

JUST THROW MORE MONEY AT IT?

The new administration in Washington has it right. We need change. But change just for the sake of change can be dangerous. There are probably a million ways to change for the worse, but very few ways to change for the better. So what changes do we need? We haven't yet heard from the new administration. We breathlessly await the specifics. Today we hear references to the Great Depression of the 1930s. There's a body of opinion that blames that depression on a contraction of the money supply from late 1929 through early 1933. Given that premise the great fear today is deflation. At any price, don't allow the money supply to contract. Thus, we have government throwing money at our economy with abandon. Is this the change we need?

Prior to the 1930s our country went through several periods of money supply contraction without experiencing a depression; a brief period of financial panic yes, but no depression. In each case the root cause of the panic was not the result of monetary contraction but prior monetary inflation. Our panic of 1929-1930 was no different. The money contraction that took place during that period was a result of the fiat money inflation that took place from 1913 to 1929. Fiat money inflation was always followed by a financial panic when the public suddenly realized there wasn't enough gold in bank vaults to cover the inflated fiat money in circulation. The cause of the panic was always a run on the banks, attempting to exchange fiat money for "hard" money.

There are several good books available that make a strong case that our ten year depression was the result of government attempts to ameliorate the affects of a financial panic, not the panic itself.

In March of 1933 the Roosevelt administration took the country off the domestic gold standard leaving fiat money, backed by nothing but faith, as our medium of exchange. "Without gold as money there can be no deflation since the Fed can ensure no monetary contraction, and there's no basis for the intrinsic value of green paper. Surely we can live happily ever after without having to worry about deflation and its consequent panic."

Unfortunately, we retained gold as an international exchange standard as a means of enabling trade and promoting at least some sense harmony among nations, while continuing fiat money inflation. It worked pretty well until we realized we had exported too much green paper while simply printing replacement paper. In 1971 the Nixon administration acknowledged there was no way to exchange our exported green paper for gold; there simply wasn't enough gold in the world. Therefore, on Sunday, August 15th, he stunned the world by declaring we would no longer exchange dollars for gold at any price.

Money inflation is always the root cause of subsequent money deflation - the dreaded business cycle. Money inflation is the scourge of the ages, from clipping coins by the Romans, the Babylonians and the Egyptians, to the printing of money today - a mere computer entry. For ten thousand years governments attempted to wrest control of money away from the marketplace. In the twentieth century governments succeeded. The free market may not be able to eliminate market bubbles such as we've seen in recent years, but we can certainly minimize their effects by not funding them with inflated money. And we can minimize the effects by allowing correction to occur as rapidly as possible rather than attempting to ameliorate the effects and dragging the pain out over a period of years rather than months.

For several decades we've been a nation of over consumers aided and abetted by money inflation and debt. We've been unwilling to make the necessary choices to live within our means. We want it all now. Let the future take care of itself. Well, we've arrived at the future and we don't like it. It doesn't look good from our new perspective. The bills are now coming due and we're unwilling and/or unable to pay them.

Today government and the Fed are throwing everything available at our troubled economy in an attempt to rescind the bills and ameliorate the effects. Money inflation, debt and unfunded liabilities are growing at alarming and unsustainable rates. Unfortunately the saviors of last resort are themselves bankrupt. All governments, national, state and local, are either already bankrupt or on the verge of bankruptcy. There isn't a single government entity that can pay its debts or fund its liabilities.

Change is essential. But we need the right kind of change. What we most need is a drastic reduction in the cost of doing business and in the cost of doing government – at all levels. This can be done. It's feasible. It's practical. And it can be accomplished while retaining necessary controls over both business and government. And it can be accomplished while minimizing the pain to individuals. But in order to succeed we must have drastic simplification and vast improvements in visibility. Today's greatest needs are to completely overhaul our tax systems and to eliminate our reliance on public debt and unfunded liabilities. Included is money inflation, the cruelest of all taxes, as it is the most regressive of all taxes and hurts most those unable to protect themselves from its effects. The rich get richer, the poor get poorer and the middle class shrinks.

If health care is so important why do we tax it so heavily? If health insurance is so important why do we tax it so heavily? If education is so important why do we tax it so heavily? If food, clothing and shelter are so important why do we tax them so heavily? If the Detroit auto industry is so important to our economy why do we tax it so heavily? All these essential goods and services are burdened with egregious hidden, as well as visible taxes. Our compounding tax structure with its visible and hidden taxes imposes a burden equivalent of up to a 40% sales tax in each of these areas. Ironically governments, national, state and local, are the largest tax payers in the country. The greatest reduction we could make in the cost of doing business, the cost of doing government and the cost to the consumer, would be to eliminate all taxes on business and replace them with highly visible, highly efficient retail sales taxes at an appropriate rate much lower than we're now paying. Today we tax goods and services so heavily, we make them so expensive for consumers, that governments feel compelled to step in and either provide subsidies for those in need or, in some instances, to simply nationalize another segment of the economy and provide goods and services at "affordable" (subsidized) prices. Remember, only people pay taxes – both visible and hidden.

As to debt, we must wean governments, national, state and local, off debt financing. If we can't afford the price of needed public goods and services, we certainly can't afford twice the price. Debt financing simply doubles the price of government purchases. Businesses can afford to borrow if they're making a profit and they can increase their profit by borrowing. Governments don't operate on a profit basis, thus, there's nothing to gain by borrowing and much too lose.

Unfunded liabilities should be a no-no. They're a huge time bomb waiting to go off.

Today we're faced with another in a series of economic crises. We have an opportunity to make real change; change from the way we've been doing business for the past century. We have an opportunity to drastically simplify the cost of doing business and the cost of doing government. We have an opportunity to provide much needed visibility. We have an opportunity to sever our reliance on debt, to get on a truly pay-as-we-go basis. We have an opportunity to unburden future generations. We can maintain necessary regulation and control of both business and government. We can do all this while providing a much higher level of individual "freedom, liberty and justice for all" at greatly reduced cost.

Today we're fighting an economic crisis using the very methods that got us into the crisis; money inflation, debt, unfunded liabilities, unnecessary complexity and inadequate visibility. These methods are simply setting us up for a much greater financial crisis in the relatively near future as we switch from fighting deflation to fighting inflation, inevitable as a result of present money inflation. Increasing debt at a rate of a couple of trillion dollars per year and financing debt at the lowest interest rates in history, will prove disastrous when it comes time to fight inflation and we have to roll over enormous amounts of debt at much higher interest rates. Debt financing costs are already approaching a trillion dollars a year (excluding any principal repayment) and escalating rapidly. Now is the time for substantive, effectual change. There is no painless remedy. We will pay a price for decades of past indiscretions. The longer we delay the needed change, the greater will be the pain. The wrong change will be disastrous.

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