex to alter the environment, which has in large part led to the epidemic.

Obesity is due to many things including genetics, education, eating habits, activity levels, amount of TV and computer time. But many factors operate in the environment to thwart the best intentions of families and individuals.

These include streets and neighborhoods that force one to use a car or bus rather than walk to schools or needed services, lack of access to safe and convenient parks and recreational spaces, easy availability of fast and not particularly nutritious food, cutbacks in school physical education programs, lack of availability of healthful and lower sugar and fat snacks in vending machines. It thus becomes a much greater problem than merely the sheer force of individual will to change.

It will take all of us: individual families, neighborhood groups, businesses, schools, government and public health agencies along with health care organizations and universities to reverse the current trend which has tripled the rate of childhood obesity (more than 28 percent of California children in grades five, seven and nine).

So what can we do? Each of us can start to get informed about the problem. If you haven't seen it yet, read the supplement published in *The New York Times* on Sunday, Jan. 15, "Childhood Obesity" sponsored by three leading health care institutions in the state of California: University of California San Francisco, Kaiser-Permanente, and the School of Public Health at the University of California Los Angeles.

Our own county Board of Supervisors, along with the county Health Department, CHIP (Community Health Improvement Partners) and a distinguished group of community organizations and citizens, recently rolled out a master plan for obesity, "Our Community, our Children". See how you can become involved.

Take it upon yourself to address one or more of the many of the environmental barriers to healthy eating and activity for our youth, which you may find right here in San Diego:

- Find out how much physical education (and how active it is) children in a local school are actually getting. Observe an outdoor PE class. Are most children active or are many just standing around? How many children per teacher? Is there any recess?
- Are school foods nutritious? Visit a school at lunchtime. You know enough about nutrition to decide.
- What is in vending machines in youth-frequented places? What portion of offerings is healthy?
- Are there adequate, safe parks and places to play in the neighborhood?
- Are there convenient sources for fresh fruits and vegetables in the neighborhood?
- Attend city council meetings to lobby for revised planning for development and codes that will promote healthy nutrition, walking and biking.
- Become a personal advocate and information source for others about the problem.

Nader is a research professor in pediatrics at the University of California San Diego Medical School.

Extra-territorial reach of U.S. concerns Mexico

By Enrique Andrade González

On Feb. 3 executives with the Maria Isabel Sheraton Hotel in Mexico City evicted a delegation of Cuban citizens, who were staying at the hotel in order to meet with a group of oil company leaders from the United States that included representatives of Exxon Mobil Corporation. The meeting was forced to another hotel that is not U.S.-owned, because according to the U.S. Department of State it is against the law for U.S. companies, their branches and/or subsidiaries to provide services to Cubans.

The extraterritorial application of United States law, in this case the Cuban Liberty and Democratic Solidarity Act (also known as the Helms-Burton Act, and called by some the "blockade law") within Mexican territory has caused a number of negative reactions from the Mexican diplomatic, political, tourist and business sector. Especially since this included two American companies as prominent as Sheraton and Exxon.

Without exaggerating this particular incident, it could signal the beginning of a new age and reality involving the extraordinary enforcement of U.S. laws beyond its borders.

Traditional legal principle defines laws, plus the officials who apply them, as having legal effect and authority within the boundaries of the state. There are exceptions, however, such as some international criminal matters allowing extradition when a crime is committed in one state and citizens of that state flee to another. In such cases, once charged the accused can be returned for trial to the country where the crime occurred, if there are reciprocal and special procedures authorizing this that respect the laws of each nation.

The case with the Cubans took place in Mexico, without taking into consideration Mexican law or officials. This would suggest that the extraterritorial application of the Helms-Burton Act is not an exception that should be viewed as a diplomatic affront, but rather part of a more and more frequent trend of the United States to impose its laws and authority on other countries.

This has happened in France, Italy and surely in many other areas. And this is bringing about legal controversies with respect to territorial laws, principles and authorities that need to be clarified, apart from attitudes towards Cuba.

There is growing interest over this subject, and not just in Mexico. This dictate that requires North American companies or their subsidiaries in other countries to comply with U.S. laws over and above those of the nation where they are located.

A phenomenon that at the very least represents host country concern over taxes, trade rights based on contracts signed in Mexico or with Mexicans, as well as local laws connected with things like construction, the environment, highway administration, security, etc.

Furthermore, it remains to be seen if a legal violation by an American company in Mexico (and there are many) would be considered valid in the United States, in accordance with its laws and before U.S. officials. For example, in cases with civil liability claims for damages regarding something done by a company in another country.

And it is hard not to imagine that the protection of the U.S. government lies behind a U.S. company, which gives it an advantage over Mexican companies or those in Mexico that belong to businesses in other countries.

What happened in Mexico with the Cubans also sets a bad precedent for North American companies and their interests, mainly with respect to possible future involvement in strategic areas of foreign economies such as energy, banking and communications.

There is another factor to take into consideration, regarding the recent events that transpired in Mexico. It was representatives of Exxon and the other U.S. oil companies who met with the Cubans, in order to possibly invest or do work in Cuba, which means that those American companies were also in violation of the Helms-Burton Act.

If the meeting with oil executives seeking opportunities in Cuba had not taken place in Mexico, would the Cuban citizens have been evicted from the Sheraton Hotel? Probably not, for application of the U.S. law only affected American interests. Which is also why there are no diplomatic problems, and thus the Mexican government should not exaggerate any claims or protests.

Yet Mexico still must define the rules of the game for the future. And to do so it would seem that a new international order will be needed to tackle important issues related to extraterritorial controversies, legal matters, and authoritarian conduct.

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