The Washington Times
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Raising Stock Prices

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Published November 12, 2008

Why do you think the stock and commodity markets have exhibited record volatility? It is largely because government officials, both in the United States and elsewhere, are disrupting the ability of markets to calculate what prices would bring supply and demand into balance.

The government actors have created additional huge risks and uncertainties for both businesspeople and investors, which are depressing the markets and causing the recession.

In addition to the normal business risks and market uncertainties, the government actors have now added increased uncertainty about: the value of currencies and interest rates; exchange rates; government subsidies and "bailouts"; international commodity cartels; major proposed tax increases; and proposals for very costly regulations.

Monetary and interest rate uncertainties had been growing for decades; however, from the early 1980s onward, the Fed appeared to have gained an understanding as to how to achieve reasonable price level and interest rate stability. But the Fed clearly made major mistakes close to the end of the Greenspan era, and has since given markets little indication it now knows what it should be doing. As a historical note; the U.S. dollar price of gold remained constant at $20.65 per ounce for the century preceding 1932, a

period during much of which the United States, the United Kingdom and other major countries were on the gold standard.

The result was that the dollar could buy as much in the early 1900s as it did a century earlier. Once the world went off the gold standard, buyers and sellers faced the additional risks and uncertainties of big changes in the value of the currency, interest rates and major swings in foreign exchange rates. The U.S. dollar is now worth about one-twentieth of its value in 1933 (and also in 1833).

During the period of the gold standard, the price of money - that is, interest rates - also exhibited rather low volatility, and foreign exchange risk was minimal.

The advent of international commodity cartels, such as the Organization of Petroleum Exporting Countries (OPEC), has also added uncertainty in that forecasting the demand and supply of a commodity such as oil is no longer enough, but traders now also must guess what the government leaders who control OPEC are likely to do.

As politicians become more prone to fiddle with the tax code, particularly taxes on business and capital gains, risk is also increased. And finally, the huge growth in both existing and proposed regulations and regulatory costs is adding another great element of uncertainty to estimating the value (future profitability) of any company.
The specific reasons for the current volatility are:

- Uncertainty over President-elect Barack Obama's tax and regulatory plans.
- Continued confusion and uncertainty over Treasury's bailout policies.
- Uncertainty over how much OPEC will reduce oil production.
- Questions about whether the risks of deflation or inflation are greater and what the Fed plans to do in either case.
- And how far the European and Japanese central banks will reduce interest rates to combat their respective recessions.

To reduce the uncertainty in the markets, the Treasury needs to give a clear and coherent statement as to its formula for extending and ending bailouts to companies, and to be totally transparent in both its intent and execution, which so far it has not done. The Fed needs to be clearer about what it sees as the relative risks and to give the markets a road map of what it intends to do when given either further negative or positive data about the economy.

If President-elect Obama were to announce he would not propose increasing any business, capital gains, or dividend tax for at least two years, this would give great reassurance to the stock markets, and would likely push them in a positive direction. If he were also to announce he would not put any punitive environmental restrictions on the energy industry for at least several years, it would both foster a stock market and real general economic recovery. (Mr. Obama's threat to shut down the coal industry has greatly frightened not only the coal industry, but all companies that depend on cheap and reliable electricity generated by coal, and is killing new investment.)

Mr. Obama missed an opportunity to calm the markets during his press conference last week by refusing to give any specific indication of what his economic proposals will be when he takes office.

He did indicate modifications would be needed in his campaign promises given the current economic situation, but by avoiding naming the modifications he is likely to make, he added to the uncertainty. By refusing to be specific, Mr. Obama and his advisers appear to overlook the fact that every day the markets drop, fewer people buy goods and services. As a result, the recession will only get deeper, which will make the challenges the Obama team faces upon taking office that much greater.

From the day after the election, it became an Obama market (and, in fact, it has been an Obama market from the moment he gained the lead in the polls two months ago), and he will be held accountable sooner than he may think or wish. The sooner he jettisons his destructive trade, tax, spending and regulatory proposals, the quicker the economy will begin to recover, and the more rapidly his fellow citizens will begin to benefit.

People will not blame Mr. Obama or the Democrats for reversing course and enacting pro-growth policies, but the body politic will throw them out if they fulfill campaign promises that leave the ordinary citizen in an economic rut, or worse.

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