



# ECONOMICS COMMENTATOR

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## SOLSTICE SURGE

by  
John A. Sondey  
Professor, Economics

Nearly 70% of what the United States produces is intangible; without shape, color, dimension – essentially invisible, but with a value of nearly 10 trillion dollars annually. In Gross Domestic Product parlance, this massive chunk is termed “services” which includes financial, education, medical, and legal services and just plain information. New and old media bracket us in an endless shelling to the extent that many of us suffer from informational overloads. In this state we process only that information that is essential to us, and do not drill down too far in our analysis of what is presented on a multi-media platter. We tend to be selective in the information we receive; moreover, we lock onto information that agrees with our point of view. Thus, while the informational revolution has made virtually every aspect of life more transparent, from politics to investment, its sheer volume has made everyone more selective in receipt and perhaps more biased and extreme in their responses.

The subprime-housing-financial crisis (SHFC) and media-overload have a symbiotic relationship; each drawing strength from the other. SHFC serves up human interest and pathos to the media who, crafting the sound bites and photo ops, tailor it to their particular market. In turn, consumers become immersed in information, and, as the message repeats itself, are convinced that at least some part of the sky is falling – and act accordingly. Hence, the drum-beat of gloomy information about economic prospects becomes the classic self-fulfilling prophecy as consumers postpone major purchases and throttle back on spending in general. The economic wheels slow.

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## THE POLISH-AMERICAN EXTENSION PROJECT

by  
Gerald W. Warmann  
Professor, Economics/Ext. Specialist

Between 1991 and 1994 a joint effort between the Polish Ministry of Agriculture and the United States Department of Agriculture was organized to modernize the Polish farm advisory service. USDA recruited teams of Extension workers—production specialists and agents, agricultural economists, home economists and Extension administrators—to serve in their professional capacities as advisors for six month periods. Teams of two US Extension professionals were assigned to farm advisory service offices and asked to assess local needs and to design a professional training program for the farm advisory service staff and their administrators. The project had various objectives but most of them centered around preparing the farm advisors to provide appropriate training programs for Polish farmers so that farmers could succeed in the developing market economy of Poland.

Polish agriculture had operated under a planned system under Communism. There were many Polish cooperatives or agricultural collectives which produced food for Poland and other Bloc consumers. Surprisingly, individual ownership of land persisted throughout the post war era and through independence from the USSR in 1989, and private land ownership is a source of pride for Polish agriculture today. Freed from operation under a production plan, Polish farmers needed assistance in free market decision making. The Polish American Extension Project was designed to train a cadre of farm advisors who could explain and teach decision making under the uncertainties of the free market.

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In October 2008, consumer purchases fell by 1%, housing prices – per the Case-Schiller index - declined 16% from a year previous, the stock market plunged to 2003 levels, new jobless claims soared to a 15 year high, and the unemployment rate rose to 6.7%. In many ways, October was the perfect storm, a confluence of negative forces so strong that some economic warriors spoke of a post-capitalism aftermath.

The stock market proved the focal point of the current crisis. Its profile rose as its prices fell. On November 21, 2008, the Dow Jones Industrial Average (DJIA) had fallen 43% from its October 2007 high of 14,164, making it the worst bear market since the 1929-1932 crash, when the stock market lost more than 80% of its value. Moreover, with the new millennium, bear markets had become global in nature, with representative indices for Europe and Asia down 50%, year to date.

Yet, as the winter solstice approaches, there are some signs of hope for the stock market. And, as a leading economic indicator (first into a slump, first out) a resurgent market just might prove the locomotive to give the economy some pull. Since 1903, there have been 13 bear markets where stocks have fallen by 20% or more, but only two where the decline amounted to 50% or more of value, 1929-33 and 1937. *Barron's* notes that the time of full recovery from bear markets, the 1929-33 crash excepted, was 22 months on average, while the tenure of the average bear was 14 months. There are no guarantees that history will repeat itself, but short of a full-fledged depression, the statistics provide hope that recovery may commence shortly and substantially.

Some might reason that with the DJIA at its all time high of over 14,000 just a year ago, the market showed symptoms of an overvalued bubble, with other key statistics such as price/earnings ratio, providing corroboration. If so, that is no longer the case - the air is out of the balloon. At the 2000 peak, stock market valuation was twice that of GDP. At the 2007 peak, market capitalization stood at a slightly higher level than GDP, about 120%. Today, the market is only 59% the size of the economy, well down from its long run average of 79%. In fact, the stock market is so thoroughly underperforming

average performance benchmarks that a simple reversion to the mean would erase at least two-thirds of the current plunge.

According to traditional stock market theory, stock prices are very quick in absorbing new information and current prices are a true reflection of stocks' *intrinsic* (real) worth; therefore, investors cannot profit from any new or old information – it is already priced into the stock. The theory is termed the Efficient Market Hypothesis (EMH), as crafted by Eugene Fama in the 1950's and it remains a cornerstone of financial theory. The theory concludes that abnormal (beating the market) returns cannot be earned even through the most diligent study of financials. Investors must settle for a normal return – and their ability to consistently “beat the market” is nonexistent. EMH proposes that investors are rational and will act and react in a rational manner – in essence, the stock market is a well-ordered venue.

John Maynard Keynes (d. 1946) would have disagreed with much of EMH, particularly regarding the rationality of investors and the orderly transition of prices. Keynes, who lost and regained a fortune on the London exchange, would claim that “animal spirits” roam the financial markets, roiling them often and unexpectedly. Keynes would add that the animal spirits are necessary in breaking inertia-generated equilibria to create new investment opportunities. A later school of thought, behavioral finance, would come to agree with Keynes that market activity is not a well-choreographed event but something more chaotic and unpredictable. The unpredictability or caprice of the market reflected the less-than-rational approach to the market by investors. Investor emotion, psyche, and bias all acted to move markets. A linchpin of behavioral finance is momentum investing; where investors pile into a stock or sector, with no heed of analytical fundamentals, simply because everyone else is doing it. This herd behavior can be seen in the current market downturn as investors flee stocks with the alacrity evidenced 14 months ago when they pushed the DJIA to a record high. Of course, the effects of the thundering herd are compounded by extremes in short-selling and gyrations of heavily-leveraged hedge funds, well-evidenced by

the volatility of stocks in the last half-hour of trading. Some financial economists would argue that because of momentum (herd) investing, stocks are *always* either under-priced or overpriced relative to intrinsic value.

It is proposed that momentum investing (and disinvesting), spurred by blanket, multi-media coverage, has helped drive the bear market. As a result, there are immense sums sitting on the sidelines, awaiting a resurgence in positive investor sentiment. Call it a solstice surge.

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(The Polish-American ... Cont'd from p. 1)

As one of the team members serving in Poland in 1992, my personal work was quite similar to my US Extension assignment in Kansas. My business card noted my expertise as an economic advisor and my efforts focused on teaching my Polish counterparts the basics of the development of a business plan. All of the Project team members had experience in Extension at county, regional, or state level work. We all were asked to speak to many stakeholder groups in Poland to explain the US system of land grant universities and the particular structures of Extension under which we worked. Polish advisors had developed working relationships with producer groups, but they often had sideline commercial interests which could have interfered with their ability to provide unbiased, research based information to their stakeholder groups.

In the US land grant university system there is a direct linkage between the three mission areas of teaching, research and extension. Newly discovered information is plugged directly into the classroom and made available to public users of the new information. Information gaps, articulated by producers or citizens, are communicated back to researchers so that those questions can be evaluated in a scientific process with research results becoming new information available to the public. In Poland we found that there was significant separation between the research institutes, the universities and the farm advisory service and the stakeholder groups which need access to new information.

The US group of Extension professionals in Poland in 1992 organized a major agricultural conference for

professionals and administrators from the research institutes, the universities and the farm advisory service, and leadership from various stakeholder groups. Developing cooperation and communication between all of these groups was an objective of the conference. Since 1992, there have been periodic joint conferences of these groups and significantly increased stakeholder involvement in the program needs assessment process for the farm advisory service.

In 2007 and 2008 it was my good fortune to be able to return to Poland and to revisit several of the farm advisory service offices which I served in 1992. Contacts between US Extension professionals and Polish advisory service professionals kindled my interest in assessing whether the effort of 1992 would have an impact upon how the Polish farm advisory service functions today. Please permit me to relate my observations informally.

In returning to Poland in 2007 and 2008 I traveled with a group of faculty and students with different educational objectives than mine. My Polish hosts of 1992 were happy to welcome my return to Poland and were very gratified that I retained professional interests in their work. Visiting in five of the advisory service offices as well as the central regional administrative office gave me the opportunity to talk with old friends and new advisors, all of whom are working closely with individual farmers in developing marketing and financial plans for their farm operations. Poland has joined the European Union, and the farmers benefit from the EU support programs for agricultural production, particularly quality improvements of processed products which have a ready market throughout Europe. Producers must file operation plans or business plans in order to qualify for these programs and to set the level of support. Thus, I could observe that the business planning which we taught in 1992 was directly being used every day in the Polish farm advisory service offices.

When I asked about the stakeholder groups, my Polish counterparts assured me that they valued stakeholder input highly. Programs are developed which address local needs. Major programs have been developed to help Polish farmers and

entrepreneurs serve a growing customer base for agro-tourism and rural hospitality services. Stakeholders have formed numerous tourism development associations which promote and stimulate economic activity in the region.

University professors meet regularly with research institute scientists and farm advisory service professionals to continue the communication and cooperation begun at the 1992 conference. The modest USDA and Polish Ministry of Agriculture project continues to provide a foundation for stakeholder educational programs, researchable issues

and university curriculum benefiting agriculture and economic development activity throughout Poland.

My interests in Poland continue—mainly in local food production, in direct marketing and in the emerging agro-tourism and rural hospitality opportunity areas. Future contact with Polish colleagues will help me bring valuable lessons back to the US.

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Economics Department  
South Dakota State University  
Box 504 Scobey Hall  
Brookings, SD 57007-0895  
Phone: 605-688-4141  
Fax: 605-688-6386  
E-Mail: Penny\_Stover@sdstate.edu  
325 copies of this newsletter were produced at a cost of less than \$100