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The Federal Attack on the Dollar

by Jacob G. Hornberger

In the wake of unrestrained U.S. federal spending, U.S. conservatives are no longer talking so loudly about how they brought down the Soviet Union — by making it spend the nation into national bankruptcy. But the marketplace is speaking as loudly as conservatives once did, as reflected in the continued plunge in the international value of the dollar.

Make no mistake about it: Despite all the economic mush and mish-mash that federal officials are now spouting, there is one and only one cause for the rapidly depreciating value of our currency: uncontrolled federal spending, including spending on the so-called war on terrorism, the expansion of the U.S. empire around the world, the military adventure in Iraq, and domestic pork and welfare to mollify the American masses, including Social Security, Medicare, and Medicaid.

What we're talking about, of course, is the same problem that has bedeviled empires throughout history. Think of the Roman Empire, the British Empire, and the Soviet Empire. Bread and circuses, and none of it has ever been cost-free. All of it has inevitably entailed the bankrupting of a nation.

Here's how the system works.

As federal spending on both foreign warfare and domestic welfare begins to soar, federal officials have to figure out where to get the money. One option is simply to tax the citizenry. But public officials are not stupid — they know that when taxes rise, citizens revolt. That's in fact precisely why President Bush continually vowed not to raise taxes even while going on one of the biggest government spending sprees in history.

How does he do that? How does the president spend more money than what the government is collecting in taxes? He borrows it, just as ordinary people do when they go to a bank to borrow money to pay for expenses that are exceeding their income.

When a person borrows money from a bank, the borrower signs a promissory note to the bank promising to repay the loan at some future date and the bank delivers the money to the borrower. A government loan works the same way, only here the borrower (the government) signs

a note or bond promising to repay the loan at some future date and the lender (the purchaser of the note or bond) delivers the money to the government.

That's what they federal officials mean when they refer to financing the "budget deficit." Government expenditures exceed government tax income, and the difference is paid for with borrowed money, which the government is obligated to ultimately pay back.

So, who are the lenders? In this case, they are mostly foreigners, primarily because Americans save only a very small share of their income, some even convincing themselves that they're "helping the economy" by spending their income — at least that portion of their income that the government hasn't taken from them in the form of income taxes, Social Security taxes, Medicare taxes, and unemployment taxes.

The savers — that is, those who are lending all that money to the federal government by purchasing the government's notes and bonds — are foreigners, a large portion of whom are in Asia.

Now, have you noticed that with the continued plunge of the dollar — some 50 percent against the Euro since 2002 alone — U.S. officials from the president on down do their best to confuse the issue by conflating the "budget deficit" and the "trade deficit," somehow implying that the real cause of the dollar crisis is that people aren't spending enough money buying American goods? The reason they do that, of course, is to avoid responsibility for what the uncontrolled federal spending is doing to our nation, just as Soviet officials didn't want the Russian people to know what their spending was doing to their nation.

When these people refer to the trade deficit, what they're talking about are statistics showing that Americans are buying more goods and services from foreigners than foreigners are buying from Americans. But how can that be? What are foreigners doing with all those dollars that they're obviously not spending on American goods and services? The answer: They're buying U.S. government notes and bonds, which don't show up in the trade-deficit statistics that U.S. officials cite as the cause of the dollar crisis! That's correct — when you factor in foreigners' purchases of American goods and services and their purchases of U.S. government notes and bonds, there is, for all practical purposes, a "trade balance."

Again, the reason federal officials try to engender confusion is that it is in their interest to do so. When people are confused over "complex" economic issues, there's less likelihood that they'll blame the government for its profligacy ... unless it's a foreign government, as was the case when U.S. conservatives publicly crowed about how they brought down the Soviet Union — not by increasing its trade deficit but instead by making the Soviet government spend the nation into bankruptcy.

So when all those notes and bonds come due, how does the government repay the loans? Well, one way is by taxing the people in order to get the money to pay off the loans. But remember: people don't like their taxes raised and are likely to reflect their dissatisfaction at the

polls. What is much more likely to happen is that government officials will simply use their printing press to print the money to repay all the loans. The process is, of course, more complicated than that but that in essence is what they are doing — flooding the market with newly printed money to avoid raising taxes.

And it's that probability that is causing the value of the dollar to plunge in international markets. The continued drop in the value of the dollar is reflecting people's perception that the government will artificially expand the money supply in the future, thereby causing its value against other currencies to drop.

That possibility, in turn, is making foreign bond-holders very nervous because they don't want to be stuck holding millions of dollars of a depreciating asset. That foreign anxiety in turn is making Washington officials very nervous because of the possibility that foreign investors will start a panic run for the exits by dumping (i.e., selling) their notes and bonds on the market all at once. While no one can predict the exact nature and magnitude of such a crisis, most people agree that it could conceivably be of earthquake proportions.

In effect, Washington officials are doing what imperial powers have done throughout history — debasing the currency to finance massive military and welfare expenditures. The consequence will inevitably be ever-increasing prices (inflation), which is simply the market's way of saying that the currency is falling in value in comparison with everything else. The advantage to public officials, obviously, is that the masses usually have no idea that government is behind the rising prices and so join the government's chorus blaming the rising prices on rapacious businessmen, profiteers, and speculators. That's when you'll also start hearing the calls for "price controls," as we did during the 1970s dollar crisis, when the Nixon administration was doing the same thing that the Bush administration is doing today.

It is important to realize that our American ancestors tried to protect us from this type of immoral and destructive activity on the part of our government officials. For example, the Constitution did not empower the federal government to issue paper money and also expressly prohibited the states from making anything but gold and silver coins the medium of exchange and from emitting paper money.

Thus, for most of the first 100 years or so of American history, Americans used gold and silver coins as their medium of exchange. The federal government could still borrow money by issuing bills, notes, and bonds, but since no one was forced to accept them as money, no one worried too much about the federal government's borrowing and spending too much money. That is, they knew that while government could crank up its printing presses, the value of their real money — their gold and silver — would simply rise along with everything else relative to the falling value of the government's debt instruments.

And that's precisely why governments have always hated gold — not only because it provides people with protection from uncontrolled government spending but also because it

provides a very public signal of how much the government is debasing the currency. Increases in the price of gold are another way of saying that the currency is dropping in value. Therefore, it shouldn't surprise anyone that federal officials during the regime of Franklin Roosevelt, which sent federal spending through the roof, did exactly what totalitarian regimes have done — they nationalized gold and made possessing it illegal: every American was ordered to deliver his gold to the federal government, on pain of fine and imprisonment for violating the law.

Today, however, it seems that there are more people than ever who are recognizing that government itself — or, more precisely, unrestrained government spending — is the root of the dollar crisis. That might even be why President Bush says that he now favors a massive decrease in federal spending, especially within the military-industrial complex. By doing so, he's effectively admitting that the looming monetary crisis is rooted in uncontrolled federal spending.

If only conservatives, who so proudly proclaimed that they brought down the Soviet Union, would rise up and take a stand against the massive federal spending that threatens the stability and viability of our country! But, alas, having committed themselves to all the socialist and interventionist programs that such spending funds, including Social Security, Medicare, Medicaid, welfare, education grants, the drug war, the war on terrorism, the Iraq military adventure to “liberate” the Iraqi people, and big “defense” spending by the military-industrial complex, conservative lips unfortunately now remain sealed.

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