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THE DOLLAR AND OUR CURRENT ACCOUNT DEFICIT

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- Fiat money, that is, money created out of thin air, causes numerous problems, internationally as well as domestic. It causes domestic price inflation, economic downturns, unemployment, excessive debt, (corporate, personal and government) mal-investment, and over capacity--all very serious and poorly understood by our officials. But fluctuating values of various paper currencies cause all kinds of disruptions in international trade and finance as well.

- Trade surpluses and deficits when sound money conditions exist are of little concern since they prompt changes in policy or price adjustments in a natural or smooth manner. When currencies are non-convertible into something of real value, they can be arbitrarily increased at will, trade deficits and especially current account deficits are of much greater significance.

- When trade imbalances are not corrected, sudden devaluations, higher interest rates, and domestic inflation are forced on the country that has most abused its monetary power. This was seen in 1997 in the Asian crisis, and precarious economic conditions continue in that region.

- Japan has yet to recover from its monetary inflation of the 70s and 80s and has now suffered with a lethargic economy for over a decade. Even after this length of time there is no serious thought for currency reform in Japan or any other Asian nation.

- Although international trade imbalances are a predictable result of fiat money, the duration and intensity of the cycles associated with it are not. A reserve currency, such as is the dollar, is treated by the market quite differently than another fiat currency.

- The issuer of a reserve currency-in the case the United States-has greater latitude for inflating and can tolerate a current account deficit for much longer periods of time than other countries not enjoying the same benefit. But economic law, although at times it may seem lax, is ruthless in always demanding that economic imbalances arising from abuse of economic principles be rectified. In spite of the benefits that reserve currency countries enjoy, financial bubbles still occur and their prolongation, for whatever reason, only means the inevitable adjustment, when it comes, is more harsh.

- Our current state of imbalance includes a huge US/foreign debt of $1.5 trillion, a record 20% of GDP and is a consequence of our continuously running a huge monthly current account deficit that shows no signs of soon abating. We are now the world's greatest debtor. The consequence of this deficit cannot be avoided. Our current account deficit has continued longer than many would have expected. But not knowing how long and to what extent deficits can go is not unusual. The precise event that starts the reversal in the trade balance is also unpredictable. The reversal itself is not.

- Japan's lethargy, the Asian crisis, the Mexican financial crisis, Europe's weakness, the uncertainty surrounding the EURO, the demise of the Soviet system, and the ineptness of the Russian bailout, all contributed to the continued strength in the dollar and prolongation of our current account deficit. This current account deficit, which prompts foreigners to loan back dollars to us and to invest in our stock and bond markets, has contributed significantly to the financial bubble. The perception that the United States is the economic and military powerhouse of the world, helps perpetuate an illusion that the dollar is invincible and has encouraged our inflationary policies.

- By inflating our currency, we can then spend our dollars overseas getting products at good prices which on the short run raises our standard of living - but, on borrowed money. All currency account deficits must be financed by borrowing from abroad.

- It all ends when the world wakes up and realizes it has been had by the US printing press. No country can expect to inflate its currency at will forever.

- Since cartels never work, OPEC does not deserve credit for getting oil prices above $30 per barrel. Demand for equivalent purchasing power for the sale of oil, can. Recent commodity and wage price increases signal accelerating price inflation is at hand. We are witnessing the early stages in a sea change regarding the dollar, inflation, the stock market as well as commodity prices.

- The nervousness in the stock and bond markets, and especially in the NASDAQ, indicates that the Congress may soon be facing an entirely different set of financial numbers regarding spending, revenues, interest costs on our national debt and the value of the US dollar. Price inflation of the conventional type will surely return, even if the economy slows.

- Fiscal policy, and current monetary policy will not solve the crisis we will soon face. Only sound money, money that cannot be created out of thin air, can solve the many problems appearing on the horizon. The sooner we pay attention to monetary policy as the source of our international financial problems, the sooner we will come up with a sound solution.