

System in Liquidation Panic; Time To Talk Physical Economy

by John Hoefle

Dec. 5—The bailout, as presented, is addressing the wrong problem by the wrong methods, and is making the situation worse, not better.

Caught in the grip of an accelerating panic, the financial world is demanding that the world's central banks and governments turn on the printing presses and flood the system with money, far beyond what they have already done. It's not working, they scream, so we need more, more, more!

At the same time, the so-called real economy is in a tailspin, with jobs declining at record rates, industries collapsing, state and local governments facing growing budget deficits, home foreclosures soaring as prices fall, and a holiday shopping season showing every sign of being a disaster for retailers. The news is bad everywhere, so bad that the official announcement that we entered into a recession a year ago seems almost like comic relief. Almost—because the situation is deadly serious.

Why, despite the trillions of dollars thrown into the financial system over the past year, does the economy continue to collapse? Could it be that the approach we are taking is fundamentally wrong? Treasury Secre-



EIRNS/Will Mederski

The triumvirate of (left to right) Ben Bernanke, Hank Paulson, and Chris Dodd, have unleashed the power of the Fed's printing press, which, Bernanke claimed, in 2002, "allows [the government] to produce as many U.S. dollars as it wishes, at essentially no cost."

tary Henry Paulson and other luminaries insist that the bailout policies are working, that we just have to give them time, but the results do not match their assertions.

As we have repeatedly shown, the so-called "housing correction" which Paulson insists is the root of the crisis, was caused by the banks, which used mortgage debt as fuel for the derivatives bubble. It was the derivatives bubble which blew out, taking the mortgage market with it.

More importantly, the attempt to resolve the crisis by throwing money at it is fundamentally incompetent. No purely financial solution is possible, no matter how

much money we print, for the solution lies in the realm of physical economy. If we are to survive, we must change the discussion to physical economy, and the rebuilding of our infrastructure and productive base, using new physical principles.

Liquidation

The continuing collapse of the financial system, which seems constantly to take the “experts” by surprise, is entirely consistent with the statement by Lyndon LaRouche, at his July 25, 2007 webcast, that the financial system had died. Under this Anglo-Dutch Liberal monetary system, the productivity of the global economy was systematically dismantled, national economies replaced with the imperial system called globalization. The United States, as the world’s leading industrial power, was particularly targeted, its scientific and technological capabilities, its manufacturing base, and the infrastructure painstakingly built up over generations, abandoned, in favor of the false promise of finance and the information age.

Once the most productive nation on Earth, we became a nation of borrowers, going deeper into debt with every passing year. As the debt grew, the bankers moved it into a virtual off-balance-sheet world, where speculation reigned. The result, over the years, was the growth of that multi-quadrillion-dollar abomination known as the derivatives market, a market which blew up in mid-2007, and took the global financial system with it.

We are now witnessing the death of that entire system, as banks, hedge funds, and others, frantically attempt to save themselves from the ramifications of that 2007 event. The kings of Wall Street, the giant investment banks, are all gone, either through failure, merger, or conversion to bank holding companies; and the collapse is spreading through the rest of the system, the hedge funds, private equity funds, the money market funds, et al.

The system itself is being liquidated, a huge pyramid scheme which has failed. The financial instruments that were once treated as if they had great value, have been revealed to be worthless.

FIGURE 1
U.S. Unemployment Rate, Jan. 1, 2000-November 2008
 (Percent)



Source: U.S. Bureau of Labor Statistics.

Printing Presses

The holders of these worthless instruments, however, are not going quietly to meet their fate. Instead, they have demanded, and received, huge bailouts from the governments, and the people. It is the largest transfer of wealth in history, the biggest swindle ever—but still they want more.

The British are leading the charge, calling for the central banks to “print” as much money as required to cover the losses. They know full well that such actions would create a hyperinflationary explosion, but they don’t care. They want their money, and they want it now. The good folks at HSBC, the bank that says we need a new Hjalmar Schacht, is openly demanding that the presses be fired up, and that the Fed begin buying corporate bonds, in addition to mortgage-backed and asset-backed securities. The London *Economist* has demanded an end to the supposed “cautious incrementalism” of the bailout, as if \$8 trillion in

one year was not wildly insane already.

In the United States, the Democrats are discussing a new stimulus in the \$500 billion range, with some economists calling for \$1 trillion or more. Federal Reserve chairman Ben Bernanke, long a believer in the printing press approach, gave a speech Nov. 21, 2002, to the National Economists Club in Washington, in which he noted that “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,” and can always defeat deflation by creating money. “Injections of money,” he said, “will ultimately always reverse a deflation.”

Under the Emergency Economic Stabilization Act, Treasury has created a “Systemically Significant Failing Institutions Program,” in the hopes of stopping the failure of any single institution from triggering a chain reaction collapse.

At this point, the Fed and the Treasury are keeping parts of the system functioning on life-support, but they are losing ground, as the damage spreads far beyond their ability to contain it.

Carnage

The pending collapse of the domestic auto sector, led by claims that General Motors will not last the month without a government bailout, is just the most dramatic element in what is a widespread economic collapse. Roughly half of America’s companies have credit ratings below investment grade, a polite way of saying junk.

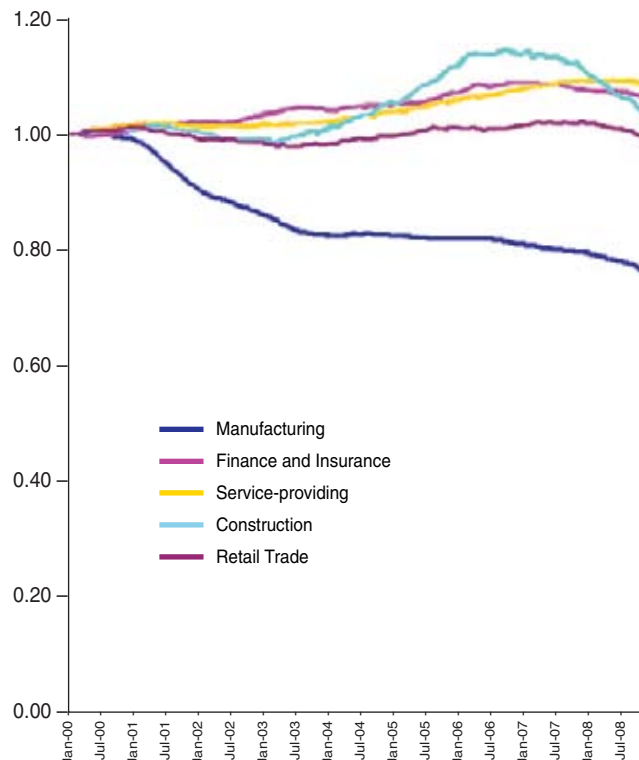
The wreckage of the economy is also reflected in the employment figures released today by the Federal government, which show unemployment skyrocketing **Figure 1**, and jobs falling across a large spectrum of the workforce **Figure 2**. The employment numbers are notoriously massaged—the true unemployment rate is about double the official rate—and the categories are routinely adjusted to hide the collapse of manufacturing employment, but even so, the official numbers show a disturbing trend. The economy is in free fall.

As employment falls, home foreclosures will rise even faster, as will defaults on credit cards and other household debts. This will cause further losses to the banks, who will restrict credit even more, which will cause further job losses, and on and on, in a vicious death spiral.

The attempt to solve this by printing money will not

FIGURE 2
Manufacturing Leads U.S. Employment Collapse, 2000-08

(Indexed to January 2000 = 1.00)



Source: U.S. Bureau of Labor Statistics.

stop the deflation of financial “assets,” but will trigger hyperinflation; and the lunatic calls for what amounts to unlimited money will destroy the dollar, and what is left of our economy.

There is a way to stop this collapse, but it involves letting go of the illusion that the funny money can be saved, and taking the discussion out of the realm of finance, and into the realm of physical economy. We cannot save, and must not try to save, the fictitious values of the derivatives market, and of all the securities it made possible. Instead, we must turn our attention to saving people, by protecting the essential elements upon which human life depends. What good is a derivative, when you have no food or electricity?

We must stop this insane bailout while we still can, before the hyperinflation destroys the dollar. It can still be avoided, if we put reason ahead of greed, and humanity ahead of money.

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