By Clive Hale www.viewfromthebridge.co.uk

What went wrong?

"What went wrong wasn't what happened this year. What went wrong was what happened in the first 11 years of the euro's history. In some ways we were victims of our success...It was like some kind of sleeping pill, some kind of drug. We weren't aware of the underlying problems". EC President Herman Van Rompuy, 14 June 2010

You have got to be smoking something pretty powerful to think you can get away with this sort of twaddle. If this is the best the EC President can come up with to defend the euro then the quicker he returns to the "non-country of Belgium", as Nigel Farage put it (some months before the recent election made it so), the better.

We all know the euro isn't working and some of us knew it never would, even before it got going. It's not hindsight; it's just plain old history. The nations of Europe have been fighting each other, literally and metaphorically, for centuries and a rigged/flawed/unworkable (you choose) agreement over a new currency had as much chance of achieving social and financial harmony as a one legged man winning the proverbial kicking competition.

As we wait to discover the cut of our hair shirt in tomorrow's budget how confident are we that our politicians are not on the same sleeping tablets as van Rompuy? Isn't it ironic that we exported Keynesianism to the US, where they still cling to the printing press principle, as Europe follows the Austrian school of economics into austerity?

Who is right? Neither or both? Geithner visited Europe last month to make the case for more deficit spending and was ignored. Germany, Spain, Italy, Ireland and not forgetting Greece are following the path of budgetary and hence spending reduction to be followed tomorrow by the UK. They believe that if they don't reign in their deficits now, they never will. Geithner probably knows that the US has already gone beyond that point, but came over here to get a repeat of Van Rompuy's prescription.

Noticeably the French have not changed out of their "chemises de soie". They were similarly out on a limb during the run up to the Great Depression by holding the franc at an undervalued level, whilst hoarding gold that helped the gold standard unravel. (For a fascinating insight into this period "Lords of Finance" by Liaquat Ahamed is a must read) It is unnerving how the social and cultural differences between the great nations, which have changed very little since those times, were largely responsible for that period of economic mayhem.

When Germany went into recession in 1929 one of its largest creditors was the French banking system, flush with cash derived as a function of France's gold "hoard". To quote from the book, a British Treasury official, recalling how much money France had pumped into Russia before the Great War, could not help remarking with cynical detachment, "The French have always had a sure instinct for investing in bankrupt countries." With a similar dose of detachment I can't help observing that nothing has changed over the last eighty years…

What has changed is that Germany and China now hold all the cards. In Europe Germany is the iron man (Angela won't be around for much longer) and without the help of a devalued currency the Greeks et al cannot hope to compete. The Germans don't see why they should help, other than agreeing to a doomed bailout fund, thus sowing the seeds of mutual "destruction".

China too with its massive foreign reserves and, until this weekend, a currency tied to the dollar, is equally over competitive, like France in the 1920s. If the massive imbalances can be unwound then there is some hope that there will not be another significant downturn. The yuan has now been unpegged and, with another dose of the aforementioned detachment, it has been suggested that this is merely a pre-emptive gesture ahead of the G-20 meeting in Toronto, but global markets have so far taken the move to heart and the 10 day rally is now heading for an eleventh.

Gold is also having another good day which will add to the confusion of the Chairman of the Federal Reserve. On June 9th Bernanke was quoted as saying, "I don't fully understand movements in the gold price." But he suggested it might be another example of investors fleeing risky assets and flocking to those that are perceived as less risky, "not only Treasury bonds, but also ones like gold."

Well I have to agree with him about gold…