MAINSTREAM ECONOMISTS' MONETARY INSANITY

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Paul Krugman's article in the December 15 issue of The New York Times under the title *G.O.P. Monetary Madness* takes G.O.P. presidential candidate Dr. Ron Paul to task for his 'ideological' stand on money. For excellent reasons, not all of which had to do with fear of a Zimbabwe-style hyperinflation, the Constitution explicitly prohibited manipulation of the dollar such as Bernanke's threefold increase of the monetary base in three years. Krugman ruefully reports that the 'hard money doctrine and the paranoia about inflation' took over the G.O.P. that has, up until now, meekly followed Keynesian precepts about pump priming and turning the stone into bread through pushing interest rates all the way down to zero.

According to Krugman, in spite of the 'false alarm' sounded by the Austrian economists over the debasement of the dollar, inflation is still only 1.5 percent. 'Who could have predicted that so much money printing would cause so little inflation?' he asks rethorically. 'Well, I could, and I did', he boasts, 'because I understand Keynesian economics that Mr. Paul reviles.'

In the event, unknown to Krugman, I also predicted the same thing. Unlike Krugman I did more than simply predicting that inflation was not the danger. I warned that Keynesianism would lead to *deflationand depression*. Money-printing has become counterproductive. Krugman doesn't understand that it will boomerang. I stated that, unwittingly, Bernanke is the Quartermaster General of the Great Depression II (see: *Front-Running the Fed*, www.professorfekete.com, February 9, 2010). He doesn't understand the monstrous mistakes prophet Keynes made concerning the role of speculation in the money-creation magic. The fact is that central bank buying makes speculation *risk free* in the bond market. In comparison, speculative risks in the commodity market appear forbidding. All the speculator has to do in order to reap risk-free profits is to preempt the Fed. He buys the bonds before the Fed has a chance. Then he turns around and dumps them into the lap of the Fed at a profit. The Fed is helpless: it must buy at the higher price. Keynes completely misrepresented the ability of the central bank to stay in charge, given its compulsive drive to suppress interest rates when confronted with a profit-hungry pack of bond speculators.

Friedman's analysis of the Great Depression couldn't be more wrong. In 1933 deflation was brought about not by the gold standard but, *au contraire, by abolishing it.* Here is what actually happened. Roosevelt has removed the only competition government bonds have, gold. The most conservative investors saw their gold confiscated and, willy-nilly, they were forced into the next most conservative instrument, Treasury bonds. Speculators became emboldened and bid bond prices sky high for risk free profits. Had gold been still available, bondholders would have severely punished the speculators for their daredevilry. They would have sold the overpriced bond and stayed invested in gold until bond prices came back to earth from outer space. Then they would have bought their bonds back at a profit.

In the absence of gold, speculators made interest rates go into a tailspin. That caused dominoes in the commodity market fall. Prices collapsed one after another. Pieces on the chessboard started falling as well, symbolizing serial bankruptcies of productive enterprises. Breadwinners of families lost their jobs in droves as money flowed from the commodity market to the bond market in the wake of speculators selling commodities short while buying bonds hand over fist. All the while Keynes was rubbing his hands together behind the scenes exactly like Mephistopheles had in the famous paper money scene of Göthe's*Faust* (Part Two).

The same thing is happening all over again. When a central bank increases the monetary base three-fold in three years, this is a clear invitation for bond speculators to move in and make a killing. But what the central bank utterly fails to understand is that, contrary to its hopes, new money is not going to the commodity market. Speculative risks there are far too great. Instead, new money is going to the bond market where the fun is. Bond speculation is risk-free. Speculators know which side the bread is buttered. Krugman doesn't.

Dr. Paul is the conscience not just of the G.O.P., but of the entire nation. Through inflation or through deflation, the mad orgy of money creation that makes mockery of the Constitution will finish the Keynesian agenda of ruining the nation and the world economy.

Krugman's joy over the supposed defeat of Austrian economics is premature. Bernanke's Fed in blissful ignorance is still putting money in the hands of speculators which they use to place bets on the further fall of interest rates and commodity prices. The day of reckoning comes when falling interest rates destroy capital and, together with it, destroy budding job opportunities. The lethargy of businessmen will continue. They will not start hiring as long as the interest-rate structure is in falling mode.

Welcome to the world of Keynes-inspired Great Depression.

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