Money: How the Destruction of the Dollar Threatens the Global Economy-and What We Can Do al
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Financial Analysts Journal; Nov/Dec 2014; 70, 6; ProQuest Central
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***Money: How the Destruction of the Dollar Threatens the Global Economy—and What We Can Do about It.* 2014. By Steve Forbes and Elizabeth Ames. McGraw-Hill Education, www.mhprofessional.com. 272 pages, $28.00.**

Reviewed by Martin S. Fridson, CFA

A study by researchers from Rutgers University, the University of California, Berkeley, and the World Bank found that financial crises have been twice as frequent since 1973 as in the period that includes the classical gold standard (1870–1914) and the Bretton Woods agreement (1944–1971), which mandated fixed exchange rates.[1] As bleak as that finding is, it was not until 2008, seven years after the study was published, that the most severe crisis of the floating-exchange-rate era began.

To Steve Forbes, chairman and editor in chief of Forbes Media, and co-author Elizabeth Ames, the solution is a return to stable currencies. Continuing to manipulate the money supply to stimulate growth, they maintain, will produce an endless cycle of subpar economic performance, misallocation of resources, and inflation. In their view, a new gold standard must ultimately emerge.

The authors of *Money: How the Destruction of the Dollar Threatens the Global Economy—and What We Can Do about It* see fatal fallacies in the prevailing wisdom that nations must preserve exchange-rate flexibility to maintain positive trade balances, which, in turn, are regarded as essential to combating unemployment. The United States has prospered over the long run, they point out, despite incurring trade deficits in 350 of the past 400 years. Achieving a trade surplus was not much of a benefit during the Great Depression, nor did chronic trade deficits prevent the US economy from booming during the 1990s. Forbes and Ames cite a finding by Dan Griswold of the Cato Institute that the United States has grown faster in years of increasing trade deficits than at other times.

What about the belief that currency manipulation is a necessary defense against countries that refuse to abide by free trade principles? Forbes and Ames note that the United States enjoys a trade surplus with protectionist Brazil and runs deficits with Canada and Mexico, its partners in the North American Free Trade Agreement. The US trade deficit with Japan has persisted even as the yen has appreciated from 300 to the dollar in the 1970s to as little as 80 to the dollar in 2012.

Specifically, Forbes and Ames endorse a new version of the gold standard embodied in a bill introduced by Ted Poe, a Republican congressman from Texas. The authors are well aware of the challenges to a system linking exchange rates to the yellow metal. In particular, they discuss the Triffin Dilemma, which many economists regard as a fatal flaw in the Bretton Woods system.[2] Forbes and Ames, in contrast, blame the fixed-exchange-rate system's breakdown on President Lyndon Johnson's excessive spending on social programs and the Vietnam War, coupled with massive dollar creation by the US Federal Reserve, under pressure from the Johnson administration. President Richard Nixon and his advisers, in the authors' view, wrongly perceived the problem as a merchandise trade shortfall, leading to the mistaken conclusion that the dollar had to be devalued.

Money is an ambitious attempt to tie many economic, social, and political problems to a single theme. According to the authors, consequences of the debased dollar include class antagonism, Middle East unrest, sovereign debt crises, corruption, rigging of the London Interbank Offered Rate, student loan repayment problems, and rising crime rates. Space permits Forbes and Ames to only sketch these connections, but their ideas may spur useful studies by researchers interested in the collateral damage inflicted by volatile exchange rates.

It is hardly surprising that so wide ranging a book contains a few factual errors. For one thing, the authors identify Charles Ellis as a successful money manager. Ellis's well-justified renown in the investment world is due to his writing and to his founding of Greenwich Associates, a provider of market intelligence to financial institutions. In addition, the authors state that economics was dubbed "the dismal science" in reference to Thomas Malthus's erroneous prediction that population growth would lead to mass famine. In reality, Thomas Carlyle coined the phrase as a comment on such economists as John Stuart Mill, whose support for the abolition of slavery he deplored.[3]

Notwithstanding these minor flaws, *Money* is a provocative book that sheds light on recurring—and potentially worsening—financial crises. Whether or not readers ultimately accept the book's proposed solution, they must reexamine their assumptions in light of the authors' critique of the received wisdom. Forbes and Ames are passionate yet reasonable, avoiding the zealotry of "gold bugs," who tend to discredit the cause of sound money. The authors point out that the Dow Jones Industrial Average gained 1,400% between August 1982 and February 2000 while gold went nowhere. They conclude that "gold is not an investment unless you're in the jewelry business."

—M.S.F.

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Notes

1. Michael Bordo, Barry Eichengreen, Daniela Klingebiel, and Maria Soledad Martinez-Peria, "Is the Crisis Problem Growing More Severe?," *Economic Policy*, vol. 16, no. 32 (April 2001):53–82.
2. Economist Robert Triffin theorized that the Bretton Woods arrangement would seal its own doom by creating a huge demand for dollars around the world. On the one hand, he maintained, if the United States tried to rein in the money supply, tight money would choke off economic growth. On the other hand, if the United States provided enough dollars to meet the demand, doing so would undermine confidence in the currency.
3. David M. Levy and Sandra J. Peart, "The Secret History of the Dismal Science, Part I: Economics, Religion and Race in the 19th Century," *Library of Economics and Liberty* (22 January 2001): www.econlib.org/library/Columns/LevyPeartdismal.html. The reviewer thanks Gene Epstein for his assistance on this item.

***Performance Evaluation and Attribution of Security Portfolios*. 2012. By Bernd R. Fischer and Russ Wermers. Academic Press (Elsevier), www.elsevier.com. 728 pages, $149.95.**

Reviewed by Kishor Bagri, CFA

In the current environment of dwindling excess returns (alpha), Bernd R. Fischer and Russ Wermers give readers the necessary tools to tackle and overcome the challenges of adding value through the efforts of active managers. This well-detailed volume establishes an excellent framework for manager evaluation and selection by delving into portfolios and analyzing them with meticulous methodologies. At the same time, the authors highlight pitfalls and traps to avoid.

They begin with basic concepts of performance evaluation and a discussion of models for valuing traded financial securities, including the capital asset pricing model (CAPM). The importance of the CAPM is balanced with criticism of its impracticality in the real world, which is due to unrealistic assumptions. Fischer and Wermers then move on to the contemporary, "empirically inspired" multifactor model.

The authors explain that two analyses form the basis of manager evaluation: return-based analysis and holding-based analysis.

Numerous return-based metrics are used to evaluate portfolios across asset classes. Fischer and Wermers highlight two nonregression approaches (the Sharpe ratio and tracking error) and two regression-based approaches (Jensen's alpha and the Treynor ratio). These measures rank managers in an effort to identify those with genuine skill. To inculcate a firm understanding of the concepts, the authors apply these techniques to several well-known funds across a variety of asset classes, including Fidelity Magellan, Legg Mason Value Trust, Janus Twenty, Vanguard 500 Index, and PIMCO Total Return.

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In their discussion of the analysis of portfolio holdings, the authors apply the Grinblatt–Titman methodology (GT) to the Janus Twenty Fund's stock positions with a lag of 12 months. This measure has statistical advantages over others, such as the Brinson–Hood–Beebower approach (BHB), because it does not rely on using a market index as a benchmark. Many portfolios have suboptimal benchmarks because available indices do not match their styles: Their product mandates involve niche or differentiated strategies, and the universe of stocks they invest in is different from the universe of stocks in the benchmark. Hence, GT is a better approach because it examines the holdings of the portfolio with a lag. For instance, a portfolio that invests in small-cap stocks will have the same style over time; using GT, one can calculate its performance measures on the basis of its historical holdings rather than its benchmark. Further, GT can be integrated into BHB to conduct performance attribution. In addition, the authors discuss the DGTW (Daniel, Grinblatt, Titman, and Wermers) measures—characteristic selectivity (CS), characteristic timing (CT), and average style (AS)—in detail. They argue that the DGTW measures are superior to factor-based regression approaches owing to a smaller standard error for CS and a more precise measure of the return attributable to AS. As a further benefit, the DGTW measures integrate the return-based approach to performance evaluation with the holding-based approach.

Fischer and Wermers also discuss the "bootstrap approach" to computing the statistical significance of a fund manager's estimated performance. Useful in evaluating short-term persistence, this analysis shows more funds having significant alphas than the standard t-test does.

If there is one chapter that defines the book, it is Chapter 9—"Does Active Management Add Value?"—in which the authors guide investors to find superior active managers, or SAMs, in "mostly efficient" markets using a combination of four approaches: past fund performance, macroeconomic correlations, fund characteristics, and analysis of fund holdings. The chapter summarizes findings

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