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Govern-mental

"It is not even a full year since the time of Cleggmania, yet, in his own Sheffield constituency, even nursery-age children now come home with Clegg jokes. ("Why did Nick Clegg cross the road ?" "Because he said he wouldn't.")"

- Matthew Engel, in the Financial Times' Budget coverage, March 24th, 2011.

From time to time since the financial crisis first broke, the suggestion has arisen that the crisis itself represented and continues to reflect a failure of capitalism. A motley combination of Keynesians and socialists has needed little excuse to argue for the expansion of the state – and for the accelerated seizure of private wealth that state expansion effectively represents. Another argument, for which we have some sympathy, has it that democracy's efficacy over other forms of government starts to collapse as soon as sufficient members of the population realise that they can vote themselves privileges. In the early stages of this land-grab of self-selected gifts, the system can continue on the back of those productive elements who haven't yet been woken up by noises from the party that the rent-seekers are enjoying. But towards the terminal stages of any democracy, the system starts to buckle under the weight of accumulated privilege. Demographics concentrate the problem; the Western welfarist model will break down long before a huge cohort of pensioners are being supported by the efforts – and taxes – of the very last private sector worker.

So perhaps government isn't the solution, but is actually the problem. And if an individual government can be detrimental to the health – and wealth – of a nation, it seems plausible that multiple governments operating within a given geographic or economic area may be compounding our problems. It was surely a widely dispersed failure of government regulation, for example, that helped to trigger the banking crisis. And there is a comparably huge problem developing throughout the western economies as governments either try to tackle their vast budget deficits (the UK) or, more visibly, choose simply and deceitfully to try and paper over the cracks (the Euro zone and US). Europe's various governments have had difficulty deciding who should take command of their latest foreign adventuring in Libya. If they can't easily agree a straightforward operational hierarchy in the middle of a war, it seems unlikely that they can agree due process for managing the variously huge national deficits within the common currency bloc during peacetime. On every side, pomposity, inconsistency and national bias predominate. European nations don't even support the common economic principles to which they have notionally subscribed. Italy has drawn up a bill designed to thwart unwanted foreign takeovers. A French bureaucrat whines in response:

"In France, the 2005 decree on strategic sectors did not include agribusiness.. Take for example the acquisition of 50 per cent of Yoplait last week to US group General Mills, even though French rival Lactalis was in the running to take it over. The Italian decision could not happen in France. It is not comparable."

Of course, the French bureaucrat in question was a liar (lying French bureaucrat being admittedly probably a tautology): in 2005, the French government introduced a veto over takeovers in 10 industries deemed "sensitive to national security". This measure was introduced after rumours of a bid by the US firm PepsiCo for French yoghurt-maker Danone.

And now we have the unedifying spectacle of European politicians denying any impact from the current economic crisis in Portugal, or any likelihood of contagion across other periphery (and comparably bankrupt) countries in the Euro zone. Sovereign Man Simon Black takes a lead from Monty Python's famed Black Knight, who shrugs off the loss of both arms and legs to Arthur's sword with the words "'Tis but a scratch":

"Never mind that [Portuguese] yield spreads and bond insurance premiums are near all-time highs. 'Tis but a scratch..

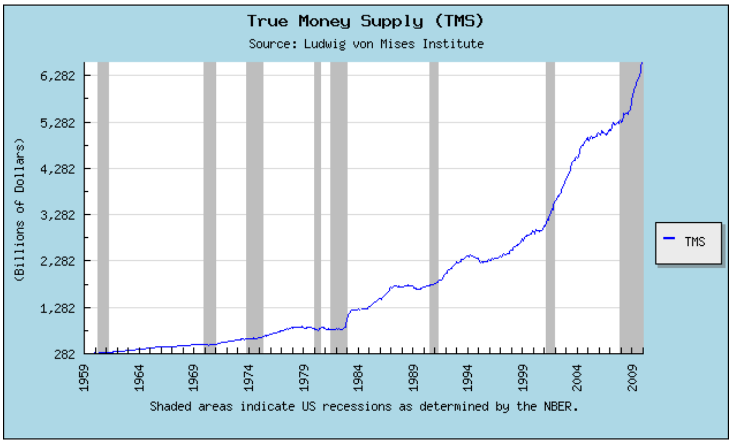
"Today in Japan, two nuclear plant workers were hospitalized with radiation-related injuries. Japan's government continues to deny risk to these workers, and to the population at large, instead raising the decontamination threshold (the danger level of radiation) from 6,000 counts per minute (CPM) to 100,000 CPM. 'Tis but a scratch..

"Earlier this month, William Dudley, the brainiac who replaced Tim Geithner as President of the New York Fed, told business leaders in Queens that "while rising commodity prices may be giving some of you a bad headache, they are not likely to lead to a sustained rise in inflation."

"Never mind that prices of just about everything ex-iPad around the world are increasing, and inflation rates from Vietnam to the UK are painfully high. 'Tis but a scratch..

"Reality is very simple for the rest of us. We know what we pay for things, and we know that amount is increasing. We know nuclear meltdowns are dangerous. We know that fake economic growth created by printing money is nonsense. We know that massive deficits are destructive.."

The topic of inflation is instructive, in that it encapsulates how government and their central bank agents collude to boost the money supply (original inflation) and then disavow all responsibility for the rising prices that inevitably follow. The growth of the US 'True Money Supply' – the amount of money in the economy available for immediate use in exchange – is shown below:



If it looks like the US money supply has exploded, it is because it has. Tangible evidence of that inherently inflationary oversupply of dollars can be seen in the prices of gold and silver – classic money substitutes, that cannot be printed at will by capricious politicians – which continue to trade close to or at record nominal highs. Those suspicious of the 'store of value' characteristics of precious metals – let us call them paper bugs, for that is what they are – continue to cry wolf and bubble in equal measure. But it is not gold, nor silver, that are caught in a bubble – rather, it is the US dollar, and for that matter fiat currency writ large, which is caught in an existential crisis that may terminate in its abandonment as a global monetary reserve.

But government-backed money will not go down without a fight. And the voice of the administration, in the form of establishment mouthpieces such as The Financial Times, continues to deny the problem. Indeed FT writers Jack Farchy and Roula Khalaf last week plumbed new lows in that organ's hysterical if fruitless anti-gold campaign. In their piece on Libya ("Gold key to financing Gaddafi struggle") they highlighted that quality that has made gold

"so appealing to criminals.. and dictators alike: it does not rely on a government for its value."

Rational investors can only add: too right. Anyone who believes in sound money will notice the inherent absurdity in this construction. Do you really want to entrust the value of anything, let alone currency, to government ? Do you know how much purchasing power the US dollar, for example, has lost in the last century ? Rounding up to the nearest 10 per cent, the answer is 100 per cent. Messrs Farchy and Khalaf have managed to establish a new low in yellow journalism, one which more objective, less intellectually stunted and less dogmatic investors will find truly repellent.

That which government cannot do well it should, perhaps, not do at all. Having allowed the periphery countries of the Euro zone to live beyond their means for the past decade and then lie about their finances, Europe's leaders now seem determined to inflict poverty on their people in order to maintain an unworkable currency union, and equally determined to prevent market forces from revealing the still insolvent banking system in all its grim reality. With government finances and bank balance sheets inextricably linked through cross-holdings in each other's debt, such sleight of hand is understandable, but no less corrupt for being so. Investors searching in some desperation for vehicles to protect their wealth in absolute terms should avoid the traditional G7 government bond markets, even now kept afloat at artificial levels through the magic of perhaps permanent quantitative easing money printing, and put their faith in real and tangible assets whose values are some way beyond the powers of venal government to manipulate and distort.

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Important Note: