The US seems to have learnt nothing from Japan's economic mistakes!

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"Data raise fears over faltering economy," says this morning's *Financial Times*.

What a surprise! What happened to the recovery?

The Dow fell again, Gold witnessed a correction of $39 also fortunately I had already taken profits in gold for RIO Professional investors fund.

Why would gold go down? Because people are finally realizing that deflation is the real risk, not inflation. Gold could continue to slip and slide, it's hard to say. It can rise in a deflationary cycle, but it depends on how volatile and uncertain the markets appear. In a stable, Japanese-style slump, gold could go down.

We could see all kinds of fluctuations before this crisis is over. Deflation. Inflation. Stagflation. Hyperinflation. You name it, what a shambles!

The latest news from the US shows that unemployment has increased. Treasury bonds are trading at their highest point in 14 months. In case members do not know, currently a 10-year Treasury note yields just 2.93%.

Facts are facts, the Fed cannot really make bad debt just go away! All they can do is move it around. The parties to a transaction - creditors and debtors - usually decide among themselves who bears which losses. Typically, if a debtor cannot pay, the creditor loses his money. However, when the Fed step in almost anything can happen, but history shows that usually it is not good news.

The general government plan is to collectivize losses - either by moving them onto the taxpayers or by moving them onto the general public. Mostly when governments borrow money to fund their bailouts, for example, this involves taking losses away from the people who deserve them and placing them on the taxpayers. It is that simple!

With a little consumer price inflation that makes it look even better. Then losses seem to disappear into the air and the public does not know what to think or whom to blame.

Today, some economists favor sticking taxpayers with the losses. Others are squarely against it, preferring to force the losses on the general public by means of inflation.

My opinion is that the trouble is that any of these plans tends to have unanticipated consequences.

A look at the Japanese's bailout version

The Japanese version of the US Fed approach really took the biscuit, in this regard. They borrowed from their own people in order to fund a 20-year bailout program. The idea was to provide counter-cyclical stimulus. Naturally, the stimulus never seemed to stimulate anything but more stimulus! The program went on for two decades and the Japanese economy is still limping along.

The effect that economists did not anticipate was that the economy did not take off. Instead, there followed two decades of on-again, off-again slump, which is why it would have been better to let the creditors and debtors resolve their problems on their own. In other words, they would have been better off taking their losses back in 1990 and be done with it!

Another unanticipated result will soon be fully realized, in my opinion. The government took savings from Japanese households and spent them, which is far more serious. A whole generation of Japanese old people looked to government bonds as the source of its retirement wealth. The fact is that there is no wealth there, which is a very ugly picture.

The Japanese version of the Fed took credits and turned them into debits; they took the surplus wealth of an entire generation and squandered it. Today, instead of looking to stored-up wealth for their retirements, older Japanese have to hope that the next generation will be kind and able enough to keep up with the debts laid upon them.

The trouble is that the next generation has too much debt to carry. Japanese Government bonds that are outstanding equal nearly 200% of GDP. At zero interest rate, it's not too hard to keep up with the interest payments. But even the Prime Minister is beginning to wonder how those debts will ever be repaid. I would suggest that interest rates will not stay low forever.

Imagine that inflation rose and that investors got nervous. Imagine that the carrying cost of that debt rose in Japan as it did in the 1970s in the US. At 10% interest, the cost would be one fifth of GDP or about as much as the entire government budget. I believe that the system will first fall apart leaving Japanese retirees with very little money, and that paints a dismal scene!

William Gray

The RIO Club