PFP
Wealth Management

3 Windsor Court
Clarence Drive
Harrogate, HG1 2PE
01423 523311

Lion House
72-75 Red Lion Street
London, WC1R 4FP
020 7400 1860

www.pfpg.co.uk

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The surgery was a success, but the patient died

"We hear that in the future we're going to have a better economy and everybody hopes so, but it's hard for me to believe because I look back on our past three years and what Congress has done and what the Fed has done is literally injected about $5.3 trillion and I don't think we got very much for it. The national debt went up by $5.1 trillion; real GDP grew by less than one per cent; unemployment really hasn't recovered – we still have 7 million people that have become unemployed.. one statistic that is very glaring if you look at the charts is how long people are unemployed. The average time used to be 17 weeks – now it's nearly 40 weeks. Nothing there reassures me.. Also, when we talk about prices, we're always reassured that there's not all that much inflation, and we're told that they might start calculating inflation differently with a new CPI.. of course, we changed our CPI a few years back. There's still a free market group that calculates the CPI the old-fashioned way. They come up with a figure – despite all this weak economy – that prices have gone up 35%, 9.4% every year, and I think if you just went out and talked to the average housewife, she might believe the 9.4% figure rather than saying it's only 2%.. So I would say what we've been doing isn't very reassuring with all this money expenditure.. Spending all this money hasn't helped. That $5.3 trillion didn't go to consumers, it went to buying bad assets, it went to bailing out banks, it went to bailing out big companies.. lo and behold, the consumer didn't end up getting this, the consumer lost their job, their houses and their mortgages.."

- Congressman Ron Paul addressing US Federal Reserve chairman Ben Bernanke, Financial Services Subcommittee on Monetary Policy, July 13, 2011.

Banks, said Murray Rothbard, are always inherently bankrupt. Because "they issue far more warehouse receipts to cash (nowadays in the form of 'deposits' redeemable in cash on demand) than they have cash available. Hence, they are always vulnerable to bank runs. These runs are not like any other business failures, because they simply consist of depositors claiming their own rightful property, which the banks do not have. 'Inherent bankruptcy', then, is an essential feature of any fractional reserve banking system."

If that isn't plain enough, try Frank D. Graham in 'Partial Reserve Money and the 100% Proposal' (American Economic Review, September 1936):

"The attempt of the banks to realize the inconsistent aims of lending cash, or merely multiplied claims to cash, and still to represent that cash is available on demand is even more preposterous than.. eating one's cake and counting on it for future consumption.. The alleged convertibility is a delusion dependent upon the rights not being unduly exercised."

The way Rothbard saw it, the business cycle is straightforward. Bank credit expansion causes an inflationary boom, which is marked by an expansion in the money supply and by what he and other Austrian economists call malinvestment, both by bankers and entrepreneurs. The crisis comes about when credit expansion halts abruptly and the malinvestments are thrust forward into plain sight. What he then calls the "depression recovery" starts the necessary adjustment process "by which the economy returns to the most efficient ways of satisfying consumer desires."

Note that Rothbard conjoins "depression" and "recovery": they are one and the same thing. You cannot have economic recovery without a cleansing, cathartic depression.

"Wasteful projects.. must either be abandoned or used as best they can be. Inefficient firms, buoyed up by the artificial boom, must be liquidated or have their debts scaled down or be turned over to their creditors. Prices of producers' goods must fall, particularly in the higher orders of production – this includes capital goods, lands, and wage rates.. Not only prices of particular machines must fall, but also the prices of whole aggregates of capital, e.g. stock market and real estate values. In fact, these values must fall more than the earnings from the assets."

US Treasury Secretary Andrew Mellon put it a little more hard-nosedly:

"Liquidate labour, liquidate stocks, liquidate the farmers, liquidate real estate."

The economic severity of the depression, in a Mellonite world, would "purge the rottenness out of the system."

But politicians, now as then, abhor painful medicine. As the scale of government support for today's banking system and indirectly for international co-sovereign debt markets swells, one is entitled to ask whether the presumed interventionist (and populist) cure will end up being worse than the disease. Rothbard, as a classic free marketeer, indicated that the economic contraction process causes no malinvestments – unlike the boom that preceded it – so it will not lead to such a painful period of depression and adjustment. "If businessmen are misled into thinking that less capital is available for investment than is really the case, no lasting damage in the form of wasted investments will ensue."

Rothbard's thesis is most striking in relation to the role of government. His first and clearest injunction to return the economy to "normal" prosperity is: don't interfere with the market's adjustment process.

"The more the government intervenes to delay the market's adjustment, the longer and more gruelling the depression will be, and the more difficult will be the road to complete recovery. Government hampering advocates and perpetuates the depression. Yet, government depression policy has always (and would have even more today) aggravated the very evils it has loudly tried to cure."

Rothbard goes on to list the various ways that government might hamper the market adjustment process. The list exactly constitutes the preferred "anti-depression" measures of government policy. What is striking today is how many of these measures are being actively pursued by western governments. The most egregious are highlighted below:

- **Prevent or delay liquidation**: by lending money to shaky businesses, calling on banks to lend further, etc.
- **Inflate further**: further inflation blocks the necessary fall in prices, delaying adjustment and prolonging depression.
- Keep wage rates up: artificial maintenance of wage rates in a depression ensures permanent mass unemployment.
- Keep prices up: keeping prices above their free market levels will create unsaleable surpluses, and prevent a return to prosperity.
- **Stimulate consumption and discourage saving**: any increase in the relative size of government in the economy encourages people and companies to consume rather than invest, and prolongs the depression.
- Subsidize unemployment: any subsidisation of unemployment will prolong unemployment indefinitely, and delay the shift of workers to the fields where jobs are available.

Rothbard concludes his study of the Great Depression by pointing out just how extensive the Hoover administration measures were in an ultimately futile attempt to combat the slump.

"For the first time, laissez-faire was boldly thrown overboard and every governmental weapon thrown into the breach.. by every 'progressive' tenet of our day, he should have ended his term a conquering hero; instead he left America in utter and complete ruin – a ruin unprecedented in length and intensity."

Rothbard holds that only governmental inflationism can generate a true boom and bust cycle, and that any depression will be prolonged and intensified by inflationist intervention on the part of presumably well-meaning politicians. 'America's Great Depression' showcases Rothbard's firm belief that Hoover's aggressive interventionist measures ended up aggravating the economic slowdown:

"The guilt for the Great Depression must, at long last, be lifted from the shoulders of the free-market economy, and placed where it properly belong: at the doors of politicians, bureaucrats and the mass of "enlightened" economists. **And in any other depression, past or future, the story will be the same."** [Emphasis ours.]

So far, the road to ~~serfdom~~ QE3 is unwinding exactly according to plan. Fed chairman Bernanke told Congress last week that "we're not prepared at this point to take further action" but almost immediately conceded that "we have to keep all the options on the table". QE3 it is, then, at some indeterminate point in the near future. As Ron Paul notes above, quantitative easing versions 1.0 and 2.0 have not been staggering in their achievements to date for any class in US society other than the narrow banking elite that the Federal Reserve represents. Recent commentary by both the Fed and the US Treasury (in the words of Treasury Secretary Geithner: "for a lot of people.. it's going to feel very hard, harder than anything they've experienced in their lifetime now, for some time to come..") has been refreshingly candid in exposing just how little influence the authorities have over the economy. When Ben Bernanke was asked by Ron Paul why people buy gold, he replied:

"As protection against what we call tail risks: really, really bad outcomes."

Well, he said it. We note that gold has now broken through the £1,000 ($1,600) level. Having become front page news, there may be better times to add to positions. But the supportive backdrop for precious metals remains utterly compelling.

Tim Price
Director of Investment
PFP Wealth Management
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Email: tim.price@pfpg.co.uk Weblog: http://thepriceofeverything.typepad.com

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