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## Do tulips grow in cyberspace ?

Over the past few months, much has been printed about manias, from tulips to the internet. What's going on ? We thought we might add our bit, for what it's worth. We have in parts summarised one or two books on the subject, or taken at times a direct quote, as highlighted. This Indicator is the first in a series over the next month dealing with manias. Here is the first instalment.

It is in our view not quite correct to compare the current market mania for internet stocks with some of the past investment manias. This discussion is not to put a negative view on current events, but merely to consider what may be happening at present with net stocks, and how this internet investment (mania ?) may continue to unfold.

### Tulips, Holland, 1634.

Europe first sighted the tulip in the 1550's. The bulbs originated from Constantinople, the word tulip being, it is believed, from a Turkish word meaning turban. From the 1560's on, tulips became much sought after by the wealthy, particularly in Holland and parts of Germany, until eventually, as reported in Charles Mackay's *Extraordinary popular delusions and the madness of crowds*, "it was deemed proof of bad taste in any man of fortune to be without a collection of them". Few flowers could produce as many variegated colours as the tulip.

To supply the wealthy with the finest and very best tulips, a whole industry grew up of merchants, shippers, shop keepers and traders. Intense competition developed to find better colours, and more variegated varieties. It was not long afterwards that similar passions took over the middle classes, and demand really started to affect prices.

By 1634, the Dutch desire to have tulips took on a passion that was so great, the "ordinary industry of the country was neglected." (Mackay, p 90) By 1636, regular markets for tulip sales had been established on the stock exchanges of Amsterdam, Rotterdam, Harlaem, and other smaller centres. Gamblers and speculators quickly cottoned on to every means possible to bring about fluctuations in tulip prices. A

few individuals grew suddenly rich. Speculation in bulbs really got underway in September of 1636, when all the bulbs previously available for examination had been planted for blooming the following spring.

Charles Mackay described the speculation this way; "A golden bait hung temptingly out before the people, and one after the other, they rushed to their tulip-marts, like flies around a honey pot. Everyone imagined that the passion for tulips would last forever, and that the wealthy from every part of the world would send money to Holland, and pay whatever prices were asked for them. The riches of Europe would be concentrated on the shores of the Zuyder Zee, and poverty banished from the favoured climate of Holland. Nobles, citizens, farmers, mechanics, seamen, footmen, maidservants, even chimney sweeps and old clotheswomen, dabbled in Tulips. People of all grades converted all their property into cash, and invested it in flowers. Houses and land were offered for sale at ruinously low prices, or assigned in payment of bargains made in the Tulip-mart. Foreigners became smitten with the same frenzy, and money poured into Holland from all directions. The prices of the necessaries of life rose again by degrees: houses and lands, horses and carriages, and luxuries of every sort, rose in value with them, and for some months Holland seemed the very antechamber of Plutus."

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"There is nothing so disturbing to one's well being and judgment as to see a friend get rich."

James B Stewart, Den of Thieves

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History does not seem to record what event took place to shake the

confidence of tulip investors; perhaps it was that the more prudent could see activities could not last forever. As described, it appears that confidence began to wane, turning quickly to fear. Tulip prices fell rapidly in late 1636, turning fear to panic. When the music stopped, many found themselves in possession of more than a few tulip bulbs that absolutely no one wanted.

### The South Sea Bubble, 1711 through 1720.

In the early 1700's, England found itself heavily in debt; previous wars had been expensive, so too the mishandling of the economy by the then administration. £10 million sterling was owed by the government.

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With the view to restoring public credit, and pay off the national debt, the South Sea Company was floated around 1711, by a number of well connected merchants. A deal was offered to the Government; the South Sea Company would take over the national debt, at the interest rate of 6%. To provide for the interest, (some six hundred thousand pounds per annum), the existing duties upon wines, vinegar, silks, tobacco, whale-fins and other similar articles were to be rendered permanent, and a monopoly of the trade of the South Seas was to be granted. It was this trade monopoly that created real interest.

The merchants could see a big deal here. Every one

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When the rest of the world are mad, we must imitate them in some measure.”

Carswell, The South Sea bubble, p 61, quoting from a certain banker, one Mr Martin, after subscribing £500 to South Sea stock.

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knew, it was common knowledge, of the newly discovered gold and silver mines of Peru and Mexico - beyond the south seas. Every one knew them to be inexhaustible. All the South Sea company had to do was send English products to Mexico, and be repaid “a hundredfold in gold and silver ingots by the natives.” The South Sea Company’s stock was offered to British investors, and from the profits of trading with the colonies, the company would pay off the national debt. A large rise in the company’s stock price was forecast.

Now we need to understand the era here. The formation of a company such as this was a fairly new, but growing development. It required royal / parliamentary ascent in fact. Competition and jealousy was rife. By 1717, when the South Sea Directors had laid before parliament their plan, the Bank of England, also wanting to be considered in the deal, hatched similar plans. The South Sea directors, not wishing to be outdone, revised their own plan. In this way, the company and its grand plans were constantly before the public eye. Exchange Alley, the share trading centre of London at the time, became over run with potential investors. The company’s stock went from 130 to 300 and continued to rise. Rumour after rumour was spread. Throughout late 1719, the stock went to 400, then settled at 330.

By 1720, Exchange Alley became had become blocked every day by crowds. Every body came to purchase stock, men discussing and meeting in taverns and coffee houses, the ladies could be found in milliners and haberdasheries. Quoting from Mackay once again:

“During the progress of this famous bubble, England presented a singular spectacle. The public mind was in a state of unwholesome fermentation. Men were no longer satisfied with the slow but sure profits of cautious industry. The hope of boundless wealth for the morrow made them heedless and extravagant for today.”

How to cash in on these developments ? Companies started up every where, enticing investors to buy their shares (and ideas). And despite protests from the government, many were floated regardless, such was the demand from the public.

Companies were floated, and shares offered to the investing public for all sorts of new ideas;

~ for the importation of Swedish iron

~ for the importation of Flanders lace

~ for the supply of the town of Deal with drinking water.

Other floats were a bit more outlandish; for a wheel of perpetual motion, another

for carrying on an undertaking of great advantage, but nobody to know what it is. The stock price on this one went wild.

It was noted, but only in hind sight, that the promoters of most schemes took the first opportunity of a rise to sell out.

In the typical tradition of English understatement, companies were given the name “bubbles”. A speculating frenzy was upon the nation. Every one was buying stocks. As more companies were floated, the crowds grew ever larger.

To give some idea of the frenzy, it is believed that two thirds of those receiving government annuities exchanged them for stock in the South Sea Company. The price of the stock just kept on rising.

History records that the price of English real estate was now moving with the South Sea company stock quotations.

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“Financial crises are associated with peaks in the business cycle.”  
Kindleberger; Manias Panics and Crashes, page 1

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By the end of May 1720, the general opinion being that the stock could go no higher, sellers began to outnumber buyers. So many sellers appeared in the Alley that the stock fell from 890 to 640. Isaac Newton, at the time Master of the Mint, was heard to say; “I can calculate the motion of heavenly bodies, but not the madness of people”, and then sold his

entire holding of South Sea stock at a 100% profit. (At the height of the bubble he went back in, and then proceeded to lose the lot.) The directors were alarmed and gave their agents orders to buy. This effectively kept the price for the next month at 750. Interestingly, in July of 1720, parliament passed the Bubble act; expressly forbidding the formation of further companies without explicit approval of Parliament. (The act lasted 136 years.) At first glance, this might have looked like an effort to stop the speculation. More likely it was to suppress rival bubbles.

With further work from the directors the price of the South Sea company rose to £1,000. The original issue price had been £2. It was now August, and talk was spreading that the chairman and others had sold out of their stock.

In this month the stock fell back to 700. A General Meeting was called. The Directors spoke of what a wonderful job all the other directors had done. Mackay records that the directors reminded the shareholders they had "extinguished all the domestic (troubles) and animosities of the nation. By the rise of their stock, monied men had vastly increased their fortunes; country gentlemen had seen the value of their lands doubled and trebled. They had at the same time done good to the church, not a few of the reverend clergy having got great sums by the project. In short, (the Directors) had enriched the whole nation, and he hoped they had not forgotten themselves."

But the same evening the stock fell to 640 then to 540, and continued to fall to 400 in following days. Directors could not appear in the streets without being insulted; dangerous riots were being continually put down. A general panic started, September 1720.

To try and stem the panic, the company issued bonds to raise further monies. So great was the turn out of people that it was thought that the £3,000,000 subscription would be filled on that day. But the stock price fell sharply after lunch and a run commenced upon the goldsmiths and bankers, some of whom had lent large sums against the value of South Sea shares. The stock fell to 150 at which time the Sword Blade bank previously chief bankers to the company, stopped payment.

The speculative rise, progress and then fall of the South Sea Company took 8 months over all, though it was some years in building. In the aftermath, the average stock in London went down some 98% in the two years thereafter. The stock exchange itself was shut down for the next half century, and the government enacted laws making it a crime to be a stock broker !!

It has been suggested that this left England chronically

short of money, eventually leading England to tax the wealth of the Americas.

### Can we compare these manias to today ?

The tulip mania was really an isolated incident, and should be seen in the background of the Dutch economy, which had been depressed during the 1620's when Holland had resumed its war with Spain, but recovered quickly in the 1630's. House prices surged in this decade also, as did shares in the Amsterdam chamber of the Dutch East India company.

Huge investments were underway in drainage schemes and canals, linking for the first time many Dutch towns and making the travel of merchants far more dependable and no longer reliant on wind and weather. Explosive growth was underway in the Dutch economy after 1630. A mania for clocks and clock towers was also in full swing.

This did not really affect the economy overall, though when new wealth is created, and yet more credit gets extended.....

The South Sea bubble was a swindle. Kindleberger in his book *Manias Panics and Crashes* had this to say: Very quickly, consolidation of British government debt overwhelmed the South Atlantic trade aspects of the enterprise, and stock-jobbing overwhelmed government debt shortly thereafter. John Blunt (a South Sea company Director) and his insiders deliberately sought to make profits on stock issued to themselves against loans secured by the stock itself, that is free. As capital gains were drawn off, they were converted into estates, for which Blunt had six contracts to buy at the time of the collapse, a man named Surman had four contracts to buy real estate on which he owed 100,000 pounds. In order to pay out profits, the South Sea Company needed both to raise more capital and to have the price of its stock moving continuously upward. And it needed both increases at an accelerating rate, as in a chain letter or a Ponzi scheme."

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An interesting observation was made by the writer of *The history of the Bank of England*, A Andreades, 1909, to the effect that "When (the) interest (rate) goes down, the English commercial world, unable to reduce its mode of life, deserts its usual business in favour of the more profitable, but on that very account more risky undertakings... speculation leads to disaster and ultimately must be borne by the central bank."

From a Kondratieff wave perspective this is interesting, since the introduction of new technology has a much more favourable climate when interest rates are low, and going lower.

Since the time of the tulips, and probably before, 'free market' economies have witnessed quite regular bouts of speculation, some of the larger years, and the item speculated in being;

1816 commodities, related to wars end, 1825 canals and cotton, related to declining interest rates, 1837 railways, 1847 railways, 1857 railways, 1866 cotton, shipping companies, 1873 railways especially in the US, 1890 Argentine bonds, Australian land (Barings bank collapses from illegal rogue trading activities saved only by a huge injection of gold from Paris), 1907 US stocks, 1919 commodities related to wars end, 1929 land then stocks;

and slightly less frequently after the 2nd World War in 1954, 1973/74, 1987, and 1990 in Japan, based always upon some commodity or other, and in this century most often in stocks.

It was after 1816 that each panic became more of a global affair. Some historians observed; the sober pace of eighteenth century business gave way to a democratic passion to get rich quick.

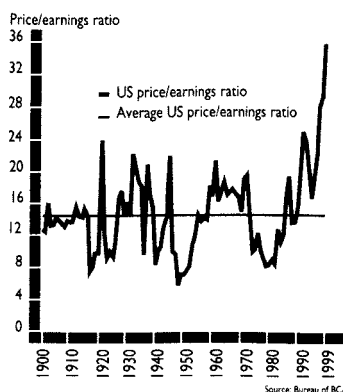
Of particular interest is the railway manias of the 1830's, 40's and 50's. Railroads wrought astounding changes on economies everywhere.

Railroads revolutionised business activity and trading as profoundly then, as the net will continue to do today. Rail dramatically sped up our communications ability. For example in the 19th century, all towns and cities kept their own local time. As rail travel sped up, this became very confusing and train timetables difficult to follow. Rail forced an international agreement to divide the world into 24 standard time zones along the meridians of longitude, with the world finally settling at Greenwich London as 0 degrees and international time zones relative to Greenwich mean time. We take these time zones for granted now, but it took until the year 1883 for general agreement to be reached.

During the rail's (new technologies) introduction and growth into maturity, the world witnessed 3, maybe 4 manias. They were part of, perhaps the cause of, each business cycle, built upon the development and movement of people, goods and information; 1845 to 1847 in particular being described by some historians as "an orgy of railway promotion".

We shall look at this in greater detail next issue in two weeks time.

Fig. 1 from BRW June 4 issue, (in case you missed it) speaks for itself.



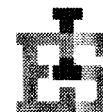
Inserted is a chart of the SPI (futures contract of the All Ordinaries Index) and hand notated comments you may find of interest.

As for the economy in general, its obvious the current position, you don't need us to tell you. Make hay whilst the sun shines, and bank your profits.

Interest rates;  
steady, further Reserve Bank induced interest rate rises extremely unlikely going into the Y2K / millennium change.

Inflation;  
our view is still for lower prices to come.

Property;  
the remarkable buoyancy looks set to continue as stock market profits are taken and put into something more tangible.



Cycles analyst: Phil Anderson  
Marketing and technical analyst: David Rasmus  
Options and futures analyst: Julie Palmer

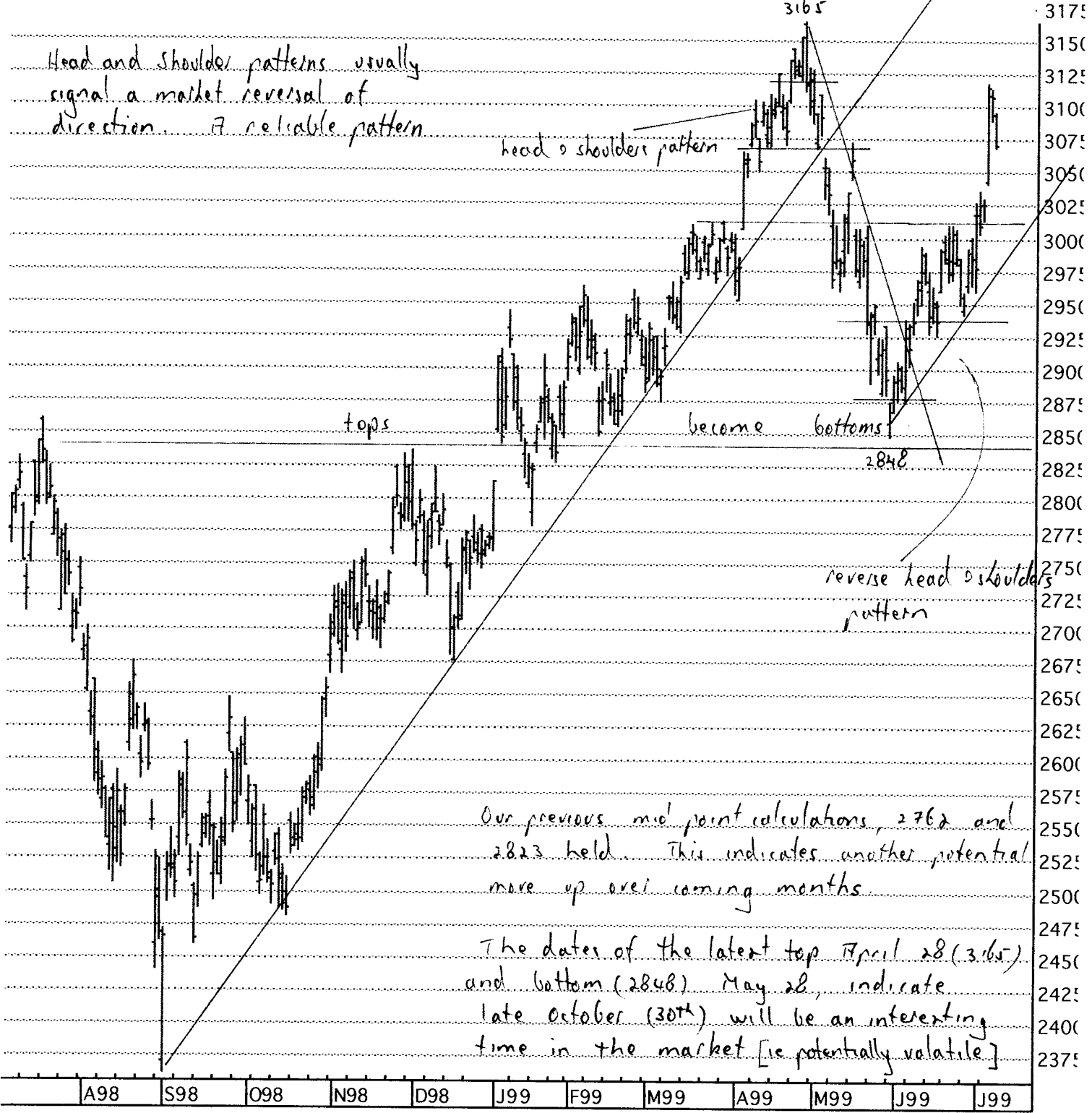
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 12 Month High 3165.00 12 Month Low 2360.00 Scale 1 inch = 105.58 Zoom Level 2

07/07/99 C/3071.00 -37.00 H/3096.00 L/3069.00 O/3094.00 MA0/4.37 MA0/4.43 MA0/4.38



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# King of the Bond castle no stranger to property plays

AFR July 2 1999

## Mark Drummond

West Australian businessman Mr Barry Patterson is developing an expensive habit of acquiring big-ticket properties from well-known identities in his home town of Perth.

In 1996, he paid \$5 million for Mrs Janet Holmes à Court's Peppermint Grove mansion, just because he fancied the 3,200sqm block it sat on.

When his demolition plans were scuppered by the local shire council, Mr Patterson wrote out a \$4.5 million cheque for a vacant block on the river's edge in Peppermint

Grove owned by Mrs Angela Roberts, the estranged wife of Multiplex Constructions chief Mr John Roberts.

On Wednesday, Mr Patterson set a new Perth residential record when his \$9.5 million tender for the mega-mansion Alan Bond built in Dalkeith was accepted by St George Bank.

That's all on top of the \$3.5 million mansion Mr Patterson and his wife actually live in in East Fremantle, which also overlooks the Swan River.

More than \$22 million of residential real estate might seem a lot for your average punter, especially given the

Bond mansion probably requires another million or so to finish the extensive renovation work carried out by its latest owner, troubled mining executive Mr Ross Atkins.

But then again, it's perhaps not all that much for someone sitting on a \$60 million paper fortune from two of the best performing stocks of fiscal 1999 - Silex Systems and Sonic Healthcare. That sharemarket fortune was built from an initial investment of less than \$1 million eight years ago.

The low-profile Mr Patterson is chairman of Silex and a director of Sonik, as well as a major shareholder

in both companies. He was also a co-founder of Kalgoorlie contracting group Eltin and a former director of Macmahon Holdings.

Despite setting a new Perth residential record, the mortgagee sale of the Bond mansion has left St George Bank facing a significant haircut on its \$18 million-plus exposure to Mr Atkins and his private companies.

Mr Atkins, who is facing bankruptcy proceedings, bought the mansion from Mr Bond for \$7.3 million in 1993 and used loans from St George Bank to fund a refurbishment costing more than \$10 million.

A continuing example of the transfer of stock gains into property