Don't Blame the Thermometers

According to the Bureau of Labor Statistics, in February the average price of a pound of ground beef reached a record high $4.29. Many Americans probably reacted with a sad shrug, assuming that prices will always go up over time. Others no doubt "blamed the corporations," believing there is an evil cabal of corpulent capitalists who, behind locked doors, smoke cigars and vote on how much they will screw the consumers in their next round of price hikes. Most people fall into one of those two opinion camps, yet neither is correct. The truth is that corporations do not cause inflation. Nor is it an inevitable fact of life.

The only cause of general, nationwide price inflation is the expansion of the nation's money supply. A truly free economy cannot experience inflation because it does not have the power to create money out of thin air and add it to the money supply. Yes, if Florida has a cold snap that kills off much of its orange crop, the price of oranges will necessarily go up because the demand for oranges will exceed the supply. But that is *not* inflation, it is simply a price increase *for one particular product*. Some consumers will choose to forego the purchase of oranges or orange juice. Other consumers will choose to pay an additional few dollars for oranges and will, as a result, have fewer dollars to spend on something else. There is no nationwide price inflation because the money supply has remained constant. If there was $1 trillion of currency in circulation in the United States the day before the Florida freeze, there will still be $1 trillion in circulation the day after the freeze. If consumers spend an additional $50 million on higher-priced oranges, they will *necessarily* spend $50 million less on something else.

Similarly, if General Motors raises the price of its cars, consumers will respond by buying Fords or some other company's product. General Motors will see reduced sales. But if *all* car manufacturers raise their prices, that is no different than the price of oranges going up. An extra $1,000 spent on a new car means the buyer will have $1,000 less to spend on *something else*. The nation's money supply has *not* been increased. *The existing money has merely been shifted from one product or service to another.* The consumer cannot "give himself a raise" to cover the higher cost of a new car (or oranges). Nor can the consumer maintain personal deficits in perpetuity. (Even if he borrows money to buy a new car, he must pay back the loan.)

When the government spends more in one year than it did in the prior year, it can make up the difference—effectively "giving itself a raise"—by increasing taxes. But, as is the case with higher orange prices or car prices, that action merely shifts the *location* of some of the nation's money. Because his taxes have gone up, the consumer may decide he cannot afford a new car. That money then goes not to a new car, but to someone else's food stamps (or "green energy" loan guarantees, or ObamaPhones, or corporate subsidies, or disability benefits for "bad backs," or Air Force One trips to golf courses). Again, the total amount of money in the economy has not changed, it has simply been "moved around" via the force of government (typically from productive to non-productive uses).

Unfortunately, the government does allow itself to run continuous deficits. When the politicians lack the courage to raise taxes or to cut spending, the government *does* run a deficit. That deficit is then covered by borrowing money or by *artificially expanding the money supply*. The Federal Reserve creates money out of thin air and uses it to "finance" the government debt. In that scenario, the total amount of money in the economy *increases*, even though the private economy is still producing the *same* amount of goods and services. That means there is more money "chasing after" those goods and services. That expansion of the money supply is inflation. The money supply is inflated, just as a balloon is inflated. If a mountain of additional money is created, it is called hyperinflation.

Unfortunately, facts get distorted by the unintentional—and often intentional—misuse of words. Again, inflation is the increase of the nation's money supply. Inflation is *not* higher prices. The expansion of the money supply *causes* higher prices. Higher prices are simply higher prices. They are not "inflation."

With a properly functioning and responsible government, there would be no deficit spending and the money supply would essentially remain constant. There would be no printing of money (except to replace currency that is worn out), and there would therefore be no inflation. With no money printing, there could be no nationwide price increases. In fact, prices would tend to come down over time, as individuals and businesses develop new and more efficient ways of producing goods and services. (A mass-produced pencil costs far less than would any pencil made by hand.) Increased productivity lowers business costs, which enables businesses to give their workers raises without having to raise prices, and everyone in the nation benefits from lower prices.

In fact, a case can be made that, over the last few years, inflation-caused price increases have been substantially mitigated by the ingenuity and productivity of the American businesses and workers. That is, the government's expansion of the money supply *should have resulted in much higher price increases than we have seen*, but Americans have come up with ways to be more productive and efficient. In other words, be thankful that ground beef is "only" $4.29 per pound.

If everyone understood these realities, of course, the government could not continue its destructive deficit games. It runs deficits because it spends more than it collects in taxes, and it spends too much because it buys votes with benefits. Yes, government officials and politicians certainly know that printing money results in price increases, but they are confident that the average voter will blame the corporations and the local supermarket, rather than the members of Congress and the White House. Inflation has often been called a "hidden tax" precisely because expanding the money supply is a tried-and-true method of confiscating wealth from the citizens without most of them knowing they are being taxed.

Some argue that we should "end the Fed" and solve the problem once and for all. But eliminating the Federal Reserve would not prevent the government from spending more money than it collects in taxes. It would simply change the identity of the agency that is creating money out of thin air. If the Federal Reserve were not expanding the money supply, the Department of the Treasury would. Putting a different mask on a counterfeiter does not make him any less a counterfeiter. The nonsense will end only when the average voter understands that inflation is not price increases but the expansion of the money supply, and that it is expanded to cover deficit spending.

For those who believe in "man-caused global warming," the expansion of the money supply is like the expansion of carbon dioxide in the atmosphere. The enviro-socialists argue that reducing carbon dioxide levels will resolve the alleged global warming problem. They may be wrong about many of their assumptions (carbon dioxide levels are far from the only factor in climate change), but they are at least attempting to use cause-and-effect logic. Yet they somehow fail to apply that same logic when they see price increases. The leftists (as well as many non-leftists) blame businesses for raising the prices of goods and services, when those higher prices are simply the *result of* an increased money supply. Blaming corporations for higher prices is like attacking thermometers for higher temperatures. If you believe that *not* pumping tons of carbon dioxide into the atmosphere will stabilize temperatures, then you should also be able to understand that *not* pumping billions of newly-printed dollars into the economy will stabilize prices.

It bears repeating: Price increases are *not* inflation. They are the *result of* the inflation of the money supply. They are a signal that the money supply has increased. Cost-of-living indexes are essentially economic thermometers warning the consumer that someone has been tinkering with the nation's thermostat. When money is printed by the hundreds of billions of dollars and tossed into the economic furnace, the temperature naturally goes up. When the heat gets to be too much to bear, *don't blame the thermometer*. Blame the federal government for spending beyond its means, and for financing its deficits via the Federal Reserve's expansion of the money supply. Stop stoking the furnace and you will stop sweating.

Don Fredrick
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