Vandalism vs. Keynesianism

Monday, 28 June 2010
Baltimore, Maryland – Melbourne, Australia
By Dan Denning

From Dan Denning in St. Kilda:

--Gold futures again flirted with an all-time high over the weekend near US$1,260. But thank goodness we read Michael Pascoe's article in today's *Age* before again pointing out that gold is a good hedge against stupid monetary policy. Not so! Gold, according to Pascoe and Macquarie Group interest rate strategist Rory Robertson, is in a bubble. Also, it has no yield, and so therefore is impossible to value.

--With short-term real interest rates on U.S. government bonds effectively negative, we've wondered lately why so many people complain that gold doesn't have a yield (either). But it's true. It doesn't. It just sits there looking pretty and yellow and heavy - preserving value and capital better than other kinds of money in which you can choose to denominate your wealth.

--But maybe we just begged the question. Our contention is that gold is being remonetised in the global financial system as the fiat money system falls apart. Yeah. Totally kooky. We know. Because so many paper currencies have lasted forever instead of returning to their intrinsic value.

--In any event, we can let the cat out of the bag and say we're delighted to be debating Mr. Robertson next Tuesday night in Sydney at an undisclosed location. Actually, the location is disclosed. But if you want to know where the event is, you'll have to RSVP to thoughtbroker@gmail.com

--The debate - and it's not about gold, it's about whether Australia has a house price bubble or not - has been organised by Parnell McGuinness and Leonie Phillips of www.thoughtbroker.com.au . We had the pleasure of meeting both ladies in Perth at the Mannkal Foundation's Freedom Factory conference in April.

--It should be a good debate. And fair warning to Mr. Robertson - we also own hiking boots and will not be intimated by bets. Having grown up in the Rocky Mountains of Colorado and twice summitted Longs Peak, we're not afraid of hitting the trail.

--But in all seriousness, Australia deserves a good debate about whether its housing market really IS different - supported by high immigration, low interest rates, constrained supply, prudent bank lending, and a national desire for home ownership...or whether the nation's lenders have overinvested in housing as an asset class, fuelling a price boom but saddling millions of Australians with debt that will be painful to carry and hard to repay if and when interest rates ever rise again.

--On the subject of gold, here is a bonus contention: you'll know there's a gold price bubble when Macquarie Group uses equity raised from its own clients to borrow lots of money, overpay for gold mines (sold to them by the government), and manufacture a yield on those gold assets, perhaps paid out of capital. That sounds more or less like a familiar model and a sure indication an asset class is in a bubble.

--Macquarie isn't involved in gold yet, therefore we contend that gold can't be in a bubble. It is, however, recently involved in housing. Go figure.

--But what about mining stocks? Is it time to buy them? We had a chance to ask just that question to our colleague Greg Canavan this weekend. And we recorded it on video! You can find part one here and part two here.

--Greg is a value investor with an understanding of what makes sound money, hence the name of his publication *Sound Money.Sound Investments*. If you haven't read any of his previous *Daily Reckoning* articles, the video is a good introduction into his investment philosophy and his current thinking on the market. Each half runs about twenty minutes. And yes, we know we have a face made for radio.

--For the record, Greg has an end-of-year special on for new subscribers to his letter. If you're a serious value investor in Australia, you should be reading Greg's weekly reports. And in the interests of full transparency, yes, we get a commission every time Greg sells a subscription. It's the only active deal like that we currently have with any third party - because Greg's writing the only newsletter in Australia that we like to read but don't already publish.

--Back to the bigger picture. It is hard to know which is the more dangerous group gathered in Toronto for this weekend's G-20 meeting. Is it the balaclava-wearing, black-shirted vandals who destroy public property and break windows to bring down "the system"? Or is it the men in suits behind the security fences deciding how to cut spending and raise taxes in order to repair the broken debt-based funding model of the Welfare State and then shove that deal down everyone's throats?

--Hmmm.

--On the one hand, the balaclava wearers have a point: why should the G20 leaders meet in private to devise and impose a global financial regulatory regime that benefits, primarily, the banks themselves? You could argue that the G-20 leaders are the democratically elected representatives of their people. But still, it feels a bit like a private party to which you're not invited.

--Our sympathy for the bomb-throwers ends at their wanton destruction of private property and vandalism. The truth is - in our experience - there is always a small group of people at these gathering who just want to break and burn stuff. They are criminals and vandals. And if we believed in capital punishment - we don't because we don't support the power of the State to take life - all property crime would be capital crime.

--By the way, the only good thing about burning cop cars and broken windows is that you have what the PC class refers to as "a teaching moment." That is, if breaking stuff were really good for the economy because it created jobs (lots of windows to repair, new cop cars to buy), then the most sensible economic strategy to create the most growth would be to break everything.

--This must be what people mean when they say that war is good for the economy. It stimulates production and jobs. Taken to its logical conclusion, the best strategy for the strongest growth is perpetual war - which funnily enough seems an awful lot like the strategy of the American Welfare/Warfare State.

--Of course anyone smarter than a fifth grader intuitively knows that you can't destroy your way to wealth - unless you're a war financier and profiteer, and most of those jobs are already taken. Is it any coincidence that governments are so often declaring "war" on social issues and then borrowing from large money centre banks (often in the form of a cartel with monopoly powers like the Fed) to pay for those wars. Isn't this war profiteering too?

--The only real difference in substance between Toronto's street vandals and the government suits is that vandals are destroying tangible value in front of your eyes while the Keynesian inflationists are travelling forward in time to destroy value. "Pump priming" deficit stimulus spending robs from future demand and misallocates current resources to create the illusion of growth - a political motive for people like former Prime Minister Kevin Rudd to hang his hat on (attached the head Labor loyalists recently cut off).

--Of course all of this goes "unseen," which is the great observation of Frederic Bastiat. The money spent repairing the baker's broken window is not spent buying a new mixer to make more dough. The money spent on the new cop car is taken as taxes from the pocket of the family that would have gone to Disneyworld.

--Everything has a cost, which is often unseen. Compared to the benefit - which is often trotted out on camera, the hidden cost doesn't seem real. And in a way, that which can now never happen is an aborted possibility, killed by the policy of refusing to live within your means (stimulus spending). To the extent that the suits in Toronto want to spend money they don't have, they are as equally destructive as the vandals in the Streets.

--Maybe they should all break bread together and discover they have common cause: a fundamental disrespect for private property and personal freedom. It would probably be a tax-payer catered lunch though. And you would be the main course.