FSU Contrarian Roundtable Discussion

Inflation Has Some Serious Benefits.

True or False?

January 21, 2004
with
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RMS Titanic
A Night at the Chicago Lyric Opera? or, Opera is for Sissies….

Have you ever hit a skunk at 70 MPH in a 1994 Lincoln Town Car on I-55 cruising to Chicago to go the Lyric Opera? Your choices are: Yes, No, Mebbe (maybe), and Hell's Bells -- Nah, I don't like Opera! What's inflation? More legal tender fiat paper funnie monie chasing fewer goods and services…. aka, Gutenberg Bernanke and his printing press!

Yes, I stunk up the Town Car, but damn those new Kelly Springfield All Season Radials are great…. didn't hurt 'em a bit! No, I missed the sucker completely… was that really a 65 MPH zone? Or, Mebbe, but Damn, I was actually doing 85 in an Illinois mandated 65 MPH zone and I didn't get caught….? Eh? For speeding! Hell's Bell's… I would hit a skunk anytime to avoid a night at the opera – Opera's for Sissies, anyway!

You all see the point here, Don't You? It is all a matter and manner of Perspective… and ehhhh… Semantics…. Welcome to Fed$peak 101… Welcome to Skunk 101.

Yes, I stunk up the Town Car, but damn those new All Season Radials are great….

Our friend Nelson Hultberg down in Dallas has penned *Invasion of the Mind Snatchers* and *Economic Meltdown, Secessionist Crackup?* Scott Trask at *www.mises.org* recently penned *The Fed's Predecessors in American History.* Andrew Dickson White penned *Fiat Money Inflation In France* in the mid 1870s. James R. Cook just penned *Funny Money.* Timeless essays know no century. Inflation is good if you are the one creating it, manipulating it, telling the citizenry that it is under control and to beware the deflationary Bogeyman! It works for creating and waging wars.

Examples are the Continental, the Greenback, the Revolutionary Guillotine French Assignat, and the Federal Reserve Note. The Continental was the silly paper issued by the Continental Congress to finance the American Revolution. When the House of Rothschild wanted something usurious like 20% for financing the War Against Southern American Secession, Mr. Lincoln pulled a Bernanke and did his own Gutenberg creating the Greenback. The Guillotine Artists of the

French Revolution made it a lose thy head crime to own and trade in heavy metal, forcing paper assignats down the Citizens' gullets, while they wrecked their country for the next two centuries…. Leading to Mr. Bonaparte, who mucked things up a bit further. However, Mr. Jefferson, not completely asleep at the switch, was able to finance Mr. Bonaparte's traipse into Russia for a mere $3 million Pieces of Eight, then called in 1803, the U.S. Dollar by the U. S. Constitution. Mr. Monticello, aka President Jefferson, pocketed the Louisiana Purchase leaving Napoleon with a PUD (Russia) in his hand. This leads to Manifest Destiny, the Teddy Bear Doctrine of Speak Softly, Carry a Big Schtick, and the Bushian Doctrine of Pre-Emptive War. Welcome to History 101. History is nothing, but the history of money systems anyway. Ask those Romans about the Emperors' coin clipping…

The Federal Reserve Note financed WWI, WWII, the Korean Conflict, the Viet Nam War, and other silly military missives… such as Iraq Crusade I and currently Iraq Crusade II. This coin clipping has been going on since the Garden of Eden or Paradise Lost. Financing wars is a mere drop in the bucket. Yes to inflation and the moral decay of societies, the great giver of social welfare capital, the keeper of politicians and big government, and all of those that will take care of you… Lemme give you a clue – the Crusades were a total flop! The proof? Israel and the PLO -- these folks will be killing each other -- after Armageddon! Inflation is the central bankers' means to ensure the Ponzi shell game continues as debt service is serviced like a perfumed, bosomed lady of the night as more patrons seek the heavenly pleasures of more debt in the bed of luscious night. For if debt be repaid, the money supply would thus contract, making illegitimate…. All those stealth Johns and Tricksters of the Night (central bankers, hint … hint). Baron Rothschild, the founder of the Banking Cartel, said something to the effect that given the ability to print money, he could control any government. Smart Dude!

The Continental became worthless paper…. So too the Greenback for most of its life and so too the FRN… the world's ultimate Ponzi Shell Game. We'll all know the jig is up when a good lady of the night will not accept the Buck for a Buck… but demands a little heavy metal on the side for a slide, Klyde. Prostitution has a reputation of being the oldest profession….? Probably is, but I suspect that the moneychangers and the politicians mentioned in the Bible, and the clipping of the coins of the realm evolved in that, self same… good night. Dear Reader, did you make the connection? Central Bankers are nothing but prostitutes… and since most are men, that means male prostitutes -- of their money systems.

No, I missed the sucker completely… or Ode to John Denver!

Again, this viewpoint is a matter of perspective. If Joe Six Pack and Sally SUV believe that their new SUVs are great investments purchased by adding more debt on their real estate, which has been making them rich, and they are watching the FED rig the DOW by Mike Bolser's work at www.gata.org on how the repurchase agreements aid Wall Street being suspended by a slender FRN, then all is well in LA LA Land, aka Main Street America.

Who cares about inflation when we are rolling in the dough…. Who cares if our groceries, utilities, gasoline, insurance, and other goods and services cost more paper? We're rich and rolling in the dough. Our appraiser just said our house was worth $500,000 on our re-finance, and gosh a golly, we only paid $250,000 for it three years ago. Thank you realty appraiser and ***www.appraisalinstitute.org*** for all your *Delphi Scams,* AVMs, and dive by (drive by or drive bye bye!) appraisals on our realty the past three years. Can you make it $600,000 this time next year? Thank you *Lord Jumpin' Jesus Raines* at Fannie Mae for Credit Scoring (aka Credit Scouring), and for teaching the world about two-tiered structured finance (aka two-teared structured finance). Should Joe and Sally live *in the several county area surrounding and inside Denver with a 15 year high* on the ***Foreclosure Flood,*** Composer and singer, John Denver, probably says it best in *Rocky Mountain High*! **--** Rocky Mountain High…. Colorado! I don't foresee many ladies of the night in Denver accepting real estate 4th and 5th Deeds of Trust as chattel promises to pay for their services in such a micro realty market. Perhaps I did miss this skunk completely? But, who's the Huckleberry?

Mebbe, but Damn I was actually doing 85 in an Illinois mandated 65 MPH zone…

Illinois is the Land of Lincoln. Chicago is considering passing another $1 tax on packs of cigarettes. Interstate speed limits on I-55 from St. Louis to Chicago are 65 MPH. We hit Illinois at Louisiana, MO at the Mississippi River on US Highway 54 for our December 2003 pilgrimage to the Lyric Opera in Chicago. Illinois is a trip. It is one of the most agricultural and rural states in the Great Mid-West, yet it has the cultural center of the Mid-West at Chicago on lower Lake Michigan. It is the home of www.appraisalinstitute.org.

Chicago rivals New York City in the world of opera as well as the European Capitals. Some of the best opera singers on the planet tour through the Lyric Opera. Currently some Illinois politicians are in the hot-seat for political trickery and taking nice folks' money. Mebbe inflation of the money supply by the monetary charlatans Bernanke, McTeer, Greenspan et al, the fleet elite Ponzi-ists at the Federal Reserve do deserve some credit and credence for the City of Chicago and the State of Illinois. It costs me more to go to the Lyric Opera now than it did five years ago.

Now I won't even get near an airplane, Columbia Regional Airport, or Midway Airport in Cicero… because of monetary policy, which creates Fatherland Insecurity, the shredding of the Constitution and the Bill of Rights… If I don't take my own tobacco, I buy a new bridge over the Chicago River. I suppose for the opportunity to hear world class opera in Chicago, costing me more, making me more self-reliant to drive my 1994 Lincoln Town Car avoiding Mr. Ashcroft's Gestapo, paying for higher food, lodging, opera tickets, and gasoline… is worth the erosion of my money. Besides, CNBC, the Wall Street Journal, Peoples Investor Daily, and the Government (BLS, aka Bureau of Lying Spats) tell me I am rich. Hummm…. Mebbe I missed the skunk on I-55… but I have a sick feeling that Social Security should be more appropriately called Social Insecurity and maybe the City of Chicago should just go ahead and pass a $100 tax per pack on cigarettes. Perhaps the City of Chicago also plans to tell Daniel Barenboim how to conduct the Chicago Symphony and *play his Steinway next!!??*

Inflation is good. When folks is rich, you can tax their assets to death -- as long as the ladies of the night accept 4th and 5th Deeds of Trust on real estate as chattel payment for services… play some *Eine Kline Nachtmusik* for me, á la Mozart! – with all those notes, if you don't know how to listen, the fleecing is a great trick, or treat, ain't it, Joe Six Pack and Sally SUV? Big Grin!

Hell's Bells -- Nah, I don't like Opera… It is for Sissies….

Perhaps, my friends, you all are forgetting the Parable of I-55 and the Skunk…. You hit it, you stink… You miss it, you may miss other stuff… You can't remember hitting or missing it? -- you were driving too fast… not paying attention! So, if you don't like opera…. Go listen to Billy Ray Cyrus and that trash from Nashville, *Achy Breaky Heart.*

Nobody considered ***you*** worthy enough to teach you how to appreciate opera or the Money Issue. That's what inflation is all about at the Federal Reserve, ***Bubba!*** These rascals have been controlling the educational system from grade school to the university level since 1913 and making sure that their pundit economists get Nobel prizes in economics and that all the American economists visit the ladies of the night at the Federal Reserve, so they can pontificate on the good sex of monetary policy, inflating the un-Holy Hell out of the money system, aka the BUX, to steal your wealth and savings. It keeps the politicians in office, erodes the U. S. Constitution and that silly Bill of Rights and protects the Bank of Rome and the House of Rothschild.

 

Inflation provides the vehicle for the social welfare capital state in the process of wealth destruction. Inflation ensures that the debt service may be paid. For Alas, Poor Yorick, if the money system contracts in a deflationary spiral, the debt service will not be paid… hence the jig, the Ponzi Shell Game of the central banker charlatans is up. The mechanism of inflation is the Mandrake Mechanism of creating money out of thin air by adding more debt behind the money system… a smoke and mirror… an illusion of wealth, power as a Nation, and prosperity. If you read Dr. Antal Fekete's work, you will understand that low interest rates and deflation through debt payoff put pin holes in the prophylaxis of the central bankers' skunk… low interest rates tender the present worth of debt much, much higher than it actually used to be. It's a hard concept to get…. But once the pin-prick is in the Trojan, you will understand how the Horse really works.

Conclusionary Remarks…. Hitting a Skunk with a Deuce and a Quarter?

1970 Buick Electra 225, aka, Deuce and a Quarter… I drive a 1970 Deuce and a Quarter. In 1970, my Deuce stickered and retailed at your local Buick GM Dealer for about $4,900+ as a Deuce Custom with a 455 with a 4-barrel carb, electric windows, power seats, AT, PB, PS, AT, vinyl top, fender skirts, electric trunk release, AM/FM, and AC. You didn't get radial tires then, but you did get the fancy naugahyde interior, speed alert (before cruise control), plush carpet, arm rests on the front seat and metallic paint with real Honest-to-God lead in it -- go price a GM Buick Electra in today's legal tender fiat funnie monie….

1994 Lincoln Town Car… Given the Choice of hitting the Federal Reserve skunk with a 1994 Lincoln Town Car… or a real Deuce and a Quarter… I should prefer the Deuce to hit the Skunk…. When I hit a skunk in a Deuce…. I don't need silly FED RESERVE mandated airbags… (aka the ability to control an industry or crush it…) Buy a Deuce today… if you can find one (heavy metal…. Hint…hint…) Inflation does have some serious benefits and a few pitfalls… for the downside, go talk to your parents about the social welfare state of affairs, the Federal Reserve and Bureau of Lying Spats robbing them blind on increases to their Social Security checks. Mother-in-law (aka Miss Melanie Bear) just got notice of a $2/month increase in her Social Security check, but an increase in her Medicare deduction. ***You all, see how this works, Don't You?*** It is all a matter and manner of Perspective… and ehhhh… Semantics…. Welcome to Fed$peak and Skunk 101. **Answer to Question:** True and False, depending on your perspective, whether or not you own, and drive… a 1970 Deuce and a Quarter for hitting skunks.

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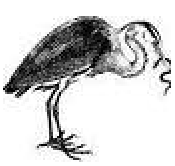

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Buy others for news. Buy us for judgment.

Does inflation have some serious positive benefits?

The view of many economists that inflation can be a good thing is, from an economic point of view, unobjectionable. Indeed, it is hard to see why, from a theoretical standpoint, that it should be at all controversial. Inflation in the sense that it is most commonly understood is just a way of looking at changes in the prices of traded goods and services. Clearly, from the standpoint of those selling those goods and services, higher prices are welcome. And that is precisely the point. Whether or not it is “good” depends really on who is receiving and who is paying those higher prices.

There are nevertheless problems associated with this way of looking at things because changes in goods and services prices do not actually represent inflation or deflation. These are correctly understood to be states of change in the value of money, and this is a very different thing than changes in the prices of goods and services. All the consumer price index tells you is how profits are shifting in the markets for goods and services. Of itself, it tells you nothing about the value of the unit of account.

This point is far from academic. It has been correctly pointed out over the years by a number of observers that by arbitrarily excluding changes in the prices of certain assets that conventional inflation measures only capture part of the change in monetary value. In the modern American economy this can be readily seen in action. Money in its modern format can be exchanged for bananas or stocks, which is to say that stocks and bananas are substitutes for one another. Over the last ten years or so it has been fashionable on Wall Street to talk about deflation, as in “China is exporting deflation because of its low wages.” At the same time, the price we have had to pay for future earnings of the S&P 500 has soared. Do low or falling wages represent deflation? Not necessarily. They may be symptomatic of it, but they are not proof.

A more serious discussion of inflation requires that its legal, institutional, ethical and moral dimension be examined. It is not for nothing that in ancient times the priestly caste monopolised the business of money and the truth of the matter is that in some ways things have not changed much. Because money has varied functions as medium of exchange, unit of account, and store of value, it is important, indeed vital, that it be dependable. That is the reason, and in my opinion the only reason, why gold is attractive as money. Because of its unique characteristics, it is dependable.

That is why inflation is problematic, and why even those who argue that it can be positive base their conclusions conditionally on inflation being both moderate and predictable. This may well be so over the course of the ordinary business cycle, but it is far from obvious, at least to me, that it is so or even *can* be so over a longer credit cycle. The reason for this is that such cycles are long. To get a feel for this consider: the last time the US economy was in a similar position as it is in today was some thirty-five years ago. Does anyone seriously think that the Federal Reserve has a planning horizon that long? In the mid ‘80s Paul Volcker was asked why he had done such and so and he replied that in central banking one deals with yesterday’s problems today, not with tomorrow’s, or words to that effect. This was nothing more than an honest description of the realities of politics.

Indeed, the real problems with inflation do flow from politics, because there is no more political act that the granting of the right to issue money. Today we are living with the consequences of the Federal Reserve Act of 1912, which created the Federal Reserve System, a collection of private corporations owned by the very institutions that it supposedly regulates, and which profit from the money monopoly that Congress granted the Fed.

The creation of the Fed represented the triumph of expedience over principle and of partisan profit over national interest, so what else is new? The Trusts that the Fed’s creation was nominally meant to control were granted ownership of the Fed. The demand of some reformers of the day that the trusts should not be allowed to control the nation’s money but that the government should do so was met by Congress in the breech: Congress nominally accepted the responsibility and then delegated it back to the Trusts. And that is where matters still rest.

The significance of this to the question before us here is that this laid the groundwork for a changed attitude toward debt and inflation both amongst the captains of industry and in society generally, and the Fed's primary role during the 30s became that of debt accommodation. To be sure, this was at first exercised with circumspection but after America emerged unchallenged for all intents and purposes from the Second World War, circumspection crumbled. The result was Nixon's expedient abrogation of America's international treaty obligation, and expedience has governed national monetary and fiscal policy since, as it has for a century at least.

That expedience has led to the progressive consolidation of monopoly control over industry after industry, and the wholesale looting of public assets on a scale not seen since the land grabs in the early days of the Republic. Monopoly control over the monetary system has made easy the financing of all this with debt ultimately backed by the obligation of citizens to pay taxes, which is to say with other people's money. Another way of putting this is that in monetary terms this has been financed by inflationary debt accommodation by the Fed.

The Fed's ability to do this rests on the degree of prevailing popular belief in the legal fiction that it is independent of political control, and that it will perform its duties in a proper fiduciary manner. This is the most transparent fiction, and has resulted in laughable expedients over the years by both the Fed and the government to maintain its "credibility." So, for instance, in the early '80s when house price inflation was soaring, it was dropped from the inflation indices in favour of "imputed rents" that were not soaring. Hedonic pricing was another wheeze that has allowed the harnessing of Moore's Law in computer performance to the price indices. The Treasury together with the Fed seeks to control the prices of gold, exchange rates and so on, but piously intone that targeting asset prices (i.e. stocks) when they are going up is improper, but supporting them when they go down is responsible behaviour. The Fed has "granted" to its owners the right to self-regulate their market derivatives businesses, which is to say to value their own balance sheets, in flagrant disregard of its Congressional charter, and promoted the extension of this right to include credit derivatives under the terms of the new Basel II Accord.

I doubt that even JP Morgan, who reportedly once told a friend that he lost sleep at nights worrying about an antitrust suit being brought against him, would have in his wildest dreams imagined that he and his kind could, never mind would, get away with this. That the Bushes and the Rubins of our world are not only getting away with this but with much else besides says volumes.

It is no accident of course that as the Fed has pushed interest rates toward zero and the administration has opened the bond floodgates that corporate profits have soared. Workers have not participated in this, and wages are stagnant. Jobs are being created, but in other countries, such that the Fed's inflationary debt accommodation flows straight through to the bottom line. The Wall Street euphemism for this is that this is higher "productivity" but this is nonsense in any economically meaningful sense of the term. When one looks at personal debt statistics in the United States it is not "productivity" that comes to mind but "predatory lending." This is a straightforward inflationary siphoning of money from one end of the economic spectrum into the pockets of the other end.

So, gentlemen, in answer to the question at hand I can only answer: it depends on which end of that spectrum you are.

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Inflation: It's Not Just a Good Idea, It's the Law.

The law in question is the Federal Reserve Act of 1913. By giving a small cartel of bankers the exclusive right to create unlimited money and credit, the Act virtually guaranteed long term price inflation. Since 1913, the US dollar has lost almost 95% of its purchasing power. This loss in purchasing power is a direct result of a massive increase in the supply of money that has occurred since the founding of the Fed.

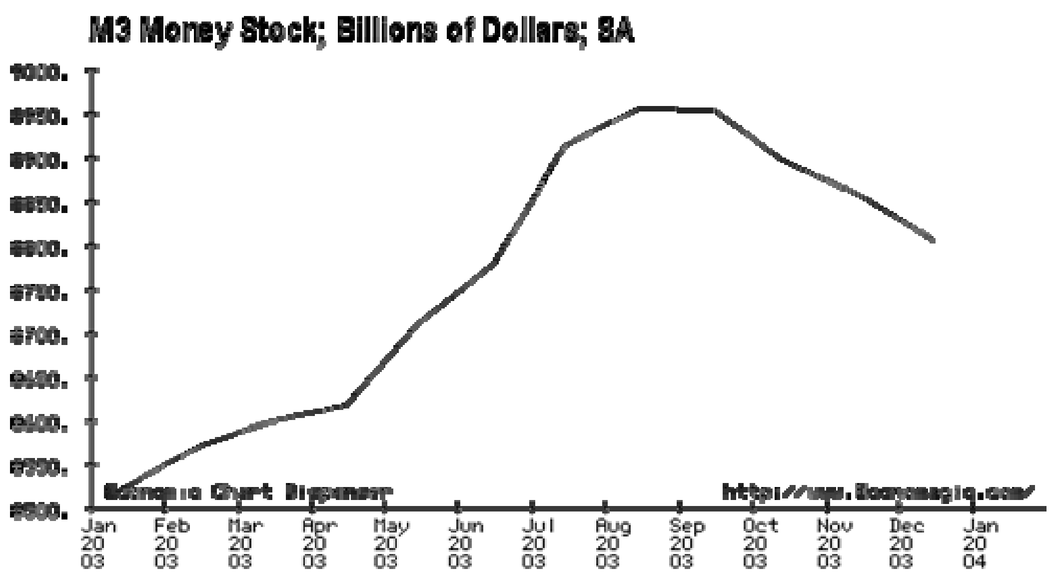
Historically, spokespeople for the Federal Reserve always maintained an illusion that the Fed was dedicated to fighting the forces of inflation using its power to set short-term interest rates. Nowadays, there is not even a pretense of fighting inflation. Fed governors have now declared **deflation,** a fall in the money supply and general price levels, to be public enemy number one. Recently, Fed governor Bernanke stunned the world by admitting that the central bank could and would use the power of the mythical money printing press to create inflation if necessary. Fed Chairman Greenspan publicly lamented that "an unwelcome fall in inflation" would be disastrous to the economy. What is an "unwelcome fall in inflation" anyways? Heck, I would gladly welcome some deflationary relief against sharply rising energy, food, insurance, housing, and medical costs. Why is to my advantage to pay more for everything that I buy?

To be fair, Messrs. Greenspan and Bernanke actually have something to worry about. The massive increase in "money" that I mentioned at the beginning of this essay was a little misleading. The Fed actually creates relatively little money in the sense of the dollar bills that you hold in your wallet. That is true fiat currency. Created from a printing press and backed by nothing, these bills at least have some tangible reality and carry no hidden obligations or interest liabilities. Most of what we call money that is carried in bank accounts, money market funds, brokerage accounts, etc. are actually just credits. There are few, if any, actual bills backing any if this "money." Money today is almost entirely a balance sheet entry. The money that you and I hold in our various accounts is actually just somebody else's debt. These debts are packaged as securities and traded as money. They come in the form of Treasury bills, commercial paper, repurchase agreements, and a menagerie of other exotic debt securities that people and institutions accept as payment in lieu of actual cash. Since these are all just debts, they posess the two fundamental characteristics of debt: interest payments and maturity. All issuers of these securities are obligated to pay interest and to reimburse the creditor full face value at maturity. So what happens if some of the issuers of these debt securities default on their obligations? Big Trouble.

The quirky design of the Federal Reserve System makes it rather inefficient at creating and distributing cash-type money, but in coordination with member banks it is fabulously efficient at creating debt. This is called "fractional reserve banking" and it allows your local bank to create gobs of new money via lending, all mediated and facilitated by the Fed. Fractional reserve banking is something like a pyramid scheme (remember Mr. Ponzi?). As long as only a few people try to cash in, the system works fine. But like all pyramid schemes, it needs a constant flow of new funds to keep the game going. Since almost all of the money in existence carries a compound interest rate, the supply of new money or debt must increase by at least as much as the interest expense to support the system. This is where the inflation comes from. Don't believe me? Look at the chart of M3 broad money supply.

Since 1960, there has hardly been a single year when this broad measure of money materially declined. This is a good thing because it allowed the money game to continue and the country to prosper and grow. Should the money supply start to decline, there would not be enough money to pay interest expense so debts would start to default at an increasing rate. Since debt is also money, disappearing debt will further shrink the money supply in a vicious circle. This is what Greenspan and Bernanke are so worried about. They MUST keep inflation above a minimum level to ensure the proper functioning of the monetary system. It's not their fault; they did not design the system.

Eagle eyes looking at the above money supply chart may see a little "hook" at the end of the graph. Is that a downturn in the most recent money supply data? Let's zoom in and see.



Yes, it's true. M3 money supply has been contracting since Sept 2003. All of the other money measures M1, MZM, and M2 are also contracting. What's worse is that money velocity is falling also, making the existing money stock less potent. If this trend continues there will almost certainly be trouble in the US economy. This is because the US is incredibly indebted at all levels. Personal, corporate, municipal, state, and federal debt are at record levels and growing at an increasing rate. Increasing debt requires increasing money to service the debt. If insufficient money is available for debt service, much debt will default and the economy will spiral downward.

Why is the money supply falling? It seems that nobody really knows for sure but there are probably a number of causes relating to overcapacity, global competition, trade deficits, bubbles bursting, etc. Maybe the country just can't take on any more debt.

What is the Fed to do? Unfortunately, they have already exhausted almost all of the tools at their disposal to "reinflate" the system. They have reduced interest rates to near record low levels in an effort to entice even more borrowing. But as we have seen, more borrowing only increases the strain on the system and the Fed is near the end of its effectiveness using its conventional policy tools. They have threatened to go "unconventional" using untried and aggressive tactics but this will only further weaken an already battered US dollar and may destabilize financial markets. The Fed is in a box and there is little left for them to do except to jawbone the economy into recovery.

It seems that we are near an endgame of some sort. There are people who think that it will end in hyperinflation and those who argue for deflation. It's possible that we may experience both simultaneously in different markets. The debt situation can only be resolved by either depreciating the currency (inflation) or liquidating the debt (deflation). Investors must prepare for either scenario. This is why many thoughtful advisors are stressing the need for some precious metals and hard assets as part of a sound portfolio. These are the few asset classes that will weather this storm.

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In my opinion, we are shifting from gold to TIPS or inflation adjusted bonds as the reserve of choice for the world central banks. That's why talk of them running out of gold is nonsense because they are going to sell it all and a weakening economy will take care of the rest. Factoring out inflation and the fall of the dollar, gold has been in a bear market since last February and will continue to be in one until there is a collapse in the world banking system.

We are not going to repeat the 1970s because there is too much debt around (in the 1970s inflation and lack of deficits made debt a much smaller % of the world economy so leverage in commodities and ignoring bonds was possible---not today!) The situation is very similar to the early 1930s---after a stock boom and massive debt accumulation due to 70 years of prosperity and government wars, there was a great struggle for liquidity and the first asset sold was gold. Gold went down under $17 an ounce in 1931 and then doubled to $35 in 1934 revaluation. Gold didn't start to recover until the Bank of England repudiated the gold standard in September 1931. My research over 300 years shows that gold is not the asset to own in a financial debt crisis (vs. an inflation boom after debts have been liquidated) until the very end. I do believe gold is heading back near 1000 sometime after this year, but it looks like it will get to a dollar/inflation adjusted bottom near 300 before that happens.

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There are plenty of good five-cent cigars in the country. The trouble is they cost a quarter.
Franklin P. Adams 1881-1960, American Journalist, Humorist

Inflation, according to Merriam-Webster online dictionary, is **an increase in the volume of money and credit relative to available goods and services resulting in a continuing rise in the general price level**.

We all pretty much have felt the effects of inflation in one form or another. However economists and the central bankers chose to define inflation as an increase in price of goods. This is a very clever way to actually hide what they are doing. If they are able to inflate the money supply but keep the cost of certain good suppressed mainly those that the common Joe uses everyday, they have more or less won. The simple reason being that the average person has come to view inflation in terms of price increases.

One mechanism to keeping the cost of common goods down is through the use of heavy subsidies. This is used everywhere in the farming sectors, Manufacturing and industrial sectors, etc. I will elaborate on this in more detail on a follow up essay as this would a deviation from the topic at hand.

There are some incredibly positive attributes to inflation. As an investor/trader I am interested in trying to find the best investment and make the most money I can on that investment and inflation actually plays a big role here. The only problem with inflation is that for the most part the poor actually become poorer and the unprepared move down 1-2 ranks. That is why the saying originated the "poor become poorer and the rich get richer" while the middle class get wiped out.

Since we have greedy slugs at the helm of the banking system, their inflationary tactics are designed to produce unequal benefits. Normally if one inflates and spreads the money equally there is no net change as the price of goods move in equal percentages to reflect this increase in the money supply. However the central bankers will have none of this. They want to inflate as much as possible and at the same time redistribute as little as possible of the new money they have just created out of thin air. The net result is that if you are unable to see in which direction they are moving, you will simply be left paying the tab. Your purse that was once full is now ¾ full and the prices of goods have moved up unevenly.

This is what is happening now. Manufactured goods are extremely cheap; yet look at the price of houses. Commodity prices have shot up, housing is getting to be beyond the reach of most in big cities. Salaries have not kept up with the level of monetary inflation. The only way people are able to buy houses is because of the low artificially controlled interest rates. This fools many a new buyer into taking a debt that he/she really does not have the means to pay of.

However despite all these negatives the astute investor can make a tremendous killing if they take a little time to look at what is going on. For example the astute investor would have started to notice that prices of houses started to increase rather drastically towards the end of 1999 and early 2000. They would have also noticed that Gold actually broke its Downtrend in 2000. They would have noticed that basic raw materials broke their down trend in Early 2003. They would have also noticed the trend of printing more dollars, if they bothered to read what this new administration was proposing. So the middle class family could have taken a mortgage and bought one house as the price inflated they could have possibly taken a loan on the existing house say at the end of 2000 or early 2001 and used it to buy a second home. They could have put some of their money into Gold bullion and a little into some gold stocks, many of which are up over 600% since 2000.

Let me give you a real example of prices, in one neighbor hood in New York and how someone really did something to preserve his way of life. I am not going to mention specific names. This person was a cab driver and in New York one can earn a living driving a cab. He noticed that houses were increasing in price and so bought his first home in 2000. In the middle of 2001 his home had increased in value by over 10%, so he took a second mortgage and bought another home and then rented this unit out. In 2002 both his properties were now really shooting up in value. So he quit his job and bought two foreclosures homes, fixed them up and rented them. Well to make a long story short. He has now sold all the homes and has enough money to retire and take it easy.

What did he do? He spoke to several knowledgeable individuals to get as much information as possible on the subject of inflation. He then read as much as he could. Remember we are talking about someone who really was not highly educated but took the time to educate himself. He has now spared himself from the insidious effects of inflation that many of his co-workers are now experiencing.

Let's now look at the true full range benefits of Inflation. In this world if you do not spend time educating yourself the price you pay is extremely high.

If you thought education was expensive, try ignorance for a lifetime.

Almost every Gold bug is secretly rooting for inflation. Why do I say this? If they are expecting Gold to reach 800, 1000, 1500 etc they are rooting for inflation. Gold prices are one of the main indicators that there is something seriously wrong with the banking system and that the monetary supply is going out of control. In the later stages we have the fear factor that actually tends to push the price of Gold right into the stratosphere as everyone panics and looks for away to protect their assets.

Those that have bought real estate are also secretly rooting for inflation, as they want the prices of their property to increase. If you really take the time to think about it inflation is very beneficial to the astute investor. Those that are investing in the stock market are also rooting for inflation. It is the free money policies that push people and business to risk more of their money in the market. Look at the present market, it keeps going higher and higher, but when you price it in Rands or any other strong currency it has done nothing. But the astute investor was able to see that the central crack head bankers were out of control and knew that not only would Gold prices rise but there would be a rise in the price of general equities to.

These prices increases have more then compensated for the inflationary practices of the central bankers. However the only ones to have received this benefit are a small group of elite investors and the cronies of the central bankers who were privy to this information, long before these Junkie started to run the press.

When you think about it, life is nothing but one huge market place and in the end someone needs to lose in order for someone else to win. Not everyone can win and not everyone can lose. The sad part is that it takes a lot of someone's to lose to make one someone wealthy. The net effect is zero. Money is not really lost it simply moves from many pockets to one big fat pocket.

When the NASDAQ crashed everyone was made to believe that several trillions dollars of wealth were lost. That was and is a fat huge lie. Those trillions of dollars simply moved out from hundreds of thousands if not millions of pockets into a select few thousand pockets.

It's a net 0 game. So when people scream about the negatives of inflation. They are doing so because they have not taken the time to educate themselves on the many tools that are available to protect themselves against this insidious disease. This once again brings life to the saying, "A Empty Tin makes the most Noise."

In spite of the cost of living, it's still popular.
Kathleen Norris 1880-1966, American Novelist

Do I condone inflation? No I don't. Do I really think it is something great? No I don't. But what I think and what can me or others rich are two different things. The central bankers are not going to change; they have been doing this for far to long. . They are masters at this game, one day they will lose but I might be dead and gone by then. So rather than being an empty can screaming from the top of my lungs about the negatives of inflation, I would rather be a silent full can smiling on some sunny beach with a margarita in my hand and reading a good book. I will leave the screaming to the Empty cans, who seem to have plenty of time on their hands.

In the end all that really matters is for one to find a way to take care of themselves and their loved ones. And if you take the time to educate yourself on how inflation works, on how the central bankers work you can ride on their backs for free and increase you net worth while you are doing so.

> Next to inflation, majority rule is the most ingenious scheme ever contrived by government. Most people have never dared to question the basic morality or logic in the assumption that the majority should have power over the minority. A majority of the people in the South once believed in black slavery. Did that make it moral? A lynch mob is majority rule stripped of its fancy trappings and its facade of respectability. In a community where homosexuals outnumber heterosexuals, should the majority have the right to outlaw sex between married partners of the opposite sex? In a community where atheists outnumber non- atheists, should the majority have the right to outlaw the practice of religion? ... a dictatorship allows only a small number of people to interfere with the rights of others, a democracy makes it possible for great numbers of people to impose their will on others -- through the force of government. Is an act of aggression more right if carried out by the majority than by a dictator? Since approximately half the eligible voters vote this means that approximately 75% of the people are ruled by 25% of the people. Robert J. Ringer, American Writer

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Alan Lunt
Contributor
Tactical Investor

It was an honour to be asked by Sol to contribute to the discussion, as I am an unknown. Before I entered the markets I spent 27 years farming and seven years on and off in forestry cutting trees off at ground level. I learnt a cartload. From forestry it was that there are 2 really dangerous times, the first is when you are learning and the second is when you know how. From farming it was the firsthand knowledge of how inflation works in a primary industry. On 3 separate occasions I saw the value of my farm double in the space of 2 years, and saw it halve in value once. Those are not conditions of stability, which are needed in order to make sound business judgments, particularly from a long term prospective.

I define inflation as an increase in monetary aggregates; an increase in volume and an unsustainable condition. When a animal dies on a farm, if it is not disposed of quickly, it inflates into a putrid, rotten, seething mess before it collapses into nothingness. It is a natural cycle, one that cannot be tampered with. In monetary inflation there comes a point when inflation will implode on itself too.

All the increase in the value of my farm did was give me the ability to borrow more so I could pay for the increase in costs, it did nothing like the same orders of magnitude to my income. Inflation stole my profitability. It is a sneak thief, a plunderer and a slowly tightening vice. At some point the production of goods has to become profitable or the production ceases. The laws of diminishing returns turns into a race for economies of scale. Inflation causes farm prices to rise but the value of what comes off the land does not increase. All that has happened is there is one more sole out there looking for work and one more deserted dwelling.

I saw, I felt, but didn't understand the dynamics of inflation. My learning came when I was a practical farmer, does this mean that now I have to face dangerous times? I think the answer is yes. I look around this town and see house prices that are double from this time two years ago. The house is still the same, it has not earned t its increase in value, sure the owners are happy but what they don't see is that the value of their cash money has been cut in half in relation to house prices. We do not measure money against things, we measure things against money. What is the constant? What is the one thing that does measure money?

I view Sir Alan Greenspan as the world's most powerful man. His decisions affect the globe. His open spigot policy is harming commodity nations. He has increased liquidity to such an extent globally that the world is sloshing around in paper money. That money must find a home, too date it is stocks and property. Also the ingrained psyche is demanding that money must be spent before it looses value.

Each country has an individual business cycle and Keynesian Theory demands a loosening of liquidity by the central bank of the country affected by business weakness. In New Zealand the business cycle was not in trouble, we were coming off a currency low, there was no need for added liquidity. But the money pump from the Fed spilled over into this country. The flight of US dollars literally poured money in. That money has found a home here and property. Prices have rocketed. In communication with Dr Brash, the past Reserve Bank Governor, he said to me "that he thought a little inflation was not a bad thing". That may be true when you are being paid in local currency, but when your income is from the international markets and you are battling currency rises as well any increase in costs inflation is destructive. Greenspan's policy is slowly but surely destroying our primary sector. Money is coming here because we are a commodity-based nation that same money is destroying the base it came here looking for. When that money leaves again it will leave a spent carcass and people wondering what on earth happened. It will leave a debased currency.

Is inflation a good thing? I view it as destructive, insidious, mercurial, hidden and most of all debilitating. Gold is the only weapon we have for protection.

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The chief salutary effect of inflation, ironically, is deflation. Of course, this is contrary to the designs of the inflationists who in 1971 advised the government of the United States to destroy the gold standard. They justified inflation as "the lesser of two evils." They abhorred deflation, a beast they admittedly could not control, but thought that inflation was a tame beast that they could. Their utter failure to grasp the fact that the destruction of the gold standard would, albeit with a lag, cause deflation once the pendulum swung the other way, has landed the world in the present precarious position. Their policies have made the Kondratieff long-wave cycle, consisting of alternating inflationary and deflationary spirals, to get out of control. It was criminal negligence of gigantic proportions on the part of the inflationists that they have never investigated the more remote consequences of the destruction of the gold standard .

Of course, the inflationists realized that their anti-gold policies would destabilize the dollar, and unleash speculators in the foreign exchange market. They welcomed this as a salutary development, and they recommended the manipulation of monetary and fiscal policy as a means to save the dollar from immediate and complete destruction. What they did not realize was that their anti-gold policies would also destabilize the interest-rate structure, and unleash speculators in the bond market as well.

Interest rates, no less than foreign exchange rates, were stable under the gold standard. Speculation in the bond market, no less than in the foreign exchange market, was non-existent. There was only benign arbitrage which kept foreign exchange and interest rates stable in the face of temporary disturbances such as crop failures or earthquakes.

No inquiry was held into the problem what consequences gyrating interest rates may have on the world economy. In particular, the deflationary danger inherent in a prolonged fall of interest rates was completely ignored. The point is still not widely appreciated, and the world is totally oblivious of the mortal danger of a depression that might come about as a delayed side-result of the destruction of the gold standard thirty years earlier. Economists of the current vintage have been trained to parrot the slogan that "the gold standard was the direct cause of depressions." This is the exact opposite of the truth, as the following discussion will reveal.

Bond speculation is no zero-sum game. Virtually all speculators are on the long side of the bond market. They follow the lead of the Fed in buying the bond (or interest-rate derivatives). In fact, the Fed makes bull-speculation in bonds risk-free through its open-market operations. The question arises: who are on the short side? Why, the producers, of course. They are passive participants, whether they like it or not, with their capital at stake, who stand to lose as the rate of interest falls. Literally, they have no choice in the matter. They are the sitting ducks in this unconscionable shoot-out arranged for the benefit of speculators by deliberate government policy. Moreover, the producers are quite unaware of what's going on. In particular, they are completely oblivious to the fact that they are being served up as the sacrificial lamb on the altar of government omnipotence. Bond speculation aided and abetted by government is responsible for denuding producers of their capital and for transferring their wealth to the bond speculators in the form of unprecedented profits. As the producers lose their capital, the domino-effect of falling firms paralyzes the economy, causing unemployment and collapsing prices.

The present deflation, caused by inflation, is most conspicuous in Japan. It should be our signal heralding the coming depression. We should heed the warning and stabilize the interest-rate structure forthwith by opening the U.S. Mint to the free and unlimited coinage of gold. If we fail to do this, then we may have to pay a terrible price as history's worst depression will engulf the world economy, wiping out prosperity.

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Does the Policy of Inflation Have Positive Benefits?
None its Proponents Would Admit To

Debating that question from a Contrarian point of view (i.e. that it does) is a tall order for me because I've argued relentlessly – as many of my peers have – that inflation has at best no benefit, and at worst, enormous negative consequences. Though I've considered many of the alleged benefits, I've discovered none that could qualify as a real economic or social gain (*for the purpose of brevity we'll assume the reader accepts the definition of inflation solely as it applies to the growth of money and credit – rather than prices or a price level*).

Clearly, at any rate, mine is a controversial position today, because it implies in absolute terms that even the slightest change in the supply of money is "undesirable." While undesirable may be a good word to conform to the common lay interpretation of that concept, it is exactly the wrong word to describe a sound objection to the policy of inflation.

Untenable or futile might be better. Lacking any utility would be accurate. But claiming that inflation is undesirable is technically incorrect, because many people actually desire it. Implicit in that fact is that they think they can obtain a benefit, and for some period of time they probably can. It's merely a matter of being in the right place in line. The real trouble is keeping your place.

Real estate developers routinely tell me how they love inflation – because their properties go up in value while they're developing them. There must be gold bulls, that underneath the surface at least, secretly worship inflation because they own a few gold stocks, or like to hoard bullion, and despite what they say in public (Kudlow is an exception). The same applies to many industries and segments of the economy. Most people must think they benefit from the inflation of money supply on one level or another, else there would be no sustainable mandate for it in a democracy.

Yet most of these benefits are largely self-interested, and illusory. Or at least I claim they are.

For, in a time where even some of the most ardent hard money types accept a degree of inflation as for one reason or another necessary or beneficial, or not worth disputing, where inflation has reigned almost year in and year out for more than a century, and where most economists both public and private impute some degree of validity to the concept, the assertion that inflation confers no economic benefit on society must also sound relatively reactionary, or outdated.

Are we to believe that everyone else has got it wrong? How arrogant!

Well, there's more. The fact that everyone has got it wrong is partly deliberated. The theoretical framework for most policy is either Monetarist or Keynesian on some level. Indeed, our argument is basically that the credibility of the theoretical constructs used to justify inflationary policies rests not with their validity, but rather with their convenience to the interests of the proponents of easy social policies, which don't benefit anyone. If making that charge is arrogant, so be it.

We live in a world that is governed by the market's laws, but which refuses to accept the market's discipline. Instead we've erected huge institutions to challenge or control the market. Through shared interests we have come to accept their flawed theories, and related alchemy.

But rather than reiterating the Libertarian and Austrian School argument that inflation confers no benefit whatsoever in the first place, I'd like to instead point out that I've found few instances where even the proponents of inflation (in terms of money and credit) are willing to argue directly that it confers a true economic benefit.

It seems their preferred strategy is to ignore such arguments, and to redefine the concept of inflation such that it is okay to despise it without arguing against an expansion in money/credit.

In other words, because inflation is generally defined as currency debasement or a quickening pace of increase in the general price level, rather than an increase in money supply, the debate over the benefits (or drawbacks) of money supply expansions specifically loses relevance.

Notwithstanding, *rationalizations* exist. The following benefits are commonly cited:

1. We need a lender of last resort
2. A growing economy needs more money (suggesting a positive impact on productivity)
3. Price stability (ironically)
4. Credit / monetary cycles can last indefinitely
5. Markets need liquidity
6. Everyone should have the opportunity to own a house
7. The socialist's goal of achieving full employment on its terms rather than the market's
8. Money supply as a general tool of economic policy

Forgive some of the overlap. For example, numbers 2, 3, 5, 6, 7, and 8 are inherently the same because they all suggest that money is part of society's productive capital (as opposed to merely the medium of exchange). Nevertheless, these seemingly positive rationalizations differ markedly from the benefits that the proponents of the policy actually aim for.

Once it is seen that the theoretical support for the veracity or efficacy of the rationalizations above breaks down easily, we're left wondering, either the government is dumb, or those aren't the real reasons they prefer the policy of inflation.

Of all the various groups that favor the policy of inflation for its perceived benefits, the two most influential sectors are the nation's banking system and government.

The positive direct benefits that governments actually believe they can obtain (*but never quite can, and never admit to aiming for*) are generally recognized as follows:

1. Policy exculpation and utility in sustaining deficit spending generally
2. The financing of programs incapable of passing taxpayer scrutiny
3. The financing of election campaigns (by using it as champagne for the economy)
4. The financing of emergencies such as war is seen as a productive use of inflation policy
5. Growing the dependency of society on the welfare-warfare state

6. Wealth redistribution to bureaucrats, politicians, regulators, and/or unions
7. Empire building

Some of the benefits a banking cartel might secretly strive for, from inflation, are:

1. Control over wealth and its redistribution to financial sector / banking czars
2. The subsidization of extravagant lending practices (and fractional reserve banking)
3. Concentration of power (since centralization is required to sustain any inflation policy)

However, just like the real estate developer would only admit to desiring inflation in confidence, these influential groups aren't likely to admit to these particular benefits any time soon, for fear of implicating themselves and undermining the credibility of the fallacious theories they peddle.

Instead, they pretend that the growth in money supply is but a byproduct of economic progress, and growing wealth. They attribute credit to the market system for inducing the creation of money all on its own, as if it could be sustained without a central bank to influence and alter values (*i.e. to control/postpone the consequences*), and as if the government's spending demands caused none of it. And they readily attribute credit to the central bank for stimulating an expansion in employment through its manipulation of interest rates (the price of credit). Socialist governments in particular tend to promote the benefits of inflation for everyone but themselves.

Thus they <u>justify</u> inflation by lying to you about the nature of the benefits it produces (*because the wealth is denominated in a currency that ultimately devalues according to the laws of supply and demand and the basic theory of the value of money*), but rarely claim to pursue any of the more insidious self-interested benefits gold bugs claim they strive for via the policy.

For instance, in the paragraph before last, the reality is opposite; the market should be credited for producing any kind of real recovery, and central banks should be blamed for their influence in the market of sustaining a policy of below market interest rate levels – easy money – leading to the creation of *too much money* (and credit), which really undermines the market's potential to efficiently satisfy society's true needs.

In conclusion, it is the monetarist idea that is victorious, in so far as the academic world does not attribute any significance to the most significant single influence on the value of the currency, and consequently, on the price structure of the economy – the growth of money and credit. In such an environment of denial, the question of the benefits of inflation is incidental to the fantastic claim that inflation is low or nonexistent.

The reason this path is chosen, in my view, is that we are in fact in the 21st century. The nature of information has changed, people should be increasingly less easily fooled, and perhaps it is easier to argue something is black when its white than to argue the veracity of some of the traditional but increasingly discredited rationalizations in favor of the policy of inflation.

But the question remains, if even the benefits that inflation's proponents secretly pursue confer no true or sustainable benefit, why has the policy lasted so long, and why is it still so popular?

Either our basic argument is incorrect, or the proponents of inflation are too dumb to understand the consequences of their actions, or they are flat out enemies of money, and consequently, the free market. If our argument is sound, the remaining two options are sobering thoughts.

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