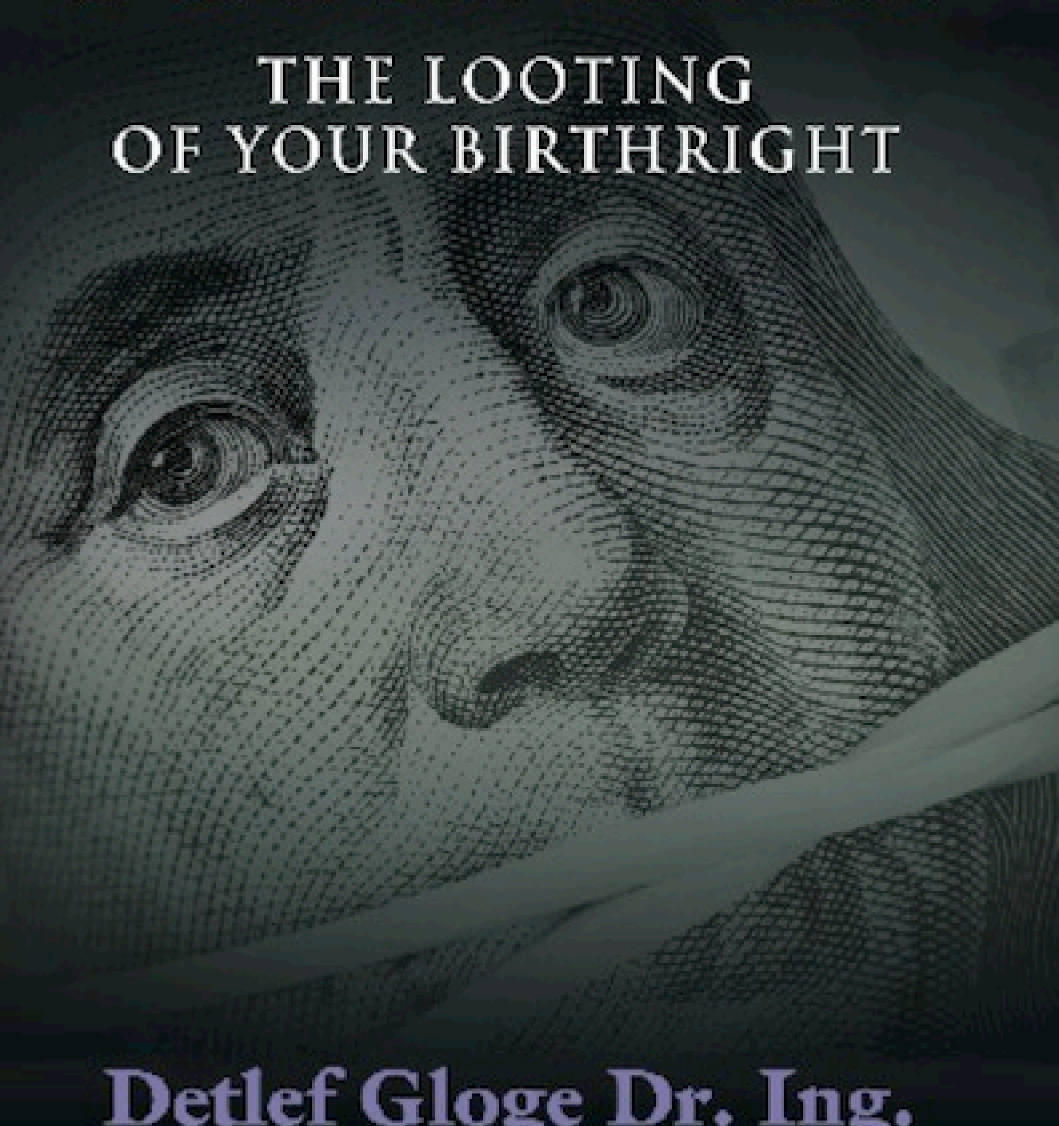
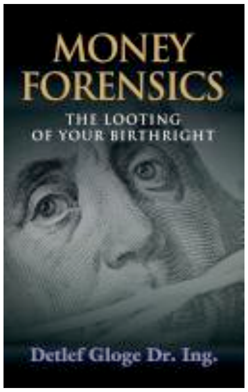
MONEY FORENSICS

THE LOOTING OF YOUR BIRTHRIGHT



Detlef Gloge Dr. Ing.



MONEY FORENSICS: The Looting of Your Birthright *provides conclusive evidence and precise numbers. The U.S. Federal Reserve and other banking systems manipulate incomes and confiscate wealth on a vast scale and money printing defrauds society's most vulnerable. The numbers prove that this activity creates society's debilitating inequality, and perpetuates itself in an irreversible tsunami of unsustainable debt. Simple language, mathematical precision, and profound insights keep the reader captivated. TMONEY FORENSICS challenges conventional wisdom and expert opinion.*

Money Forensics

Order the complete book from

Booklocker.com

http://www.booklocker.com/p/books/7672.html?s=pdf

or from your favorite neighborhood or online bookstore.

Your free excerpt appears below. Enjoy!

Money Forensics:

The Looting of Your Birthright

ISBN 978-1-63263-506-8

Published by BookLocker.com, Inc., Bradenton, Florida.

Printed in the United States of America on acid-free paper.

BookLocker.com, Inc.
2014

First Edition

Prologue
The Roots of Money Mischief

The evidence is there for all to see: inequality, instability, and manipulation are rampant. Financial speculation is out of control. Blaming capitalism and free markets has become many authors' favorite pastime. It is easy to fill books with generalities, but is there evidence of specific malfeasance or misconduct? What do we really know about free markets?

Thousands of years of monetary manipulation have buried all counterfactual evidence of markets operating freely. History is replete with calamities created by financial excesses. People remember the Great Depression. Being able to repeat the same follies just eighty years later only shows how little we know.

Bankers say they create money *ex nihilo*, in reference to God's *creatio ex nihilo,* implying they do God's work serving the hapless masses. But what do they create ex nihilo? If it has value, do they create value from nothing? If not, from whom do they take it?

Counterfeiting is illegal because it debases the currency, diminishes its purchasing power, and undermines the trust in its authenticity. Ex nihilo money is legitimate and authentic, but identical to counterfeit money in its effect on the currency and in its deception of currency users.

Three thousand years of ex nihilo money creation have given it legitimacy. But it is looting of wealth nevertheless. We shall identify the victims and quantify the damage. It is called inequality. Don't take our word for it. We shall argue our case and you will be the judge.

The damage is not just that caused by inflation. If banks create money in step with society's productivity gains, prices will not rise. But banks still confiscate the growth of society's wealth. Yes, the activity is confusing, which is why it works so well. But we shall clarify things.

There is another equally damaging aspect to ex nihilo banking: all money in circulation is money borrowed from banks. That means bank lending must increase for the money supply and income to grow. Debtors depend on that growth to service or repay debts. When bank lending slows, contracting incomes cause debtors to default. It is preordained economic collapse. People call it a crash or a depression.

But we are getting ahead of ourselves. Don't worry, it will all be explained. Here is what we plan to argue:

- Ex nihilo banking creates inequality by confiscating wealth.
- It causes indebtedness that collapses when lending slows.

- Frenzied lending to escape the trap worsens the collapse.

These three simple facts have confused mankind since the 6^{th} century BC. Mythology is sketchy about the first occurrence, but King Midas of Phrygia issued notes backed mostly by his alleged golden touch. This kind of banking made his heirs, and especially King Croesus of Lydia, famously rich. But by 547 BC, the Midas curse, as we might call the collapse, destroyed his heirs and their ingenious money machine.

The Romans outlawed ex nihilo banking as a form of counterfeiting, but medieval sovereigns from the Habsburgs to the Bourbons resurrected it and had their bankers manipulate the coin of the realm until their finances, their subjects' trust, and their empires lay in ruin. The founding fathers of the American Republic remembered the Bourbons' debacle and kept banks under reasonable control until the American Congress granted banks cartel status in 1913. The crash of 1929 could have served as a lesson, but changes were superficial and were later reversed.

Obviously, this subject matter can be exploited for its entertainment value and for arousing public emotions. There are enough publications of this kind. Bankers are honorable people, and banking is lawful business. When we question some of its value to society, we must avoid feeding public anger. We must let the arguments speak for themselves.

Unfortunately, they show that ex nihilo banking does not serve the public interest.

This book requires no special expertise or knowledge. The reader may want to ignore mathematical detail, which is merely used for logical consistency and precision and to keep cognitive biases from corrupting the arguments. The book's intent is not to find new economic models or theories but rather to present a consistent logic that relates money to economic activity. This formal logic leads to inescapable conclusions, which are the basis of our forensic arguments.

They concern economic science only insofar as monetary manipulation affects fund flows and balance sheets. We avoid commentary on public policy except where the government functions as creator and partner of the banking system. The focus is on the economic consequences of monetary policy as executed by the banking system.

To let the arguments speak for themselves, we refrain from citing respected authorities or renowned schools of thought. As author, I gratefully acknowledge the debt I owe to generations of economic thinkers, past and present, including today's bloggers. Among the latter, those who especially influenced my thoughts include David Stockman, Mike Shedlock, Charles Hugh Smith, Pater Tenebrarum, Detlev Schlichter, Michael Pettis, John Mauldin, Steve Keen, John Hussman, Charles Gave, and Tyler Durden.

Monetary Policy

Just like the natural pricing mechanism balances output and income, it balances the three segments of GDP: when consumer income lags, producers must reduce consumer prices; their profit margins and savings shrink; and they slow expansion until consumers' purchasing power equals output. This mechanism also tends to align consumer prices with wages in the same way it aligns profits with replacement and expansion of productive capital.

By changing money supply and income, ex nihilo credit foils the balancing mechanism. Producers see no reason to lower prices, even when wage pressure from automation and global competition reduces incomes.

Consider Federal Reserve activity as an example of how ex nihilo credit changes the natural fund flows. The Fed's stated policy since the 1980s has been to assure full use of the US labor and capital stock and to maintain 2% inflation. Figure 1 shows the feedback loop this policy creates.

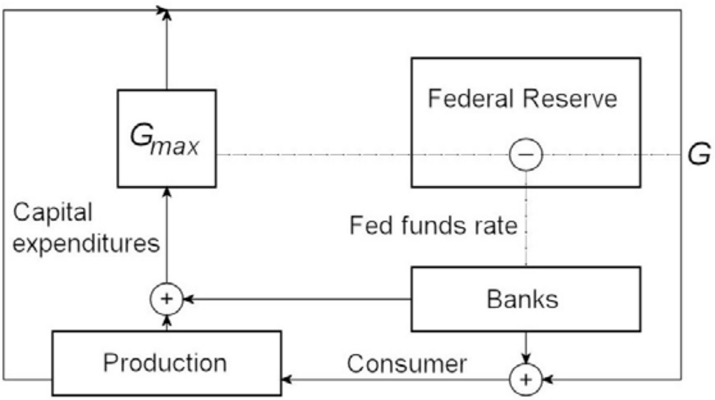


Fig. 1 Fed policy fills the income gap by money creation.

The Fed compares current income G with productive capacity G_{max}. A positive value $G_{max}-G$ causes the Fed to lower interest rates and stimulate borrowing. Banks add ex nihilo credit to the money supply and income increases. The Fed continues lowering rates until the gap $G_{max}-G$ disappears and prices rise to the Fed's inflation target.

People quickly adapt their strategies to the Fed's pledge. Producers increase target capacity G_{max} in anticipation of consumer borrowing. The Fed encourages bank lending, until capacity and inflation reach the target. Households and small businesses borrow to fill the recurring income gap, which keeps expanding as a result of automation, foreign wage competition, and price inflation.

In this way, long-term growth and borrowing has generally followed the Fed's desired exponential growth path, which is distorted at times by cyclical over- and undershoots. By diluting the money supply, banks keep shrinking consumers' purchasing power, which consumers must then supplement by lending. All the while, producers' savings increase beyond what they need to meet consumption growth. They lend the excess back to consumers or invest it in speculative assets.

Here are the conclusions we draw from basic principles:

- Natural price and rate adjustments balance the economy.
- They balance consumption, saving, and capital creation.
- The Fed foils this mechanism and harms wage earners.

The Fed justifies all these distortions and imbalances with the unsubstantiated argument that its policy improves employment. It ignores the fact that it boosts prices without having any influence on wages. Debt accumulates until the private sector reaches its borrowing limit, bank clients refuse to borrow, the Fed's loop stops working, producers hesitate to invest, and the output gap remains open.

When the 2008 crash stopped consumer borrowing, the Fed created money by *quantitative* *easing*—that is, buying government debt from savers and banks in the hope they would channel the new money into the economy. Some of that money may have helped to sustain tepid growth, but most of it just accelerated financial speculation.

Bank lending of ex nihilo credit obscures and magnifies imbalances until they become unsustainable and irreversible. Part 2 explains how ex nihilo lenders confiscate wealth from savers and people who work with cash. The numbers show how compounding dispossession leads to poverty and dangerous inequality.

Balance, Birthright, and Banks

By now the reader is probably wondering what the outcome is when natural price adjustment is left to work without hindrance. Suppose banks can lend only what savers have previously deposited. Nobody creates money. What people have in their wallets is all there is. In a growing economy, producers must reduce prices to match the growing production to the unchanging money supply. Nominal growth is g=m=0 even though there is real growth y.

This real growth induces mild deflation p=−y. People's nominal incomes are fixed, but their purchasing power increases at rate y, which allows them to consume the growing output. Real savings and real wages also increase even when raises are absent. Steady and anticipated deflation is benign when debts are not excessive. Coins and bills slowly gain value. Prices decline too slowly for anybody to consider deferring purchases.

Everybody partakes in the productivity gain. There is no redistribution of income or wealth. Cash savings grow like everybody else's wealth at the rate of real growth y. Savers lend their cash at interest rates equal to or larger than y, which is the natural market rate. Under such balanced conditions, prosperity spreads all across society and enriches everyone.

Remember money holders are the equity owners of the national enterprise. In the absence of dilution, price adjustments assure that equity grows with the enterprise value. Hence, cash holders participate in growth along with everyone else. It is the national birthright. As money gains value, people lend their savings if they earn interest at or above a rate y. Capital costs exceeding y encourage frugal deployment of capital.

Compare this condition to bank lending, which creates ex nihilo money and dilutes the existing money stock at the rate m. By this dilution, owners of cash and cash equivalents lose wealth at the rate m. The technical term for this process is *financial repression*. The term *cash equivalents* covers all contracts based on fixed cash values. Most loans are of this kind. Just like cash, loans lose value at the rate m.

Note that cash dilution occurs at the rate m, not at the rate of price inflation $p=m-y$. The real loss to cash holders and savers is $m=p+y$. That is the true loss of purchasing power. In addition to suffering from price inflation, cash holders fail to participate in real growth y, of which the rest of society takes advantage. Money dilution denies cash holders the birthright all members of a productive society enjoy.

This loss occurs even when the money dilution is $m=y$, which causes no price inflation. It is a fallacy to believe money supply must expand with economic growth. Money supply expansion is always money dilution and financial repression. Price adjustments retain the value of money commensurate with real economic growth, but they do so only if the money supply is left unchanged.

The true loss money dilution causes in a growing economy is equal to nominal growth g=m. It is a loss of purchasing power that has two parts: the loss evident in price inflation; and the failure of purchasing power to expand with real output growth. The public focus on price inflation alone is a smoke screen deceiving people about their true loss.

What money holders lose does not disappear. Any ex nihilo money creation involves a transfer to the money creator. Compounding year after year, the redistribution creates massive inequality between rich and poor.

Those who question whether it is fair for money holders to participate in real growth must justify why it is fair for banks to be the beneficiaries of that windfall. In the absence of ex nihilo banking and money dilution, the natural pricing mechanism distributes real growth among everyone.

We accept this as the fair outcome, which is a logical consequence of a consistent theory of money. The chapter titled “The Equivalence Principle” will shed more light on this fact.

Job Destruction

People prosper when their activity provides the resources they need to be creative and take risks. Studies show that self-sufficiency encourages productivity because it ties the ability to spend to the need to produce. When a minority controls most resources, communal efficacy suffers.

Borrowing or government redistribution seems unable to correct the problem. A natural uniformity of resources is a sign of a productive society and healthy undisturbed markets. Deprived of these resources, people lose confidence and initiative and eventually become a burden to society.

The Fed pretends transferring wealth to potential job creators is in people's interest. And the claim is believable. Car loans sell cars and create work. Promulgating this argument, the Fed diverts wealth from ordinary people, small business owners, contractors, and households. This compounding loss destroys productivity and purchasing power and eventually ends in loss of jobs and declining real GDP.

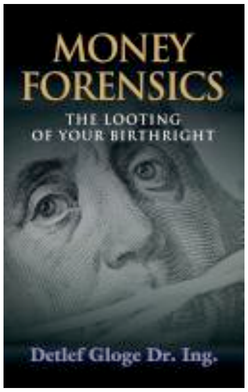
But the Fed is not without company. Banks and governments worldwide pretend to serve the public by financial repression. When Chinese policy makers realized their unabashed wealth transfer from consumers to export industries had practically destroyed domestic consumption, they reacted predictably. Rather than stop financial repression and let consumers recover and rebuild their lives and incomes, they merely altered the strategy of redistribution.

Summarizing our analysis so far, we can make the following points backed by logical arguments and empirical evidence:

- Money, income, and debt are inextricably connected.
- Banks confiscate resources of the productive majority.
- Ensuing inequality impedes progress and harms society.
- Eventually it destroys productivity and real growth.

Apart from creating social tension, financial repression has serious consequences: it denies the majority the resources for healthy productivity; it wastes skills and resources on financial speculation, which is the subject of a later chapter; and it generates economic instability, as discussed in part 3.

Exceeding 3.5% of national income, repressive transfers dwarf what the beneficiaries of this transfer are able to consume. Those who know how to match capital to skills and opportunities are denied its use while those who lack the incentives and capability waste it on luxury and speculation. The result is that productivity and real growth decline as financial repression progresses.


MONEY
FORENSICS
THE LOOTING
OF YOUR BIRTHRIGHT
Detlef Gloge Dr. Ing.