GRANT'S
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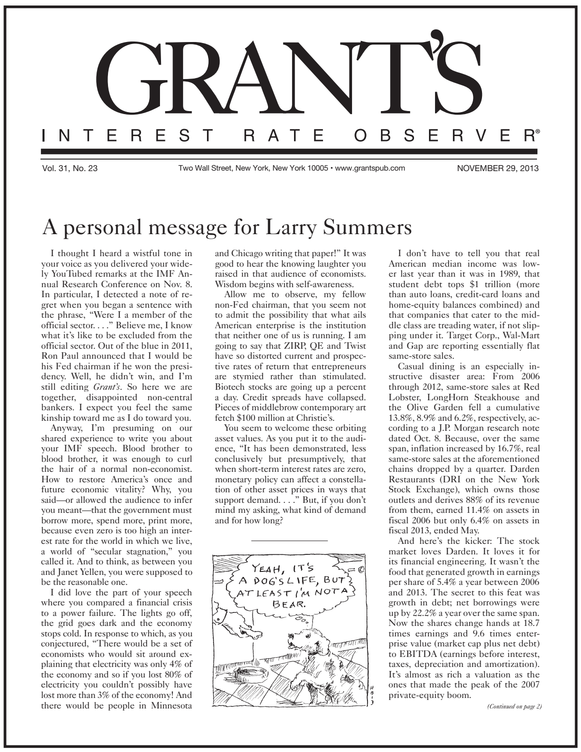

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INTEREST RATE OBSERVER®

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A personal message for Larry Summers

I thought I heard a wistful tone in your voice as you delivered your widely YouTubed remarks at the IMF Annual Research Conference on Nov. 8. In particular, I detected a note of regret when you began a sentence with the phrase, "Were I a member of the official sector. . . ." Believe me, I know what it's like to be excluded from the official sector. Out of the blue in 2011, Ron Paul announced that I would be his Fed chairman if he won the presidency. Well, he didn't win, and I'm still editing *Grant's*. So here we are together, disappointed non-central bankers. I expect you feel the same kinship toward me as I do toward you.

Anyway, I'm presuming on our shared experience to write you about your IMF speech. Blood brother to blood brother, it was enough to curl the hair of a normal non-economist. How to restore America's once and future economic vitality? Why, you said—or allowed the audience to infer you meant—that the government must borrow more, spend more, print more, because even zero is too high an interest rate for the world in which we live, a world of "secular stagnation," you called it. And to think, as between you and Janet Yellen, you were supposed to be the reasonable one.

I did love the part of your speech where you compared a financial crisis to a power failure. The lights go off, the grid goes dark and the economy stops cold. In response to which, as you conjectured, "There would be a set of economists who would sit around explaining that electricity was only 4% of the economy and so if you lost 80% of electricity you couldn't possibly have lost more than 3% of the economy! And there would be people in Minnesota and Chicago writing that paper!" It was good to hear the knowing laughter you raised in that audience of economists. Wisdom begins with self-awareness.

Allow me to observe, my fellow non-Fed chairman, that you seem not to admit the possibility that what ails American enterprise is the institution that neither one of us is running. I am going to say that ZIRP, QE and Twist have so distorted current and prospective rates of return that entrepreneurs are stymied rather than stimulated. Biotech stocks are going up a percent a day. Credit spreads have collapsed. Pieces of middlebrow contemporary art fetch $100 million at Christie's.

You seem to welcome these orbiting asset values. As you put it to the audience, "It has been demonstrated, less conclusively but presumptively, that when short-term interest rates are zero, monetary policy can affect a constellation of other asset prices in ways that support demand. . . ." But, if you don't mind my asking, what kind of demand and for how long?

I don't have to tell you that real American median income was lower last year than it was in 1989, that student debt tops $1 trillion (more than auto loans, credit-card loans and home-equity balances combined) and that companies that cater to the middle class are treading water, if not slipping under it. Target Corp., Wal-Mart and Gap are reporting essentially flat same-store sales.

Casual dining is an especially instructive disaster area: From 2006 through 2012, same-store sales at Red Lobster, LongHorn Steakhouse and the Olive Garden fell a cumulative 13.8%, 8.9% and 6.2%, respectively, according to a J.P. Morgan research note dated Oct. 8. Because, over the same span, inflation increased by 16.7%, real same-store sales at the aforementioned chains dropped by a quarter. Darden Restaurants (DRI on the New York Stock Exchange), which owns those outlets and derives 88% of its revenue from them, earned 11.4% on assets in fiscal 2006 but only 6.4% on assets in fiscal 2013, ended May.

And here's the kicker: The stock market loves Darden. It loves it for its financial engineering. It wasn't the food that generated growth in earnings per share of 5.4% a year between 2006 and 2013. The secret to this feat was growth in debt; net borrowings were up by 22.2% a year over the same span. Now the shares change hands at 18.7 times earnings and 9.6 times enterprise value (market cap plus net debt) to EBITDA (earnings before interest, taxes, depreciation and amortization). It's almost as rich a valuation as the ones that made the peak of the 2007 private-equity boom.

(Continued on page 2)

Grant's Interest Rate Observer

is an independent, value-oriented and contrary-minded journal of the financial markets. We publish 24 times a year. Our mission is to identify investment opportunities in a range of markets at both extremes of valuation, high and low alike. A typical 12-page issue is likely to contain a long idea, a short idea, a macroeconomic comment and a monetary or credit analysis (and, of course, one of our famous cartoons). Without bragging, we like to think that we are the financial-information medium that *least* resembles CNBC.

GRANT'S ON THE WEB

Grantspub.com delivers the current issue of ***Grant's Interest Rate Observer***, an issue archive, background information, cartoon treasury and publication schedules. **Grantspub.com** posts the most current issue of ***GIRO*** on the Wednesday before the Friday of its cover date. Complete issues and individual articles are posted in PDF and FLASH formats and can be read using Adobe Acrobat Reader and the Flash player and plugin.

Anyone can search the archive, buy individual issues, browse the Cartoon Treasury and read about past **Grant's Conferences**. Only current paid-up subscribers can access the latest issue and search the archives (which go back to 1983) at no additional fee. To use the site, one simply needs to register.

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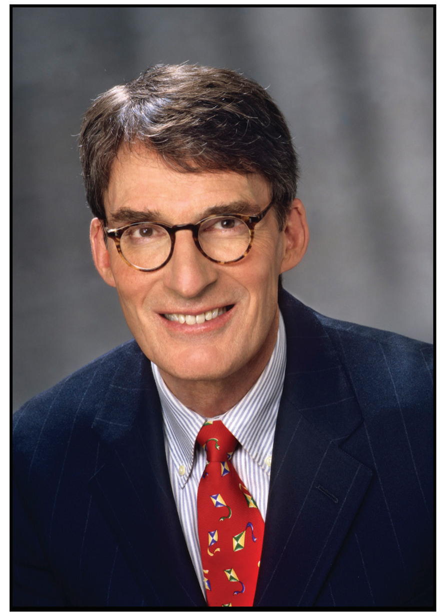
ABOUT THE EDITOR

JAMES GRANT



James Grant, financial journalist and historian, is the founder and editor of *Grant's Interest Rate Observer*, a twice-monthly journal of the investment markets. His latest book, *The Forgotten Depression, 1921: the Crash that Cured Itself*, a history of America's last governmentally unmedicated business-cycle downturn, won the 2015 Hayek Prize of the Manhattan Institute for Policy Research.

Among his other books on finance and financial history are *Bernard M. Baruch: The Adventures of a Wall Street Legend* (Simon & Schuster, 1983), *Money of the Mind* (Farrar, Straus & Giroux, 1992), *Minding Mr. Market* (Farrar, Straus, 1993), *The Trouble with Prosperity* (Times Books, 1996), and *Mr. Market Miscalculates* (Axios Press, 2008).

He is, in addition, the author of a pair of political biographies: *John Adams: Party of One*, a life of the second president of the United States (Farrar, Straus, 2005) and *Mr. Speaker! The Life and Times of Thomas B. Reed, the Man Who Broke the Filibuster* (Simon & Schuster, 2011).

Mr. Grant's television appearances include "60 Minutes," "The Charlie Rose Show," "CBS Evening News," and a 10-year stint on "Wall Street Week". His journalism has appeared in a variety of periodicals, including the *Financial Times*, *The Wall Street Journal* and *Foreign Affair*. He contributed an essay to the Sixth Edition of Graham and Dodd's *Security Analysis* (McGraw-Hill, 2009).

Mr. Grant, a former Navy gunner's mate, is a Phi Beta Kappa alumnus of Indiana University. He earned a master's degree in international relations from Columbia University and began his career in journalism in 1972, at the *Baltimore Sun*. He joined the staff of *Barron's* in 1975 where he originated the "Current Yield" column. He is a trustee of the New York Historical Society. He and his wife, Patricia Kavanagh M.D., live in Brooklyn. They are the parents of four grown children.

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2016 PUBLISHING CALENDAR

Issue Dates

January 15 • January 29 • February 12 • February 26

March 11 • March 25 • April 8 • April 22

May 6 • May 20 • June 3 • June 17

July 1 • July 15 • July 29 • August 12

September 16 • September 30 • October 14 • October 28

November 11 • November 25 • December 9 • December 23

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