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Freedom !

"During the 17th century, Scottish investors had noticed with envy the gigantic profits being made in trade with Asia and Africa by the English charter companies, especially the East India Company. They decided that they wanted a piece of the action and in 1694 set up the Company of Scotland, which in 1695 was granted a monopoly of Scottish trade with Africa, Asia and the Americas. The Company then bet its shirt on a new colony in Darien – that's Panama to us – and lost. The resulting crash is estimated to have wiped out a quarter of the liquid assets in the country, and was a powerful force in impelling Scotland towards the 1707 Act of Union with its larger and better capitalised neighbour to the south. The Act of Union offered compensation to shareholders who had been cleaned out by the collapse of the Company; a body called the Equivalent Society was set up to look after their interests. It was the Equivalent Society, renamed the Equivalent Company, which a couple of decades later decided to move into banking, and was incorporated as the Royal Bank of Scotland. In other words, RBS had its origins in a failed speculation, a bail-out, and a financial crash so big it helped destroy Scotland's status as a separate nation."

- John Lanchester, 'It's finished', in the London Review of Books.

"It is never difficult to distinguish between a Scotsman with a grievance and a ray of sunshine."

- P.G. Wodehouse, from 'The custody of a pumpkin' in 'Blandings Castle and Elsewhere'.

Given the financial crash that gave rise to RBS 1.0, or the financial crash that gave us all RBS 1.1 (the gift that just keeps on giving), quite why the Scots have a reputation for prudent money management is unclear. We think it has something to do with that one-line headline from 'Not the nine o'clock news': "Scotsman found dead on pay-as-you-leave bus." Nevertheless, Alex Salmond seems determined to exorcise the ghost of past Scottish financial crises by instigating a real doozy this time around. Some of us would object less to the demands for independence for the Scots if the English Parliament wasn't already overrun with them. (Even the name 'Cameron' doesn't exactly sound ***very*** English, does it ?) And the pursuit of local, rather than larger, community does seem to be part of the spirit of the age, even if developments in the Crimea are taking a somewhat darker turn..

Just to twist the knife, having over the last six years cumulatively lost more than the £45 billion in emergency funding provided by the taxpayer in 2008, RBS last week defended the £576 million it set aside for bonuses in 2014. If only businesses outside the banking sector could resort to this sort of fantasy remuneration policy. Ross McEwan, the new CEO of RBS, proudly displayed his own tin ear to criticism of the banks by labelling attractive interest rates for his own customers – which he has now banned – as "abhorrent" and "unfair". Takes one to know one.

There's not a whole lot of point in rehashing the bail-out of RBS *et al*, because there is no counter-factual. The money has been squandered; the milk has been spilt. In his original essay, John Lanchester pointed to four reasons why government would be reluctant to take over the banks and run them, rather than simply pour infinite amounts of taxpayer funding into them:

1. "Because the government would be bad at it." This is obviously a moot point: bad, compared to what ?
2. "Because every decision made by the bank would come at a potential political cost to the government." But this ignores the below-the-line influence of subsequent government policy, such as its fatuous 'help to buy' scheme, which ensures that a permanent under-class will be priced out of the property market unless and until the market crashes precisely ***because*** of the government's own property bubble policy.
3. "They also don't want to admit the extent to which we are all now liable for the losses made by the banks." Well, all of us apart from the recipients of that £576 million, obviously.
4. "Because it would be so embarrassing." Lanchester goes on to add: "To nationalise major financial institutions would mean that the Anglo-Saxon model of capitalism had failed. The level of state intervention in the US and the UK.. is comparable to that of wartime. We have in effect had to declare war to get us out of the hole created by our economic system. There is no model or precedent for this.."

In a previous commentary ('Forty centuries of learning nothing') we highlighted the lasting extent to which governments have tried – and failed – to enforce wage and price controls, from the dawn of civilisation to the present day, in an illusory and doomed fight against inflation. (One critical reason for this failure is that governments wilfully turn a blind eye to the fact that they themselves provoke inflation through the irresponsible expansion of base money beyond any increase in the rate of productivity.) Maintaining interest rates at near-zero is price control. Pumping trillions into the bond market to suppress longer term interest rates (and coincidentally to service the debts of massively indebted governments) is price control. Attempts at competitive currency devaluation are price control. There is not a single investment within the world of global capital not affected by government price control. Warren Buffett famously observed that if you've been playing poker for half an hour and you still don't know who the patsy is, then you're the patsy. So we are all patsies now.

While we search for assets whose prices are less obviously distorted by malign government intervention, it's refreshing to hear a *mea culpa* from a member of the economics "profession". Earlier this month, William White, a former economist at the Bank of England and the Bank of Canada, made a frank admission:

"The analytical underpinnings of what we [mainstream economists] do are actually pretty shaky. A reflection of that fact, is that virtually every aspect you can think of with respect to monetary policy, about best practice, has changed and changed repetitively over the course of the last 50 years. So, this stuff ain't science.

"Think about what's happened recently. One, its completely unprecedented. People are making it up as they go along. This is hardly science – building on the pillars of the past. Secondly, what they've been making up as they go along actually differs across central banks [The Bundesbank, for example, is fighting the threat of high inflation, whereas the Fed is more concerned about the prospect of deflation]. They can't even agree amongst themselves about what's the best way to do things. I'm becoming more and more convinced that all of the models we use are basically useless.

"The best way to look at the economy is as an ecosystem. Some live, some die. There is no equilibrium as such; things are constantly growing. It's surprising that we've had this huge crisis that the mainstream didn't predict. It's gone on for years, which the mainstream absolutely didn't predict. I would have thought this was a basis for a fundamental rethink about what we used to think we believed. But that hasn't happened. The policies that we've followed - on the monetary side at least - since 2007 are just more of the same. Demand-stimulating policies that we've been following, I think, erroneously, for the last 30 years.

"We've got the potential to do so much harm by not getting the creation of fiat credit and money right. We've got the capacity to do so much harm that we should be focusing much more on making sure that doesn't happen."

Doctors, at least, have the Hippocratic Oath: first, do no harm. If only economists and central bankers had a similar ethic. As we navigate these treacherous investment waters, we offer up a humble prayer: Lord, grant us freedom from the actions of governments.

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