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Groundhog Year !

"If you are going to buy worthless banks then it makes sense to use worthless money to do it."

- Posting on The Daily Telegraph website in response to story 'Bank of England hits the panic button'.

Harold Ramis' 1993 film 'Groundhog Day' may well be the funniest thing to come out of the 1990s, apart from Vanilla Ice or New Labour. Bill Murray's cynical weatherman finds himself trapped in a surreal existential crisis, and forced to live out the same day over and over again. Pretty soon he begins a plot to seduce his boss, Andie MacDowell, which gives rise to the following exchange:

Him: You weren't in broadcasting or journalism ?

Her: Uh-uh. Believe it or not, I studied 19th Century French poetry.

Him: What a waste of time !

Now we have something that trounces the original Bill Murray response. In the HBO movie version of Andrew Ross Sorkin's 'Too Big To Fail' (a.k.a. The Last Days of Lehman Brothers), Paul Giamatti (playing The Ben Bernank) tells a roomful of politicians that he spent his entire academic career studying the Great Depression.

Him: **What a waste of time !**

Even by the standards of Economics, which as we have stated before, as per P. J. O'Rourke's definition, is an entire scientific discipline of not knowing what the hell you're talking about – and there's some question over that use of the adjective 'scientific' – you'd have to be going something to devote **an entire academic career** to studying the Great Depression, **and drawing all the wrong conclusions.** A little like devoting an entire career to building a scale model of the Great Wall of China out of matchsticks, and then accidentally falling on it one night, and setting fire to it. Whilst being an idiot.

Here is what we think. More specifically, here is what Murray Rothbard wrote in 1963:

"There are other values in deflation, even in bank runs, which should not be overlooked. Banks should no more be exempt from paying their obligations than is any other business. Any interference with their comeuppance via bank runs will establish banks as a specifically privileged group, not obligated to pay their debts, and will lead to later inflations, credit expansions, and depressions. And if, as we contend, banks are inherently bankrupt and "runs" simply reveal that bankruptcy, it is beneficial for the economy for the banking system to be reformed, once and for all, by a thorough purge of the fractional reserve banking system. Such a purge would bring home forcefully to the public the dangers of fractional reserve banking, and, more than any academic theorizing, insure against such banking evils in the future."

Contrary to the received wisdom that interventionist government (under the administration of the ill-fated Herbert Hoover for some years before FDR took the presidency) ameliorates and foreshortens a dismal business depression, Rothbard suggests (in 'America's Great Depression') that the very intervention so clamorously called for (both then, and now) actually **extends** and **amplifies** it:

"If government wishes to see a depression ended as quickly as possible, and the economy returned to normal prosperity, what course should it adopt ? The first and clearest injunction 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 aggravates 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. If, in fact, we list logically the various ways that government could hamper market adjustment, we will find that we have precisely listed the favourite "anti-depression" arsenal of government policy. Thus, here are the ways the adjustment process can be hobbled:

1) ***Prevent or delay liquidation***. Lend money to shaky businesses, call on banks to lend further, etc.
2) ***Inflate further***. Further inflation blocks the necessary fall in prices, thus delaying adjustment and prolonging depression. Further credit expansion creates more malinvestments, which, in their turn, will have to be liquidated in some later depression. A government "easy money" policy prevents the market's return to the necessary higher interest rates.
3) ***Keep wage rates up***. Artificial maintenance of wage rates in a depression insures permanent mass unemployment. Furthermore, in a deflation, when prices are falling, keeping the same amount of money wages means that real wage rates have been pushed higher. In the face of falling business demand, this greatly aggravates the unemployment problem.
4) ***Keep prices up***. Keeping prices above their free-market levels will create unsaleable surpluses, and prevent a return to prosperity.
5) ***Stimulate consumption and discourage saving***. We have seen that more saving and less consumption would speed recovery; more consumption and less saving aggravate the shortage of saved capital even further. Any increase of taxes and government spending will discourage saving and investment and stimulate consumption, since government spending is all consumption.. Any increase in the relative size of government in the economy.. shifts the societal consumption-investment ratio in favour of consumption, and prolongs the depression.
6) ***Subsidize unemployment***.."

When too much easy money helped provoke the banking crisis, it is difficult to see how even more of the same can help to resolve it. But then, in light of the Bank of England's latest foray into quantitative easing, all £75 billion-"worth" of it, it is increasingly clear that the Bank of England has no interest in protecting savers, consumers, retirees, or for that matter anyone outside a narrow clique of banking interests. We can say with certainty that printing money is of itself inflationary. And as Rothbard also said,

"Only governmental inflation can generate a boom-and-bust cycle.. the depression will be prolonged and aggravated by inflationist and other interventionary measures. In contrast to the myth of laissez-faire, we have shown [in "America's Great Depression"] how government intervention generated the unsound boom of the 1920s, and how Hoover's new departure aggravated the Great Depression by massive measures of interference. 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 belongs: at the doors of politicians, bureaucrats, and the mass of "enlightened" economists. **And in any other depression**, past and future, **the story will be the same**." [Emphasis ours.]

FT columnist John Gapper ("In praise of Wall Street protesters") issued a strangely sympathetic note about the motley arrangement of banking sceptics assembled in New York. In passing, however, he wrote the following:

"The policies I have seen are either crazy (one protester railed on a video about closing the Federal Reserve and abolishing fiat money) or have little chance of gaining wide support.."

Having recently published some of our unpublished letters to the editor of this somewhat confused financial journal, we weren't about to let that remark go without further discussion. So, here is the first in an occasional new series of unsolicited letters to FT columnists who show no obvious understanding of the current crisis and its origins:

"Dear Mr. Gapper

You write that closing the Federal Reserve and abolishing fiat money would be "crazy". Could you deign to suggest why ?

I would suggest it is crazy to have the entire global economy continually imperilled by a narrow constituency of Wall Street and banking interests. There is nothing inherently "sensible" about fractional reserve banking – it is crazy that savers are reliant on a system that continually and cyclically breaks down as confidence is lost on the back of imprudent bank lending, bank leverage and insufficient bank reserves. Fractional reserve banking itself, as you surely know, is really nothing more than an elaborate Ponzi scheme that shifts the balance of wealth from savers and producers to bankers of dubious social value. For as long as we have fractionally reserved banks we will have bank runs. Is the pursuit of monetary stability really so crazy ?

The same goes for fiat money – monopoly money enforced by the state, which it has every incentive to destroy over time through inflationism. If wanting something slightly sounder and more honest in money-as-a-store-of-value is crazy, I don't much value your idea of sanity.

You may wish to ponder the following quotation from Austrian economist Ludwig von Mises which I am sure you will have read before:

"There is no means of avoiding the final collapse of a boom brought on by credit expansion. The question is only whether the crisis should come sooner as a result of a voluntary abandonment of further credit expansion, or later as a final and total catastrophe of the currency system involved."

The governments and central banks of the western economies seem to have decided on further credit expansion, not to say money printing. I hope you're enjoying your apparently sane fiat money now, while you can still use it. A US hedge fund manager suggested to me last year that if there was a second bailout for US banks, there would be a revolution. Bring it on, I say. I know whose side I'm on. When it comes down to it, do you ?"

I don't, of course, expect a response, as I'm sure Mr. Gapper has his time taken up in not understanding other similarly pressing issues of global economic importance, like so many of his colleagues at the FT. But if I do receive one, I will be delighted to reprint it here.

There is something beyond tragic in our monetary authorities doing all the wrong things, again and again, in a 'Groundhog Day' parody of appropriate free-market activity, that unless quickly reversed can only end in monetary disaster.

We now have the latest bill for a one-day rally in the stock market: £75 billion. Meanwhile gold is still on sale, and we are (perhaps not so happily, but resignedly) buying more.

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