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Voters Got What They Wanted - More Socialism

By Russell Redenbaugh & James Juliano

Yesterday's election was a vote for more socialism. It is what the majority of voters want, and it may even be what a majority of public companies want. But it is a bad idea.

We define socialism as the use of government and public resources to protect people from the consequences of their actions. Under this definition, we already have a great deal of socialism here in the United States. The current Bush administration's financial bails outs, whether necessary or not, are just like the RTC in 1990 and are another example of the government socializing the losses in real estate, mortgage and financial markets.

Many large companies, especially those whose growth is behind them, prefer government to protect them from both change (especially in the form of new competition) and the consequences of their mistakes. There are numerous examples of these types of companies in the auto industry, insurance industry, banking industry and even in city and state governments.

The stock market is comprised of companies that are already public, and thus is a measure of successful companies. Ironically, these already successful companies often prefer to be protected from upstarts, the unformed or even the unborn company. There is no stock index of unborn companies. The unborn companies are often incubated in the hatcheries of venture capital firms. They may also start as your average "Joe the plumber" small business or in the dorm room of an entrepreneurial college student.

Microsoft certainly prefers to be protected from an upstart like Google in precisely the same way that Digital Equipment and IBM wanted protection from former upstart Microsoft. In fact, it is clearly in the self interest of well established public companies to encourage and support an environment that strangles current upstarts while they are still in the cradle, thus preventing future competition. If this is doubted, think back to how many large public companies actually supported Sarbanes-Oxley given the knowledge that the law's draconian accounting rules would keep many companies from floating shares altogether.

An environment meant to keep out the upstarts would be characterized by higher capital gains tax rates, more restrictions on trade and capital inflows, higher marginal income tax rates, mandatory health insurance, and greater regulation of products, lending, leverage and the environment. These are all changes that protect the established firms from upstarts eager to take their place at the top of the pyramid.

It is clear that we already have a great deal of socialism here in the United States. And we certainly *did* socialize some of the housing market with the passage of the 1978 Community Reinvestment Act (CRA), which forced lenders to make non-economic loans that would never have passed muster in a truly free market. The CRA's failure revealed that lenders would

have not made many of these loans on their own, yet despite the negative outcome, yesterday's elections show that the electorate wants more of the same.

The political question we must ask now is, "Do we really want more or less socialism?" Do we want the government to continue to tell lenders how they must lend now that "they" have, as Barney Frank said last Friday, "our money?" Do we want the power in the hands of a Congress with a 20% approval rating, a rating somehow lower than even President Bush's?

If so, there will be consequences to this apparent yearning for more socialism. That is so because tighter regulation, greater government control over the economy, socialization of losses, and more public influence over private decisions will create winners and losers.

The winners in the private sector will be those with influence in Washington, and who support the "enlightened" wisdom of those elected. The losers in this battle for influence are sadly tomorrow's innovators and upstarts, the very unborn companies that presently have no stock market index or influence in Washington.

It is interesting to note that the socialist politicians of Western Europe in modern times, as well as the nationalist, socialist and fascist leaders in the middle part of the century were all put into power by substantial, popular majorities. The powerful winners of today by definition have more political influence than those companies interested in taking their place.

In the end, it is a certainty that a highly regulated economy is far more orderly, while an entrepreneurial, regulation-free economy is far more erratic. But rather than blanch, we should embrace the latter because it is thanks to the "spontaneous order" wrought by free economies that great companies are born.

So while there are those who might deserve punishment for their roles in this financial crisis, the question we must ask is, "Punishment at what cost?" Should the expense be so great that the U.S. and the world miss out on the next Google, Apple, or Microsoft? We think not. In that case, the price of a resurgent state would be way too high.

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