

## How to end the bailout mess

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According to Wikipedia, "A bailout is an act of giving capital to an entity (a company, a country, or an individual) in danger of failing in an attempt to save it from bankruptcy, insolvency, or total liquidation and ruin; or to allow a failing entity to fail gracefully without spreading contagion."

First we saw private citizens and major government agencies being saved from debt default in various government bailouts. Then we saw bailouts of major banks, financial institutions and corporations. Now we are seeing bailout of entire countries. First out is relatively small Greece, with a GDP of 2% of EU GDP and a bailout at \$133bn. Another of the PIIGS countries in line for bailout is Spain, bailout size a monstrous \$364bn according to rumors. Comparatively large California - 11% of US GDP and world top 10 if it was a country a country - might be another candidate, a state that is reported not even being able to meet its pay roll obligations for May.

### Who bailouts the bailouter?

But who is making these bailouts? Where do they get the necessary capital? To the most part, governments use various schemes to create more capital through issuing more debt – 'monetizing debt' it's called – as admitted by Fed chairman Bernanke just the other day. And this begs the question, what's next? Who will bailout the bailouter? Who will provide the necessary capital that time? Who can monetize the amount of debt necessary for that?

The answer is that no one can.

### Ways out of the bailout mess

So what are the options to get out of this bailout mess? I see a couple of ways. Firstly, the governments could default on their debt, just like Russia did in the late 90's. That's a tough political decision to make and one that will not be made if it can be avoided. It should also be noted that it amounts to treating the symptoms rather than addressing the true problem.

Secondly, there is the theoretical possibility that all countries defaulted simultaneously, thus cancelling out all mutual obligations, something like the process used when companies merge balance sheets. But how to convince for example China and the US to merge their balance sheets? Not even the Goldman Sachs wizards could do that, I suppose.

Thirdly, the governments could inflate their way out of debt, maybe with Zimbabwe as model. It would be hard to notice at first, but as prices turn sharply upwards it wouldn't be possible to hide any more. Granted, it would be harder to detect if many countries did this at the same time, which actually is exactly what is happening right now without anyone reporting it in mainstream media. One reason for this is that the exchange rates are a relation between currencies, and if they all loose value at the same rate the exchange rates are rather stable. This way isn't a very

honest thing to aim for and once more it would be addressing the symptoms rather than the problem.

## **Making the problem disappear in an honest way**

A fourth way would be to simply repay the debt. That would make the problem disappear and it would also be the honest thing to do. But why doesn't Greece do it? Why can't Spain or California do it? Why wouldn't the major bailouter be able to simply repay the debt? Well, this is a very important thing to understand so I expand a little on this. The reason they don't repay the debt is because they simply cannot. They simply don't have the necessary tool anymore to do extinguish all that debt.

Let's say the US government wanted to prematurely repay all US treasury bills, i.e. a big debt, to for example China. What should they pay with? Fed notes? But that would only transfer the debt to the Fed balance sheet, another US government agency (more or less). How could the Fed in turn repay the debt? By handing over Euros? That would only transfer it to the ECB. By using some imaginary IMF money? That would only be to transfer the debt to yet another balance sheet.

Thus, the only way to extinguish debt is to repay with something that only appear as an asset on the balance sheet, the only way to extinguish debt is to hand over something real. If they handed over cars, wheat, timber or houses, that would be a way to repay the debt instead of transferring it to someone else. But few would accept such payments, especially on that kind of scale. No, it has to be an asset financial with some financial properties, notably gold and to some extent silver.

## **The gilded way**

Paying someone in gold means that the debt is repaid, end of story. And you would be just as happy with the first ounce as the last, which is what makes gold so unique. Gold has monetary properties that nobody can deny (without making a fool out of himself). Even former Fed chairman Greenspan wrote a famous article about that way back (called Gold and Economic Freedom) before joining the power elites.

Gold would be the only way to really reduce the world's total debt. But is there enough gold at current price to extinguish all the debt? No, and I've seen numbers indicating that gold would have to be priced at \$9,000 per oz if those balance sheets would be in order again, as compared to around \$1,200 today. Now, that would make the problems disappear and would also be an honest way out of this mess. Will that ever happen?

Hyperinflation, sovereign or joint government debt default or gold at \$9,000 – how will this bailout mess end? Your guess is as good as mine, but at least we know an honest way to strive for.