
PART III: HOW WILL IT UNFOLD THIS TIME?



By Urs Bruegger

*"Lord Keynes was right ... the world will bitterly regret the fact that his arguments were rejected."
Geoffrey Crowther, editor of the Economist at the time of Bretton Woods, quoted by Michael Rowbotham*

Welcome to the third and final instalment of this series on the state of the global economy.

In Part I: Why Can't They See It? and Part II: A World Without Growth?, I argued that further "Japanification" of our economies is inescapable. It is caused by the global monetary system on the dollar that has evolved from one once entirely controlled by the US authorities to one where large banks provide much of the global dollar liquidity. The system is comparable to the structure of an iceberg, the tip the US dollar and the bottom, hidden from view under water, the global dollar liquidity supplied by banks.

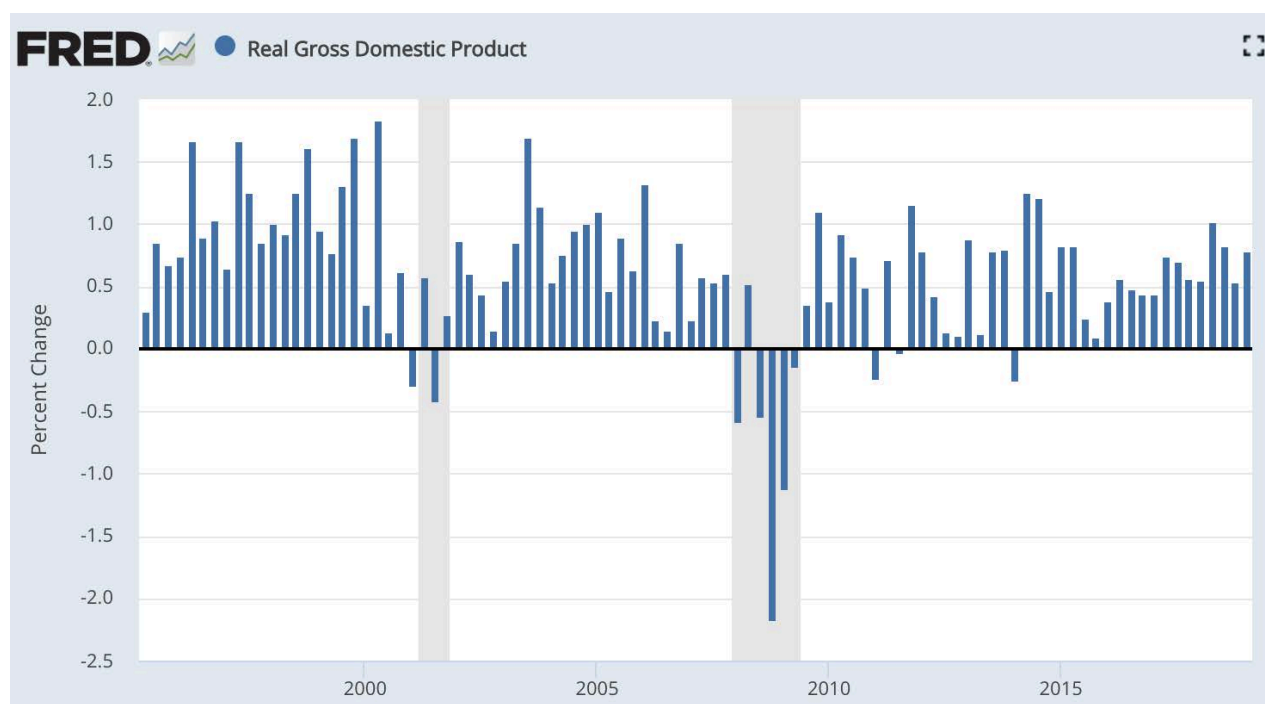
Part III: How Will It Unfold This Time?, is about the erosion of the system that eventually will have to lead to the establishment of a new global order. Until such time, what lies in store?

The great American monetarist Milton Friedman said a far better way to determine whether monetary policy is “tight” or “easy” is to look at the rate of change of the quantity of money.

It is both parts, the visible tip and the hidden bottom of the iceberg, the entirety of the system into which it has evolved into, that needs to be looked at to know whether global dollar liquidity is “tight” or “easy”.

It is in the hidden part where the erosion of global liquidity happens, observable in many places. For some reason it manifests itself in measurable steps. In the US, the long term real growth rate broke first in 2000 from 3.5% to 2.5% and in 2008 to 2.1%.

The Congressional Budget Office (CBO) projects real potential growth of 2% for 2019 – 2023.



The iceberg remains frozen at the tip and melting at the bottom. The hidden place shows, whatever is undertaken above sea level in the cold air, large asset purchase programmes, tax cuts, the decay under water continues unabated. Sometimes the hidden space gets impressed by what is going on above sea level, slowing or even reversing its erosion for a while, as in 2017, only to return to its relentless march to illiquidity.

This is my theory, based on my observations. I call it the Iceberg Theory.

Close your eyes. Consider everything I have written about in each part of this series as the reality. Open your eyes again. You will come to the conclusion dollar strength will go on, bond yields will remain compressed in developed countries and higher in emerging market economies. You will know where to put your money safely and profitably, and where not. You can also see it would be foolish to think all this will continue eternally. You know, at some point, a domino may fall. While you may not know which one, you will know where to look for it.

You will also know when the dollar sinks, yields shoot up, stocks fall, you have not been wrong in your conclusions. It will be the Iceberg that expands again. You will know how to monitor this, though.

Close your eyes and open them again.

Looking at the erosion, from a very different perspective:

At a private dinner at Brooks's, I recently had the honour of listening to a speech given by Sir Mark Lyall Grant GCMG. Sir Mark, formerly National Security Adviser to PM David Cameron and Theresa May, expressed his concerns that in many respects the world may be in a worse state than before the 2nd World War.

Sir Mark identified the erosion of the international rules-based order that was built up after WW2 as the biggest strategic security risk we face today.

The former National Security Advisor said this order is now under severe threat, citing the financial crisis of 2008 that undermined faith in the elite's ability to manage global capitalism, as one of the main reasons.

The eroding Iceberg, with large chunks of bottom ice breaking off in 2000 and 2007, is behind stagnating wages and income inequality. The erosion of the rules-based order Sir Mark observes, has made the world a more unstable place.

■ *"Every act of creation is first an act of destruction". Pablo Picasso*

The Iceberg is a crazy system, with no one at the helm. It will not fix itself. But we do not need to wait for it to reach its deathbed.

We need to go back to Bretton Woods to get it right this time and accept John Maynard Keynes' proposal for a new global order that the world may return to normality.