Saving fish from drowning

> *The art of economics consists in looking not merely at the immediate but at the longer effects of any act or policy; it consists in tracing the consequences of that policy not merely for one group but for all groups.*
>
> Economics in One Lesson, Henry Hazlitt[1]

It has been suggested in economics, to get to the heart of the problem, simply ask 'who benefits?'

We question central banks' motives for moving interest rates to zero and keeping them there. It is obvious that whole swathes of the population do not benefit.

They claim they are helping to keep the economy growing but what happens if the economy has a tumour? Keeping it growing is not the answer – cutting it out is the answer! The tumour is the debt that has accumulated in the system, mainly government debt, over the last 40 years – or in the case of China, the last 10 years.

So the real reason we pursue GDP growth is to avoid addressing the elephant in the room, and instead grow the room so that the elephant looks smaller!

Thus the organisation which actually benefits is the government and their ability to finance their deficits. At 4% interest rates 100% of Japanese government tax revenue would go towards interest payments.

Imagine how big your negative credit card balance would have to be such that 100% of your salary would be required if interest rates went up 4%.

And they cannot tax the rich much more than they are doing because ultra-rich people are mobile… they will simply move (as we've seen in France).

So they do what they must… grow the room not shrink the elephant.

Central banks are effectively bailing out governments. They appear to be saving the economy, but in effect they are saving fish from drowning; they are inadvertently killing the very people they purporting to save.

But it is to divert deflation they argue…

We want inflation they wail…

Let us be unequivocal – central banks can create inflation ANY time they want. They choose to maintain a slack tide where the rate of deflation of various credit bubbles is roughly equal to the amount of money they create, either present or future (credit).

In fact the last thing they want is runaway inflation because it has some very nasty second order consequences.

Here is a snippet from Howard Marks' latest monthly newsletter that sums up the effects of inflation:

> *In the last two years Venezuela has experienced the kind of implosion that hardly ever occurs in a middle-income country like it outside of war. Mortality rates are skyrocketing; one public service after another is collapsing; triple-digit inflation has left more than 70 percent of the population in*

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[1] Accessed at http://steshaw.org/economics-in-one-lesson/chap01p1.html

poverty; an unmanageable crime wave keeps people locked indoors at night; shoppers have to stand in line for hours to buy food; babies die in large numbers for lack of simple, inexpensive medicines and equipment in hospitals, as do the elderly and those suffering from chronic illnesses.[2]

So, we the fish are being saved from drowning whilst being given a lecture on flying. (Get tech savvy, extend your risk profile, invest in risk assets, bet the retirement ranch.)

Closer to our home, real price discovery is being depressed which is resulting in the same for volatility. We stress time and time again, when the day of realisation dawns, the resultant move will have exponentially more adverse consequences than if the central banks had allowed the free market hand to determine the supply and demand of capital.

And so we watch in amazement at the absence of directional volatility and a preponderance of noise.

It brings to mind the quote from the book *China's Future*:

雷声大雨点小 (much thunder, little rain)[3]

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[2] Latest memo from Howard Marks: Economic Reality, accessed at https://www.oaktreecapital.com/insights/howard-marks-memos

[3] Shambaugh, D. (2016) China's Future, Cambridge, UK; Malden, Massachusetts: Polity Press; p. 38