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The American Inflation:
Where we are, How we got here and Where we are going

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DEFINITION OF INFLATION

Over the years, as United States policy makers have pursued an inflationary monetary policy, the definition and attention towards inflation has changed from the cause to the effect. Here is Webster's definition in 1983:

"An increase in the amount of currency in circulation, resulting in a relatively sharp and sudden fall in its value and rise in prices: it may be caused by an increase in the volume of paper money issued or of gold mined, or a relative increase in expenditures as when the supply of goods fails to meet the demand.

Here is Houghton Mifflin's definition in 2000:

A persistent increase in the level of consumer prices or a persistent decline in the purchasing power of money, caused by an increase in available currency and credit beyond the proportion of available goods and services.

Here is Wikipedia's take:

In mainstream economics, the word "inflation" refers to a general rise in prices measured against a standard level of purchasing power. Previously the term was used to refer to an increase in the money supply, which is now referred to as expansionary monetary policy. Inflation is measured by comparing two sets of goods at two points in time, and computing the increase in cost not reflected by an increase in quality.

The cause of inflation has been relegated as secondary. The changing definition illustrates our changed perception of inflation. In the days of the gold standard, everyone knew inflation resulted from an increase in the supply of money. In today's world, few know or understand the cause of inflation because society has been educated to believe that inflation itself is the effect, rising prices. As the great economist Milton Friedman said, "Inflation is always and everywhere a monetary phenomenon." Now that we know the correct definition of inflation, we shall take a brief and general look at the monetary history of the United States.

US MONETARY HISTORY

Prior to the creation of the Federal Reserve in 1913, there were two national banks. The first bank existed from 1791 to 1811 at the behest of Alexander Hamilton, who opposed the views of Thomas Jefferson and James Madison. In 1811 Congress refused to extend the bank's charter. The Second Bank of the US (1816-1836) a copy of the first, was brought down by President Andrew Jackson. Jackson vehemently

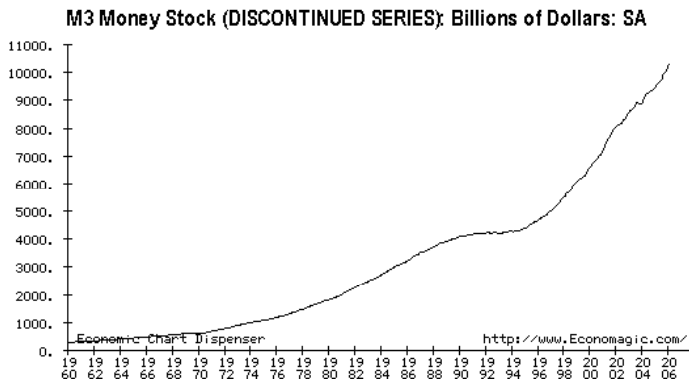
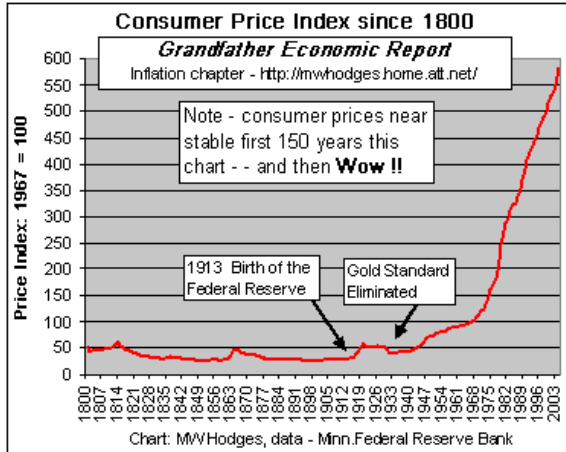
opposed the idea of paper money and a national bank. While most would say that the Federal Reserve has given us faith in a central bank and paper money, we must remember that the idea of a central bank has been a contentious issue for most of our history. Thus, it would come as no surprise, historically speaking if contention over the Fed's existence surfaced.

Turning to the money component of the monetary system, it was "hard currency" that played the large role until 1971. From 1785 to 1861 the country was on a silver standard. Following the Civil War, the country was on a gold standard from 1871 to 1971. Inflation only spiked during wars as the government essentially printed money to fund each and every war. After the wars, inflation (presumably because the paper was drained from the system) receded to pre-war levels. The country was on a strict hard money standard until it was first significantly altered by FDR during the Great Depression. He outlawed ownership of gold and baited citizens into turning in their gold. The government's ownership of increased quantities of gold, allowed it to devalue the dollar by 66% and thus, institute the New Deal programs.

Following World War II, as per the Bretton Woods agreement, nations maintained a fixed price of their currency in terms of gold. This agreement fell apart when President Nixon took the US off the gold standard. He had little choice as foreigners were draining the country's supply of gold, in exchange for their paper dollars.

While I support some kind of gold or silver standard, it must be noted that all was not well, all the time with the gold and silver standard. Runs on banks, financial panics and depressions were frequent occurrences. Small businessmen such as farmers struggled to advance themselves because under the gold standard they could not always get the credit they needed. Tight credit conditions also caused numerous banks to fail. Nevertheless, from a very long-term perspective, the country flourished and became a world power under the standard. The gold standard limited excess money creation, prevented fruitless growth in government and thus enabled primarily the free market and the private sector the opportunity to drive the country forward. Hence, in a little over a century, the US grew from 13 colonies into a world economic power.

Now take a look at these charts of the Consumer Price Index (CPI) and the M3 Money Supply:



(Hodges marks FDR’s dollar devaluation against gold as the elimination of the gold standard. It didn’t end officially until 1971 and at that point, you see prices soaring).

These charts, coupled with an understanding of our monetary history, illustrate beautifully our modern inflationary world and why and how this came to be. Since 1971, there has been excessive money and credit creation and prices have skyrocketed in a historical context. Without a gold or silver standard, there is no check on the amount of money or credit that can be created. Now lets take a look at the group that creates the money.

THE FEDERAL RESERVE SYSTEM

In the early 20th century financial and economic leaders wanted a central bank for the role of lender of last resort. There were more than several bank runs and panics that occurred from 1890-1910. As a result, the Federal Reserve was established in 1913 with the mandate of fighting inflation and maintaining full employment. It attempts to achieve these objectives through managing interest rates via open market

operations.

The truth is that the Federal Reserve, and central banks in general, are a form of Soviet style central planning. The Fed has control over the currency, its supply, and its value and therefore maintains great control over the economy. This means that there is no restriction (absent a gold standard) on its ability to inflate the money supply. Conversely, it can also contract the money supply, as it did by nearly 1/3 in 1929. Moreover, the Federal Reserve is a private, unaccountable, unelectable body that creates money out of thin air and loans it to the government and makes interest on it. It is shrouded in secrecy in that the public does not know the ownership structure of the member banks that own the Fed's stock. The member banks derive profits from US taxpayers who foot the cost of the government borrowing from the Fed.

Why does the government borrow money from the Federal Reserve, when it has the constitutional authority to issue its own money, debt free? And why does the Fed have the authority to create money out of thin air and then charge interest on it? I'll leave that to the "conspiracy theorists."

What we do know is that since the advent of the Federal Reserve inflation has been a constant. Prior to the Fed, inflation over extended periods was nearly non-existent. Since the creation of the Fed, the dollar has lost 95% of its original value. It's obvious that the Fed has failed on its inflation mandate. In terms of managing the overall economy and employment, the Fed has succeeded through continuous inflation (money creation). Though time will tell if the Fed can continue its inflationary ways without any visible and obvious adverse consequences. Now let's take a look at the various inflation outlets.

MONEY AND CREDIT OUTLETS

There are several different outlets for new money and credit. Hence, inflation can manifest itself in various ways and forms. Monetary stimulus can make its way into the productive economy (capital goods and investment), or be used for consumption, or make its way into the various asset markets. Utilized effectively, monetary stimulus can have a positive impact on the overall economy. Unfortunately, the Federal Reserve maintains no control over the outlet of inflation. The Fed cannot control hedge funds borrowing money to speculate in the markets, it cannot control the extension of risky loans to speculators, it cannot control the federal governments wasteful expenses and it cannot force lenders to loan to only those making key capital investments. The hope is that money and credit growth yields greater growth in the production of tangible goods and services.

One can glean, from a look at our history, that since money and credit has become more widely available, the cumulative outlets have not been positive for the

economy. According to Dr. Chris Martenson¹, the first trillion dollars was created from 1620 to 1974. It took 10 months to create the last trillion dollars. Do you think that the progress made in the past eight months is in anyway commensurate with that progress made from 1620 to 1974?

An abundance of available money and credit, as we have had for years, badly distorts usually reliable economic signals. This stimulus, rather than savings, earned income and gains from production, has fueled growing consumption, asset bubbles in stocks, bonds and property and in turn, the perception of a healthy and growing economy. Yet, most mainstream economists ignore these facts and automatically assume that asset bubbles reflect true economic strength. Credit is necessary to grow the economy but as I will explain in the next section, too much money and credit for too long severely exacerbates the foundations of an economy and ultimately the economy itself.

FIAT MONEY AND DEFICITS

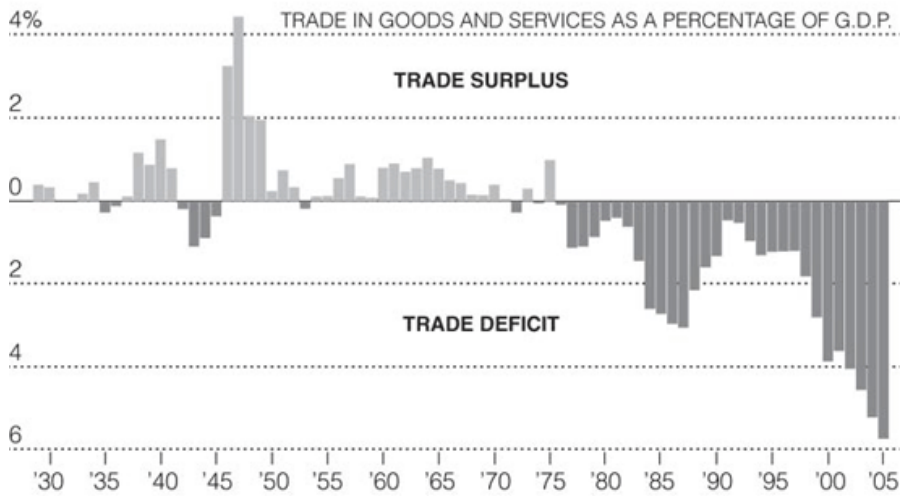
Since 1971, when President Nixon abandoned the Gold Standard and effectively ended the Bretton Woods agreement, the United States and all other nations have possessed a currency that is fiat money. The dollar's value (and value of the other currencies) is derived from its acceptance as money by consumers and governments. Because it has no backing by anything tangible, the dollar, intrinsically is worth only the paper it's printed on.

One can turn to 1971 and the desertion of our currency's link to gold to examine how we have become extremely indebted and why deficits have been the norm. Here are graphs of the US trade balance as well as the US national debt, which accumulates from yearly budget deficits.

- ¹ Dr. Chris Martenson,
<http://www.financialsense.com/fsu/editorials/martenson/2007/0108.html>

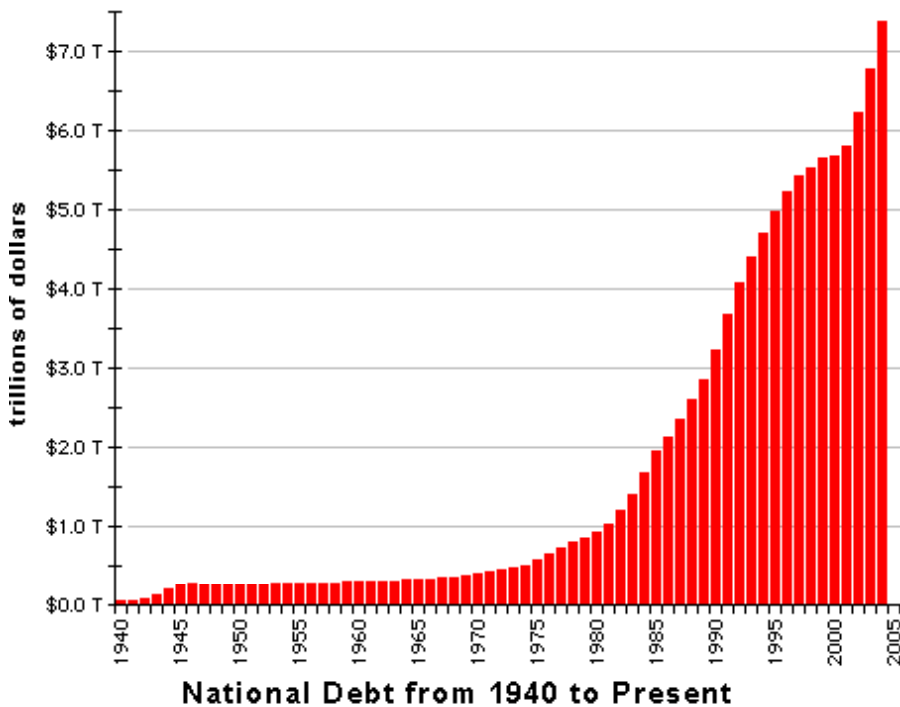
A Widening Deficit

The United States trade deficit has grown sharply over the last decade.



Source: Bureau of Economic Analysis

The New York Times



Source: U.S. National Debt Clock
http://www.brillig.com/debt_clock/

Both charts clearly show that 1) prior to the gold standard we rarely had trade deficits or debt problems and 2) since the abandonment of gold, growing budget and trade deficits have been the trend. The root cause of all this is a fiat currency.

Without a gold standard, there is little incentive to have a balanced budget as the deficit money can be borrowed or printed out of thin air. Hence, the national debt has grown steadily since 1971. How a fiat currency has affected our trade deficit, is more complex.

A fiat currency has gradually increased the cost of living and the cost of doing business. Here are a few difficulties American producing businesses face. The expansion in the money supply has created a real estate bubble, which is a negative for businesses looking to setup shop here. That means higher rent on the property. Second, because of inflation, the cost of labor has risen. Third and on a macro scale, massive growth in government has occurred (inflation is a cause of this) thus causing more regulation of business. Essentially, a fiat currency, enabling inflation, has made it more difficult for American producers to compete with emerging nations. These emerging nations offer cheaper labor, favorable tax laws and less regulation because they are hungry for economic growth. Thus, American manufacturing and large service companies have either closed operations or moved them abroad.

Pundits state that the dollar needs to decline more for the trade gap to decrease. Since the dollar began its secular decline, the trade gap has actually grown larger. If the dollar falls another 30% will that suddenly boost our manufacturing sector and the products we export? How can that be the case when businesses have closed up shop and moved? The evidence is already there that the deficit is a problem of a larger magnitude that has little to do with short-term currency relationships. Seeking to solve the problem, some of our supposedly enlightened politicians are hungry for protectionist legislation to spur our exports. This of course would penalize our trading partners, (like China) who happen to hold most of our debt. And, as Peter Schiff recently wrote, “What (industry) is left to protect?”

The reality is that inflation has gradually made it far more difficult for the average American business to compete against the emerging economies of the world. The inflation of the past 35 years has gradually destroyed the real and the productive economy of America. A further fall in the dollar is not going to help our deficit. It will make the deficit worse as has happened in the past several years. After all, a falling dollar is a form of inflation. How can the supposed solution help when it's an actual cause of the problem?

THE GOVERNMENT AND THE PRIVATE SECTOR'S SHARE OF THE ECONOMY

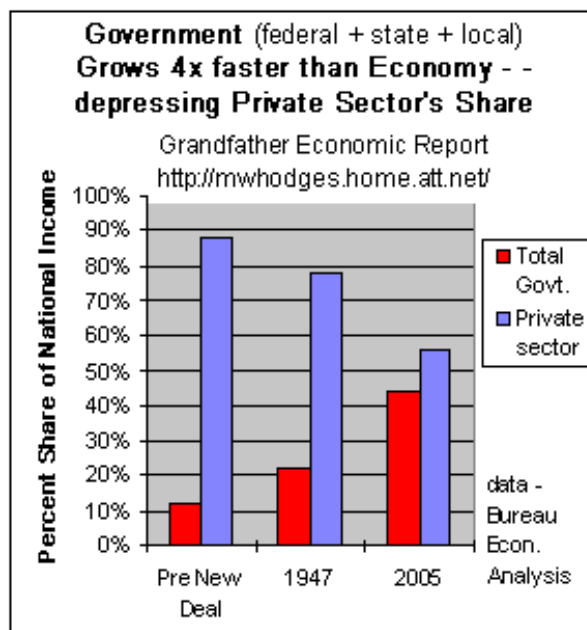
Prior to the Great Depression, the American economy flourished under the Gold Standard. By the early 20th Century, the US economy had become the strongest in the world and led the US on the path to becoming the world's superpower. It was almost entirely the leadership of the private sector that drove America to unseen economic heights. In a gold standard system, the government cannot spend

fruitlessly or into deficits unless it has an increase in gold to account for an increase in spending. Therefore it is entirely the private sector that drives an economy.

Since FDR expanded the role and size of government under the leadership and advice of John Maynard Keynes, the government's share of the economy has constantly increased. Keynes' ideas bridged what was once an impenetrable wall between government and the free market economy. Since FDR's implementation of Keynes's ideas, the US government has consistently increased its role in and control of the economy.

Regarding the effects of Keynesian policy, Jim Puplava writes²:

Following Keynes' views has transformed this country from the world's largest creditor to history's largest debtor nation. We have gone from a country that saves, invests and makes things to a country that borrows, spends and consumes. When we first embarked on this present course of action, another book appeared by F.A. Hayek called "The Road to Serfdom." When the book first published in 1944, it inspired as well as infuriated the politicians and scholars of the day. In 1944, the Labor Party ruled Britain and in the US, the Roosevelt Administration favored the path towards socialism. Eleanor Roosevelt even supported the economic programs of Joseph Stalin. "The Road to Serfdom" challenged these views and warned of the dangers of states' control over the means of production. "The Road to Serfdom" stands to this day as a warning over the dangers of collectivist thought and a serious meditation between individual liberty and government control.



² Jim Puplava, <http://www.financialsense.com/editorials/fso/021103.html>

Today the US government comprises almost half of the US economy. As a result of a half century of increased government spending and regulation, the average middle class family is overburdened with taxes, inflation, state taxes, state fees, and ever rising costs of life's necessities such as energy, food and healthcare. A century ago when America became the world's economic superpower, the average family thrived as the cost of living was far less. Moreover, such was the case during a period of little government and essentially zero government programs. If one compares the government's share of the economy prior to the New Deal versus its share today, they would conclude that America is now a socialist nation. Moreover, in the coming years, the trillions in Medicare and Social Security obligations will render an even larger share of the economy to the government. How can this current situation, consisting of growing deficits, debt, liabilities and government ever resolve itself?

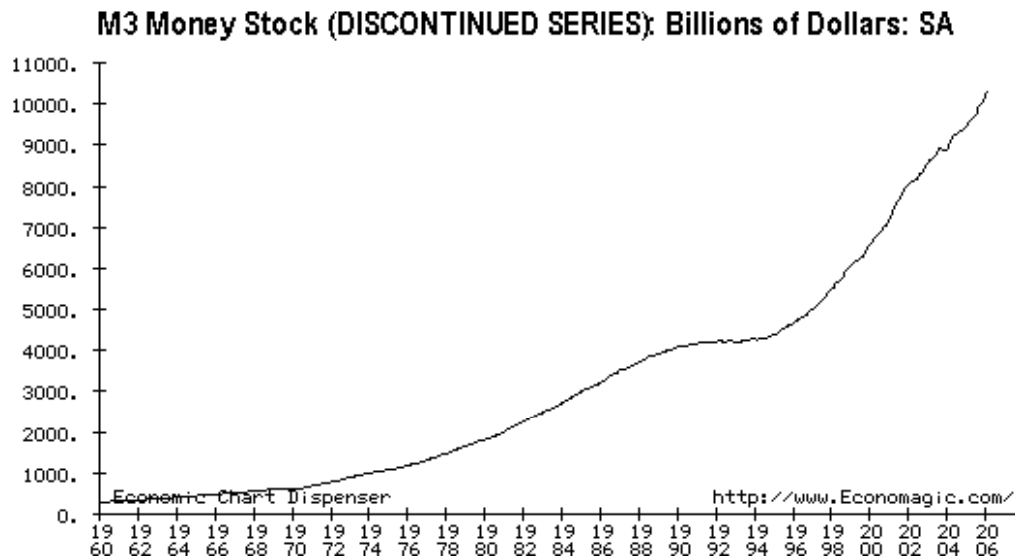
INFLATION OR DEFLATION

Economic booms become bubbles when the credit and money supply continues to expand (towards the end of a boom) in order to take advantage of the never-ending boom. Bubbles peak precisely when confidence becomes manic and investment behavior turns purely speculative. There are two ways and only two ways that a bubble bursts. One is through deflation. The money supply contracts as investors, businesses and consumers default on debts and liquidate losses or even gains in the face of declining consumer confidence. Think of deflation as debt liquidation on a large scale. The most notable deflations occurred in Japan in the 1990s, and in the United States in the 1930s, 1838 and after the Civil War.

The other way a bubble deflates is through hyperinflation. More money is created (by government and/or central banks) to stave off the inevitable collapse and liquidation (deflation) of credit and money. As debt builds up, the deflationary forces grow stronger, forcing greater and greater growth in money and credit to prevent deflation. Furthermore, subsequent inflations need to be larger (due to a natural currency decline) just to match previous rounds of inflation. Eventually the hyperinflation reaches its peak when the currency has lost all value or when the government decides to back the currency with something tangible. Think about blowing air into a balloon. Think of the balloon as the economy and the air as the money supply in that economy. Eventually adding too much air causes a complete bursting of the bubble, in which the air becomes worthless. Then, a new foundation has to be set for a new form of money (air). In deflation, as the economy reaches its boom/bubble peak with high debt (full size of the balloon), money (air) and debt starts to contract, thus causing the size of the economy (balloon) and economic activity to shrink considerably.

Newton's third law can be applied to inflation. For every action there is an equal but

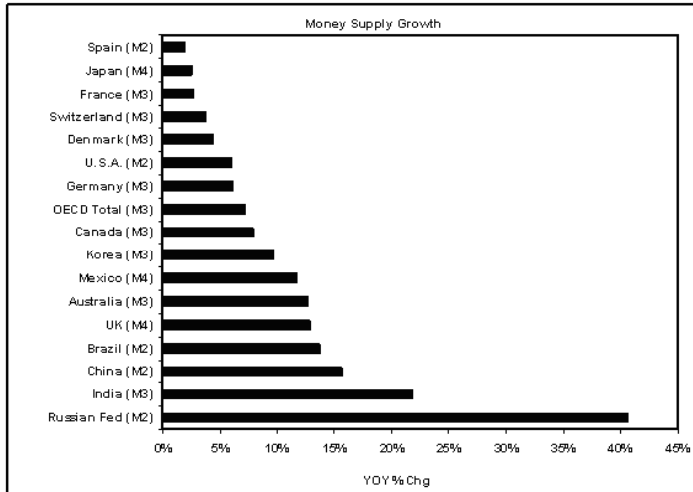
opposite reaction. Inflation is fundamentally a man-made action and its reaction is deflation. However, man can prevent deflation, but only through accelerated inflation. Does American monetary policy favor deflation or hyperinflation? What does this chart, of M3 Money supply tell you?



INFLATION IS NOW A GLOBAL PROBLEM

Yes, money and credit growth is excessive in the United States, but it doesn't end there. Money supply in Canada, the UK, Europe and Australia is growing annually at or near double-digit rates. Money growth in China and India is nearly twice that. Take a look at this chart that details, by country, money supply growth³.

³ Tony Allison/Bloomberg,
<http://www.financialsense.com/Market/allison/2007/0402.html>



For the first time in world history, every country is operating with a fiat currency. This is incredibly dangerous as there is little protection against the ravaging of savings and earnings by governments and central banks. Fundamentally, the various currencies are all the same. The Dollar, Yen, Euro, and Yuan are all pieces of paper that derive their value from public acceptance and government enforcement. Governments and central banks are playing a tricky game, a confidence game with the public. More dangerous, is that they are tempting the time-tested laws of economics. The price of gold, silver and all commodities will explode in all currencies if and when the market decides there is too much money in the global financial system.

WHERE WE ARE AND WHERE WE ARE HEADED

From 1949 to 1982 (34 years) we had eight recessions. Since then we have just two recessions in 23 years. Most would say that is the result of such a strong economy. It's entirely the result of our fiat monetary system that allows for unabated and unchecked expansion of money and credit that can postpone recessions. Marc Faber explains⁴:

"In the American school, the downturn is postponed through monetary measure. In other words, the capacity that never gets cut back, because if you ease massively, you don't create an environment of the survival of the fittest, but you create an environment of the survival of the weakest. Even the weak market participants, continue to produce, especially if they go into Chapter 11, because then they don't have to pay any debt payments, and therefore, they can undercut the other. That is why the American school, in my opinion, in the current situation, has policies that will then lead to a prolonged recession at the later stage."

⁴ <http://www.valuestockplus.net/2007/03/investment-nuggets-by-marc-faber.html>

By constantly increasing the credit and money supply, policy makers can postpone the natural recession but at a long-term expense. Recession is healthy and necessary as it bolsters the entire system by cutting the weak and the fat while allowing only the strong and efficient to survive. The economy is then stronger in the subsequent expansion. Postponing recession allows for imbalances to grow to unhealthy and unnatural levels. Moreover, over time it threatens the sustainability of the system. In our case, yes we have only had two recessions in the past 23 years but as I will list later, many negative things have developed in the process.

Quite simply, there is not much more room for the Fed to postpone recession without pushing this country into an unavoidable hyperinflation. On the other hand, if the Fed were to contract the supply of money and credit like they did in 1929, it would bring about the worst deflation in modern economic history. Total credit market debt as a percentage of GDP now exceeds that of 1929. In 1929, this country was self sufficient in energy, manufacturing and capital. Today we import most of our energy, inflation has destroyed the manufacturing sector and finally, we are history's greatest debtor.

Unfortunately, the majority of the American populace is not aware of the situation. This is because since the Great Depression, Keynesian economics has completely dominated the American educational system. Most citizens, politicians and Wall Street professionals would tell you and believe that we have a free market economy. They have been educated to believe that government involvement and central bank involvement is part of a free market economy. In the same vein, Americans who adhere to the free market Austrian economic principles that the founding fathers espoused, admit they didn't learn these laissez-faire principles in school. At this juncture, our monetary policy and entire monetary system is on its last lifeline. The current long-term trends and outcomes of our overall policy is clear:

- A currency that consistently loses purchasing power
- A negative savings rate
- Skyrocketing national debt
- Declining balance of trade
- Perpetual budget deficits
- Excessive taxation (income tax, sales tax, estate tax, property tax, gas tax)
- Loss of economic liberty
- Loss of most competitive industry
- Widening inequality
- High stock prices

- High real estate prices

A sustainable economy cannot be built on rising asset prices. Savings are necessary for consumption and productive investment. A stable currency is imperative so that savings can be accumulated and purchasing power maintained. Low taxes are needed to encourage work, production and investment. A balanced government budget is needed to maintain a stable currency and thus limit inflation. Overall, the post Great Depression economic policies of our nation have destroyed the free-market economic foundation America was built on.

CONCLUSION

A fiat currency has allowed the policy makers to pursue an inflationary monetary policy and it has allowed the government to run large budget deficits for decades. This has resulted in epic deflationary forces that recently have been counteracted by increased inflation. This policy, over time has damaged the real goods producing economy while giving rise to a financial economy that consists of paper transactions, non-exportable services and asset price bubbles, which creates the illusion of economic strength and health. Until the 1970s, expansion in money and credit stimulated the real economy, resulting in technological breakthroughs and consistent increases in productivity and the overall standard of living for all Americans.

In 2001 when the economy was early into a deep recession, the government and the Federal Reserve intervened strongly making money and credit abundant and cheap. Through debt consumption and deficit spending GDP has pushed higher, despite rising price inflation and limited capital investment from the business sector. This heavy stimulus has served to exacerbate the troubling imbalances as well as further tarnish the remains of the real economy. While the headlines have not stated it, the economy is in a recession and has been for much of this decade.⁵ The underreporting of inflation has disguised, what has been a stagnant economy since 1990. Tax receipts, although growing, are severally lagging government spending. In turn, the national debt is skyrocketing each month. And because of the inflation of the past 30 years, American business is faltering behind the emerging economies of the world. Moreover, we soon must deal with the tens of trillions of dollars in unfunded liabilities (Medicare, military/government pensions, social security) that the government must pay. According to USA Today⁶, these liabilities will come due very soon:

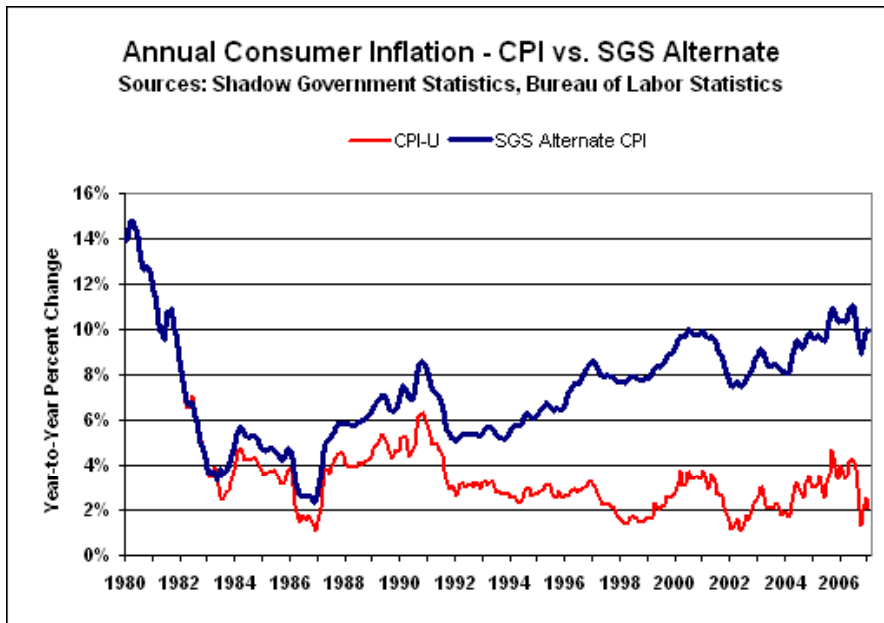
⁵ W. John Williams- Shadow Stats, <http://www.shadowstats.com/imgs/sgs-gdp.gif>

⁶ USA Today, http://www.usatoday.com/news/nation/2004-10-03-debt-cover_x.htm

“Big payments on the debt start coming due in 2008, when the first of 78 million baby boomers — the generation born from 1946 to 1964 — qualify at age 62 for early retirement benefits from Social Security. The costs start mushrooming in 2011, when the first boomers turn 65 and qualify for taxpayer-funded Medicare”.

Current and future fiscal and monetary policy is quite clear. To avoid a deflationary depression, we will continue to create new money to monetize our debts and to keep economic activity from reaching a standstill. In the coming years, to meet the entitlement demands and the budget gap, monetary expansion will have to accelerate rapidly. All indications point to Fed Chairman Ben Bernanke following Alan Greenspan’s easy money policy and leading us to hyperinflation.

The government and Federal Reserve have already spent the last 15 years laying the groundwork for an accelerated expansion in the money supply, while deceiving the public as to the real level of inflation. Since the early 1990’s the government and Fed have taken several steps to artificially lessen the outcome of the CPI (consumer price index). These steps include seasonal price adjustments, substitution of goods, geometric weighting of the index and hedonics. The result is shown below in a chart from W. John Williams’ “shadowstats.com” which shows today’s CPI against its outcome based on its original calculation.



Even more recently, the policy makers have taken two more steps to alter the public’s perception of inflation. With the CPI creeping up, they developed a “core CPI” index that essentially removes things that show inflation, such as food and energy. The media and Wall Street now refer to “core CPI” when judging inflation. Last and

most important, the Fed did away with the reporting of M3, the broadest and most accurate gauge of money supply. Would there be any other reason why the Federal Reserve abandoned the reporting of M3, then to prepare for even higher rates of money creation?

The coming hyperinflation will be so powerful and widespread that money will make its way into everything: Commodities, Stocks, Real Estate and consumer prices. We have already seen the start of this, as every asset class has risen handsomely since 2002. Folks, that is a powerful warning sign that hyperinflation has already begun. Ultimately, commodities will be the only investment that maintains "real" value. Don't be deceived by the rising market indices as they are falling dramatically against real money (gold and silver).

The troughs in the Dow/Gold ratio occurred at the following prices and in the following years: 1.01 in 1896, 2.01 in 1932 and 1.04 in 1980. History mandates that this cycle will end when Gold's price is at least 50% of the Dow. Considering that the Dow is at 12,000, one can understand the large scope of the American inflation and realize the extreme magnitude of the adjustments that lie ahead. Gold's rise from \$250/oz to over \$700 is only a fraction of the rise that awaits us. Today's Dow mark would put the next peak in gold at a minimum of \$6,000/oz.

That may sound extreme but not if you consider the array of driving forces. First, bull markets always run to the extreme. Second, the size of the gold market is currently miniscule relative to the size of the entire stock market. Third, despite over a 150% rise in the price of gold, gold mine supply is running woefully short of demand. South Africa, the top gold mining country, just reported that its gold output was at a 74 year low! Australia, the third largest, reported that it's 2006 production was at a 13 year low! The bear market of the 80s and 90s decimated this industry in terms of resource development and talented people. Fourth, there is no indication that this market is anywhere close to being saturated in terms of investors or investor funds. Joe Sixpack has no idea what is going on and even most educated professionals are oblivious to gold's bull market. Fifth, the price of gold increased 25.3 fold from 1971 to 1980. Using the bottom in 1999, that would put gold at over \$6,000 an ounce. If there was ever a time and situation to be buying gold and silver with reckless abandon, now is it!

The engine of the gold train is revving. Will you be aboard?



WHAT WILL BE THE AFTERMATH AND RAMIFICATIONS?

That is up to all of us Americans. Today, our economy is a mixture of free market capitalism, socialism (welfare, entitlement spending) and fascism (central bank, big corporations in bed with the government). Which way will it drift? Contrary to what one might think, the gold bull market will go a long way in restoring a solid and constitutional economic foundation. Gold is pure. It is money, freedom and liberty. While all fiat currencies ultimately encounter the same fate, gold and silver as real money has stood the test of history. The most basic element of commerce is a stable medium of exchange. If an economy's form of money isn't sound what will happen to the economy? What would happen to airplanes if we built them with cardboard?

It is true. We do not have free money nor do we have a free banking system. Rest assured, the flight from paper assets to hard assets will gradually expose both fiat currency and the Federal Reserve System for the frauds they are. In the process of hyperinflation, both the Fed and the government will destroy themselves in trying to prevent what they have made inevitable. I fully expect the dollar to be backed by some combination of gold and silver and the duty of handling the nation's money to be returned to Congress as was intended by the Constitution. These developments,

among others, would help refurbish a previously defaced economic infrastructure and ultimately lay the foundation for 21st century economic success.

Undoubtedly the path to economic reconstruction will be an extremely difficult and turbulent one. In the coming years, as more and more individuals move their money away from government paper to sound money, the government and Fed will be exposed for their excessive roles in a free market economy. Consequently, this will lead to an array of political and social problems. Unfortunately, the undereducated, misinformed, disadvantaged and underprivileged will become victims as they lack the means and resources to protect themselves from the massive economic and social displacement that is on the way.

Furthermore, the voting public and the government are extremely deficient in their understanding of our economic problems. They are ill equipped to offer insight and the necessary solutions that will reform the system. When the crisis hits, it will be exacerbated and lengthened, as the public and government will misdiagnose the causes. Few understand money, gold and our current monetary system. Like the Great Depression, most will blame the problems on the free market, while not realizing that what once was a free market system has been considerably altered, tinkered with and corrupted since 1913.

Is it a coincidence that since our monetary system has evolved, most facets of American society have declined in tandem with the purchasing power of the dollar? American education used to be the best in the world, now it is falling. 21% of our adult population is functionally illiterate. American culture used to be revered, now it has become a mindless charade, over obsessed with meaningless celebrity. Forty years ago the American family thrived as a single high school graduate's income was enough to support the entire family. Foreigners once admired America as the beacon of liberty, freedom and free markets, though all have been gradually eroded in the wake of the American inflation.

The American inflation has also produced a decline in the respect and civility towards our fellow man. This is even shockingly apparent in the financial industry. Peter Schiff of Euro Pacific capital is one of the very few outspoken individuals who appear regularly on the various programs. On CNBC, Schiff recently spoke with host Mark Haines. Haines' behavior and treatment of Schiff (because of his bearish views) was appalling. This is not limited to CNBC. On a recent appearance on Fox News' Bulls and Bears, Schiff was the lone bear. When he gave his case, everyone else on the panel laughed. I thought the name of the show was Bulls and Bears? Nevermind that Schiff's views were absolutely correct on both accounts.

The previous paragraphs illustrate how the ramifications of inflation extend well

beyond the financial and economic sphere. Ironically, the word inflation engenders a thought of something growing, rising and getting bigger. In reality, inflation is about erosion in value. The value of the currency decreases and you are getting less than you did before. Consider the government. The "value" of the services it provides has declined considerably in tandem with the buying power of the dollar. Recent history is a powerful indication that government ineptitude is a consequence of inflation. Just think of the 2000 election, the Iraq War, Katrina and the poor treatment army veterans get. Need I say more? Ultimately, a devalued currency leads to devalued morals, values, behavior and a devalued society.

Those that understand and prepare for the drastic changes headed our way will grow wealthy and prosper in more ways than one. Those that ignore the warning signs and rely on the status quo will do so at their own peril. While this editorial carries a negative tone, there are several important positive insights I can offer. As Doug Casey says, the longest running trend is the ascent of man. While there are always peaks and valleys, life and the standard of living usually improve from generation to generation. Secondly, the government is not the same thing as the country. Governments come and go but nations, states and peoples remain. Finally, after the coming Depression runs its course, American assets and factors of production will be cheap and a tremendous value given the right political climate. The majority of Americans who emerge from the coming crisis will have done so because of true American values such as sacrifice, self-reliance, responsibility and hard work. It will be the lasting values of such people that ensure America's economy and monetary system are reshaped to reflect true free market principles.

In closing, I would like to leave you with four quotes about inflation. These four quotes are all you need to remember concerning the dangers of inflation and why and how such dangers will be realized in the coming years. Read the first three and pause before you read the last quote which, I should add, is incredibly naïve, absurd, and outright dangerous.

"The trifling economy of paper, as a cheaper medium, or its convenience for transmission, weighs nothing in opposition to the advantages of the precious metals... it is liable to be abused, has been, is, and forever will be abused, in every country in which it is permitted."

-Thomas Jefferson

"Lenin is said to have declared that the best way to destroy the Capitalistic System was to debauch the currency. . . Lenin was certainly right. There is no subtler, no surer means of overturning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which not one man in a million can diagnose."

-John Maynard Keynes

“In the absence of the gold standard, there is no way to protect savings from confiscation through inflation. There is no safe store of value. If there were, the government would have to make its holding illegal, as was done in the case of gold. If everyone decided, for example, to convert all his bank deposits to silver or copper or any other good, and thereafter declined to accept checks as payment for goods, bank deposits would lose their purchasing power and government-created bank credit would be worthless as a claim on goods. The financial policy of the welfare state requires that there be no way for the owners of wealth to protect themselves. This is the shabby secret of the welfare statist's tirades against gold. Deficit spending is simply a scheme for the "hidden" confiscation of wealth. Gold stands in the way of this insidious process. It stands as a protector of property rights. If one grasps this, one has no difficulty in understanding the statist's antagonism toward the gold standard.”

-Former Fed Chairman Alan Greenspan in 1967

“But the U.S. government has a technology, called a printing press (or, today, its electronic equivalent), that allows it to produce as many U.S. dollars as it wishes at essentially no cost. By increasing the number of U.S. dollars in circulation, or even by credibly threatening to do so, the U.S. government can also reduce the value of a dollar in terms of goods and services, which is equivalent to raising the prices in dollars of those goods and services. We conclude that, under a paper-money system, a determined government can always generate higher spending and hence positive inflation.”

-Current Fed Chairmen Ben Bernanke in 2002

Hyperinflation may only be a few years away.....



Special Thanks to the following sources for charts/data/cartoons:

- John Williams, Shadowstats.com
- Economagic.com
- Michael Hodges, Grandfather Economic Report,
<http://mwhodges.home.att.net/product.htm>
- Cartoons by CustomCartoons.net

THE END