THE FOLLY OF ECONOMISTS: NEGATIVE INTEREST RATES

The person nicknamed “Helicopter Ben”, because he said it would be easy to fight DEFLATION, even if it had to be done by throwing money out of helicopters, gave us ‘ZIRP.’ That means “zero interest rate policy.” Now he seems to be leaning toward ‘NIRP,’ “negative interest rate policy.” He is an economics professor now. We can only hope that his students do some outside reading, like Ludwig von Mises.

Jeff Cox and Katie Kramer of CNBC wrote this:

> Former Fed Chairman Ben Bernanke thinks policymakers should give serious thought to implementing negative rates.
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> "Since that can't be assured, and since the current low-interest-rate environment may persist, there are good reasons for the Fed and other central bankers to consider changes in their policy frameworks," he added. "The option of raising the inflation target should be part of that discussion. But … it is premature to rule out alternative or potentially complementary approaches, **including the possibility of using negative interest rates."**
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> "In the political sphere, the fact that negative rates would **be temporary** and deployed only during severely adverse economic conditions would be an advantage," he said. "Like quantitative easing, which was also unpopular in many quarters, a period of negative rates would probably be tolerated by **politicians** if properly motivated and explained."
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> *The full text of Bernanke's post is here.*

Note the word **“temporary.” As a wise man said a long time ago, there is nothing more permanent than a governmental “temporary” program.** Also note that he focuses on pleasing the politicians.

It is clear that central bankers are totally confused. They have no idea of the damage they have wrought in the global financial system. Over $13 TRILLION of government bonds are now yielding below zero, which means that the buyers have to PAY interest instead of receiving it. **That’s the first time in 5000 years of recorded world history.**

What can possibly go wrong? All these people probably have Ph.D. degrees in economics. They learned everything from text books.

During the hyperinflation of the 1920’s in Germany, money supply was growing slower than the rate of inflation. For example, when the inflation rate was 150%, but money supply might only have been growing at a 75% rate. The elite economists, in Germany called the “Herr Professors,” who are just a step below godliness, advised the government that money supply was growing too slowly and this would lead to a recession.

Therefore, the government let the presses run day and night in order to speed up money growth. As money supply growth accelerated, naturally so did inflation. But the economists didn't make the connection.

Because inflation was accelerating faster than money growth, the government confiscated private printing presses to print more money faster. At the end, they were using rubber stamps to make a "1 million Mark" into a note worth "1 Milliarden Mark" (1 billion). Of course, that increased inflation even more.

At the end, different cities created their own money that had more value than paper with ink. A city known for its fine silk weaving created currency out of silk. Another, known for its fine porcelain, created money out of porcelain. My parents still had some of the money. Yes, this was less than 100 years ago.

What will we eventually create in the US as a substitute for the current currency? Big Macs? Gold and silver may be better alternatives, if they are still allowed or not taxed out of existence.

I have often proposed a rule that no economist be allowed to serve on the FOMC, only a group of business people, representing large, medium, and small companies. CEO's of firms would **not** be allowed. In other words, only representatives of the real world. They might make better decisions.

Paul Singer, head of leading hedge fund group Elliott Management, warned about the lowest global interest rates in "5000 years" at last week's excellent **Delivering Alpha** conference. That's exactly what we and others have been saying for some time. He called central bank policies **"radicalized."** That's very strong but also appropriate.

He mentioned meetings that he and hedge fund ace Jim Chanos had with members of the G-7 group, presenting their views of the dangers that were being created. Then they went to Germany and spoke with top GERMAN finance officials about the dangers in the financial system and what central banks were creating. **He said that they were struck by the "amazing arrogance" of all these people.**

During the 2008 financial crisis, when the politicians where running around like chickens with their heads cut off looking for a solution, we suggested this: Put the top five hedge fund managers in a room for two days with the mission to write a rescue plan. They would have come up with something much better than Paulson, Geithner and their crews.

Conclusion: the top people at the largest central banks will continue with their ill-conceived policies until something breaks. And when it does, it will likely be worse than in 2008.

Wishing you successful investing,

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