ALAN GREENSPAN DID NOT SPEAK LIGHTLY

BY ALVERY A. BARTLETT JR.
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It is my personal view that Alan Greenspan's speech will be considered one of the most significant in the history of the Federal Reserve. It clear to me that he was saying that the asset valuation of stocks had gone too high. He implied that the Federal Reserve may have to raise rates to prick the stock market bubble before it is too late (reference Japanese real estate. and stocks of a few years ago). Most commentaries have focused on the fact that commodity inflation numbers do not support-additional austerity. Wall Street is in denial! They are not hearing what the man clearly said. His entire speech, from the history of the Fed, to a discussion of its powers and responsibilities, was scripted for justifying possible action. His issue was not inflation; it was runaway liquid asset valuation. Former Chairman of the Federal Reserve, William McChesney Martin, once said something to the effect that it was the Fed's role to take away the punch bowl when the party got too frothy. Maybe this is one of those times.

Enclosed is a quote that Mike Oliver sent me from Alan Greenspan's chapter "Gold and Economic Freedom" and Ayn Rand's "Capitalism: The Unknown Ideal", pp. 92-93 in the first hardcover edition, 1967. Reprinted from article in The Objectivist (July, 1966).

> "When business in the United States underwent a mild contraction in 1927, the Federal Reserve created more paper reserves in the hope of forestalling any possible bank reserve shortage. More disastrous, however, was the Federal Reserve's attempt to assist Great Britain who had been losing gold to us because the Bank Of England refused to allow interest rates to rise when the market forces dictated (it was politically unpalatable). The reasoning of the authorities involved was as follows: if the Federal Reserve pumped excessive paper reserves into American banks, interest rates in the United States would fall to a level comparable with those in Great Britain: this would act to stop Britain's gold loss and avoid the political embarrassment of having to raise interest rates"
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> "The Fed succeeded: it stopped the gold loss, but it nearly destroyed the economies of the world, in the process. The excess credit which the Fed pumped into the economy spilled over into the stock market - triggering a fantastic speculative boom. Belatedly, Federal Reserve officials attempted to sop up the excess reserves and finally succeeded in braking the boom. But it was too late: by 1929 the speculative imbalances had become so overwhelming that the attempt precipitated a sharp retrenching and a consequent demoralizing of business confidence. As a result, the American economy collapsed..."

On November 9, 1996, I wrote to you that "If Mike's (Oliver) "Outcome One" prediction proves correct, we should see an important and lower risk buying opportunity at substantially more attractive levels by the end - the first quarter of 1997." Since that time the market moved higher than "Outcome One" would have suggested but not as high as the market would have to have gone to support an "Outcome Two" conclusion. For the moment, I am still placing my stock and bond bet for the lower prices of "Outcome One".