Weep For America

By The Mogambo Guru

12/08/03 The inevitable wages of America's staggering macroeconomic sins: the death of the Dollar Standard System.

GDP went up by 8%? Big deal! I laugh at anyone who thinks this is good news. It is not. Eight percent of a ten- trillion dollar GDP is $800 billion dollars. More than that has been borrowed and spent in the last year by the federal government alone. And when you add in all the other debt that has been assumed in the last year, a lousy $800 billion in GDP is nothing!

And Richard Benson of Specialty Finance Group is one of those guys who is, apparently, not being driven insane by the staggering macroeconomic sins that have been committed over the last, oh, let's say, sixty years or so. Instead of gobbling down handfuls of tranquilizers and laboring under the strain of constantly lugging around caches of weapons and ammo from room to room, ceaselessly checking and re- checking perimeter defenses, and all the while muttering to himself about vast conspiracies, he is able to calmly rattle off a litany of relevant statistics known around these parts as Numbers That Destroyed The Tranquility Of The Mogambo, And Turned Him Into Some Kind Of Trigger-Happy Paranoid Whacko.

For instance, the current market price of stocks is $10 trillion, down from the peak of $17 trillion, indicating that you need a 70% gain just to break even. Man, it makes you wonder how in the hell "buy and hold" ever got to be popular!

Benson also writes that "Credit market borrowings are approaching a pay-off balance of $34 trillion. With the U.S. Treasury running $500 billion deficits a year and the single family mortgage market still growing at a rate of over $600 billion a year."

Richard Benson: Owning Someone Else's Liabilities

My eyes are glazing over, and if you look closely you can detect a small trickle of spittle at the corner of my mouth, which seems to be ominously tinged with blood.

Benson goes on: "In our economy, the vast majority of financial assets are nothing more than the ownership of someone else's liabilities. The current total market price of financial assets (liabilities) is certainly over $47 trillion, or four times GDP. The cash flows from our $11.8 trillion economy will not support payments on this level of liabilities."

Since interest rates are surely about as low as they can go, opines Benson, then the price of bonds is also surely about as high as, and maybe this is just me reading things into his words that he never meant to say, they will ever be again for as long as you are alive, or your children, which means that if you are buying bonds, then for the rest of your life you will never again see prices this high, and you will forever curse yourself for having bought them, and your children will soon find out that you squandered their inheritance, and THEY will also live their whole lives in squalor and never see debt prices this high again, and so they will spend the rest of their miserable lives also cursing you, because maybe they could have been spoiled little rich brats who inherited a fortune from you, but nooOOOOoooo, they get a fistful of worthless bonds, which you seemed to have bought at the exact high.

The Fed is holding down interest rates on short maturities to less than 1%, making it painful to hold cash. Therefore, the impetus to get cash "working" has led to a liquidity-driven rush in stock prices, so that P/E levels are, to use Benson’s phrase, up to "1929 levels." And as for what the phrase "1929 levels" means, he explains: "This has propelled stock prices to inflate to extraordinary levels given all logical means of measuring value."

Richard Benson: Losing Another 30%

Benson and I agree that all of this means the dollar will lose another 30% in value, which I also say would seem to indicate that gold must also go up by 30% in terms of dollars. The only way that this would NOT happen is if foreigners, whose currencies are appreciating against ours, decide that the price of gold is too high, and everybody decides to sell their gold holdings, driving the price down in their local currencies. Only thus, and I love it when I use the word "thus" for some reason, would gold not go up in price, in dollars, by at least 30%.

Getting beyond that, I think that a 30% devaluation in the purchasing power of the dollar is entirely achievable, if that is the term that one uses to describe such a catastrophe, and I have a hard time conceiving that all foreigners would suddenly decide against owning gold and instead elect to invest in dollars, especially when considering the economic ramifications of what is happening today.

Fortunately, I know that you will proudly stand with me, linking our arms in solidarity, and together we can loudly express our hope that we can continue to count on OPEC and all the other petroleum exporters, who are willing to not raise their price of oil when the price and value of a dollar falls. Then we fall to our knees and say "Thank you! Thank you! Thank you!" Because man, oh man! A thirty percent increase in the price of crude oil, which would only exactly offset the fall in the purchasing power of the dollar, puts it at $40 per barrel! So what does that do to the price of, you know, a gallon of gas at the pump, huh?

All this is inflationary, which is The Thing That Is To Be Feared, according to that loudmouth Mogambo, which is me. As Mr. Benson says, "Beef prices are at a 24-year high and insurance, education, health care, property taxes, and many other day to day expenses make the CPI a joke."

Richard Benson: Owner-Equivalent Rent

Furthermore, he exposes the fraud of "owner-equivalent rent," which is keeping the official inflation statistics artificially down. "The CPI assumes every one rents, even though 65% of households actually own their homes. Rising home prices are not in the CPI but the declining cost of renting a home is. (Rents are weak and many people are opting to buy, rather than rent.) Housing is 22% of the CPI." So, more than a fifth of the CPI does not reflect a dime’s worth of the gigantic double-digit explosion in housing prices. Fabulous.

He goes on to say, "The Federal Reserve wants inflation because only the rising prices of goods will help companies service their massive debt loads, and only rapidly rising wages and salaries will allow individuals to service their record debt loads as interest rates rise and inflation kicks in."

Abruptly, and this is the jarring part that made the ice cubes tinkle in my glass as my hand involuntarily shook at the startling revelation, and I think I spilled some in this keyboard here, judging by the sizzling and popping and that little shower of sparks, Mr. Benson zeroes in on the necessity of "rapidly rising wages and salaries." Rising prices is one thing, and that is bad enough, and I say this as a guy who is finding that he is paying higher and higher prices for damn near everything. But to have rising prices, at the same time as wages and salaries are NOT rising, is quite another, wouldn't you say? Well, whether or not you say, I say.

But the massive debt load, the service for which we need rising salaries, which we don't have, and won't have anytime soon, wouldn't even be possible if there wasn't someone silly enough to lend to us in the first place. Enter Asia. The Economist magazine writes, "Some, such as Peter Garber of Deutsche Bank, see Asia's official purchases of dollars as part of a grand bargain: Asia ploughs its savings into America, and America, in return, remains open to the products of Asia's export industries. But protectionist pressures rising in Congress raise worries that America may fail to keep its side of the bargain."

(Mogambo side note: America keep its side of a bargain? Hahahaha! For example, ask any Indian who has ever signed a treaty with the USA, and he will tell you we palefaces speak with forked tongue, and our treaties are a "Heap big pile of buffalo chips.")

But the real culprits aren't Asians in particular. It is the Foreign Central Banks – particularly Asian Foreign Central Banks – that are footing the bill. "The private foreign sector," writes Benson again, "realizes the only reason the dollar hasn't crashed is because the Foreign Central Banks are allowing speculators to take massive dollar short positions, while the dollar is 'eased down' in value."

Now, speaking for myself, if the foreign sector realizes this, then who is the big dummy who is taking the other side of the short position that is being taken by these speculators? Who is so dumb is to take the wrong side of a big bet that everybody sees coming?

Well, we are going to find out who, and pretty soon, too. As the dollar comes tumbling down.

Regards,

The Mogambo Guru,
For the Daily Reckoning

December 08, 2003

— Mogambo Sez: Nobody has ever argued that the government deficit-spending and all the rest of the heroic, last- ditch, pull-out-all-the-stops monetary excesses would not make statistics of economic activity blip upward. The argument is whether or not it will eventually destroy the economy. I say it does. The rise in the price of gold says it does. The decline in the dollar says it does. All of recorded economic history says it does.

The Fed and the talking heads of America say it won’t.

And it embarrasses me, the Mogambo, to have to be the one who has to say it, because I am a guy who is so stupid (audience shouts out "How stupid, Mogambo!") that restaurants refuse to serve me because my profound stupidity actually makes the food taste funny.

And now you know why I, too, weep for America, and why the food I eat always tastes, you know, funny.