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The coming hyperinflation crisis

What will it mean for you? William Engdahl examines Weimar Germany, when a wheel-barrow full of money couldn't buy a loaf of bread.

Among prominent economists, government officials, and central bankers, debate today is over whether, or not the world stands on the brink of a new round of savage price deflation, as a consequence of the rolling series of financial crises which began out of Asia two years ago. In reality, however, the world, outside of a handful of economies in emerging markets which are implementing International Monetary Fund conditionalities, is far from being hit with deflation—a process in which manufacturers, facing collapsing markets, desperately slash prices to sell products to market inventory, in turn cutting their profits or running losses, which in turn leads to job cuts that depress the economy further, all in a self-feeding downward spiral.

Present trends are continued further, most emphatically in Japan and the United States. Here, the two largest industrial economies in the world, stand on the brink of not merely inflation, but, rather, a global hyperinflation of a sort until now only seen on a national level during the early 1920s in Weimar Germany, following its defeat in World War I and the imposition of punitive Versailles reparations.

The Weimar Germany example is crucial today to illustrate where the money-printing policies of the Greenspan Federal Reserve and, most especially, of the Bank of Japan and Ministry of Finance since 1995, are taking us.

The Weimar hyperinflation

In the early years after Germany's defeat in World War I, the country underwent an inflation never before seen. Inflation reached such dimensions in 1921-23, that it was renamed "hyperinflation," to indicate its unprecedented scale.

Like every case of inflation—simply defined, the continuing rising of prices for the same or equivalent goods in the market—the German inflation of the early 1920s was the result of specific policy decisions. It is useful to look at those decisions before looking at their social and economic consequences, effects which to this day evoke vivid nightmarish memories for many German citizens.

The initial disproportionate rise in the price of goods and services came as a result of the onset of the Great War in August 1914, a war that found Germany facing foes on two fronts: Russia and the Anglo-French Entente. To finance the extraordinary costs of what everyone in the government of Chancellor Theobald Bethmann-Hollweg was convinced would be a short and limited war, the Reichsbank, under Rudolf Havenstein, demanded the suspension of gold convertibility. This action was approved by the Reichstag on Aug. 4. This was done to stop a run on the central bank's gold reserves and to maintain the required gold backing for new currency issue of 30% gold for every reichsmark printed.

This tiny step, a very modest one by today's monetary standards, opened the door to the ensuing inflation. Existing gold reserves, as well as the private gold hoards of citizens which were called into the Reichsbank, were soon insufficient to cover new money issue needed to finance the war procurements, as the fighting dragged on into 1918.

Rather than impose tax increases, the government of Chancellor Bethmann-Hollweg chose to finance the war by borrowing to cover the growing budget deficits. Over the four years of fighting in the trenches of France and in the East, the Reichstag approved various spending bills totalling a then-staggering sum of 164 billion marks for what had become the first global war. Of this sum, 40 billion marks was raised by issuing Treasury bills, most of which went to middle-income citizens.

During this period, the Reichsbank was authorized, for the first time, to accept government Treasury debt as backing for issue of new banknotes. Previously, only gold or commercial bills, that is, paper representing underlying real goods transactions, could be used as currency backing. Now, in effect, there was no limit to how much currency, or fiat money, the Reichsbank could issue to finance the war. So long as the Treasury issued new bonds and the Reichsbank discounted them, the process could go without apparent limit.

This action, too, proved insufficient to meet the war's costs, and by 1916 the government authorized local savings associations or municipal governments to borrow to finance their costs, by using their holdings of Reich bonds as collateral. This allowed enormous deficit spending to take place across the land, in the midst of the hardships of the war. There was little concern initially about the mounting money supply and government debt tied to it. Finance Minister Karl Helferrich told the Reichstag, "After the war we shall not forgo . . . our claim that our enemies shall make restitution for all the material damage they have caused by the irresponsible

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Depositors carry their money in suitcases and baskets outside a Berlin bank in 1923. "The Weimar Germany example is crucial today to illustrate where the money-printing policies of the Greenspan Federal Reserve and, most especially, of the Bank of Japan and Ministry of Finance since 1995, are taking us."

launching of the war against us." No one in Berlin in 1916 could imagine anything but a German ultimate victory, which would allow the debt to German bondholders to be repaid by reparations from France and other defeated Entente powers, as in the Franco-Prussian War in 1870-71.

It didn't quite go according to plan, however.

The November 1918 defeat of Germany by the Entente powers, set the stage for the next step in an inflationary situation in Germany that was then relatively under control. When the German government signed the Armistice on Nov. 11, not only was it forced to agree to evacuate all occupied territory, to repatriate all prisoners, to hand over 5,000 large guns and 30,000 machine guns, to evacuate the entire left bank of the Rhine, to restore or replace 5,000 rail locomotives, 150,000 freight cars, and 5,000 trucks, and to surrender the entire German naval fleet.

But also, in June 1919, Germany was forced to sign the Treaty of Versailles. Thus, Germany agreed to the infamous Article 231, to accept sole guilt for the war, and to repay an unspecified amount in "reparations" to the Entente powers, above all to France, the main field of battle for most of the war. In addition, the Versailles victors, at the insistence of France, demanded that Germany cede 13% of its territory, which included some of its most vital iron production, coal mining, industry, and agricultural lands, as well as all its colonies.

At war's end, Germany was gripped by serious inflation. The debt of the Reich, only hundreds of millions of marks in 1914, had climbed to billions of marks—no one knew exactly how much, because of bad official statistics. By 1920, the total German public debt was estimated at 236 billion marks. The public held 96 billion marks more in war loans, which when redeemed would put more money in circulation, fueling inflation.

The result was a fall in the international value of the mark from the pre-war rate of 4.2 to the dollar, to 8.6 in January 1919 (**Table 1**). Inside Germany, prices for basic goods had doubled. There were some 6 million German war casualties—

TABLE 1

The Weimar Germany cost of living index

(1913 = 100)

1913	100
1914	103
1915	129
1916	170
1917	253
1918	302
1919	415
1920	1,019
1921	1,341
1922	21,252
1923	13,047,440,148
Nov. 23, 1923	657,010,000,000

Source: German Statistical Office.

the prime of the country's labor force. The outbreak of tuberculosis and other diseases took an added toll, in a population weakened by near-famine conditions by war's end. Major industry had been converted to war production, and funds were lacking to reconvert to civilian output. The rail and roads infrastructure was in shambles after the heavy military use or war damage.

There were labor strikes everywhere in Germany, in protest against the desperate postwar economic conditions and anarchy which threatened. The Ebert government decided on the expedient to print more money, to restart the economy and get food and goods into circulation. Between the November 1918 Armistice and July 1919, when Versailles was signed, the government deficit rose 50%, and the money supply accordingly. The mark collapsed against the dollar, and internal prices rose 42%. The dollar was worth 14 marks by July 1919.

Between July 1919 and February 1920, foreign confidence in Germany's ability to recover began to fade, and the currency fell to 100 marks to the dollar. The official cost of living index, published for the first time in February 1920, revealed an 847% increase since August 1914. Flight capital out of Germany by wealthy businessmen, who feared that new taxes would be demanded to finance the reparations, fuelled the currency fall.

The Versailles reparations

Much of the blame for this phase of the inflation and currency collapse could be placed on the fear of the anticipated economic consequences of the Versailles reparations clauses. Actual reparations payments were not to begin until May 1921, according to the schedule reached by the Reparations Commission. This triggered the next distinct phase in the inflationary spiral, as the grim economic terms of the Versailles reparations burden became reality.

On May 5, 1921, British Prime Minister Lloyd George handed the German Ambassador to London the final Allied Reparations demands, the infamous "London Ultimatum." Germany was to pay a collossal sum of 132 billion gold marks at an annual installment of 2 billion, plus 26% of the total value of its export earnings. In the event of a failure to meet payments in a timely manner, Germany would be subject to sanction, including military occupation of the Ruhr industrial heartland by the Allied powers.

The German government refused to sign the accord, and resigned. But, the successor government of Josef Wirth, the "Weimar Coalition," fearing worse from the victors, rapidly accepted, as did the Reichstag. In August, a down-payment of 1 billion gold marks was made as stipulated.

In a real sense, the Allied insistence on such huge reparations, even if parcelled out over 46 years, proved to be the detonator which turned an ugly postwar inflation crisis into the unheard-of Weimar hyperinflation.

In order to get the foreign currency to pay its foreign reparations and other debts, the German government sold paper marks abroad, marks created, again, by fiat, by having the Reichsbank discount new Treasury bills, i.e., printing-press money-creation unrelated to any increase of goods-creation. The large mark sales triggered a new panic selloff of the mark in exchange markets from London to Paris to New York, and the panic was aggravated by deliberate mark selling by certain German factions bitterly opposed to the "Fulfillment Policy" of the Wirth government.

A new economic blow struck Germany on Oct. 20, 1921, when the League of Nations decided arbitrarily that the rich industrial basin of Upper Silesia would be partitioned from Germany and given to Poland. The surprise League decision came despite a March 1921 plebiscite, as mandated in the Versailles Treaty, in which an overwhelming majority had voted to remain German. This devastating economic loss of Upper Silesia unleashed panic within Germany anew, fuelling even more German capital flight or conversion of paper marks into goods.

By the end of November 1921, the mark had plunged to 276 to the dollar, and by early 1922, the cost of living index had risen 2,400%, compared to the end of 1913.

At this point, the Reichsbank began to greatly accelerate printing new bank notes, apparently in an attempt to prevent the bankruptcy of industries and agricultural enterprises unable to get ordinary bank credit. The Reichsbank expanded its discounting of commercial bills in 1922, from 1 billion to 422 billion. Not surprisingly, by June 1922, the mark was nearly in free-fall, or at least it seemed, by comparison to what had gone before.

It was only a foretaste. The mark went from 300 to the dollar in June, to 8,000 by December 1922. German inflation had entered a qualitatively new phase. Newspapers printed charts with the daily currency fix, and the mark was an object of everyone's obsession. Everyone suddenly realized that the mark was galloping into the abyss.

At that point, every citizen who could, in effect began to speculate against the mark, in a frantic bid to protect themselves as best they could in a desperate situation, further aggravating the crisis.

Rathenau is assassinated

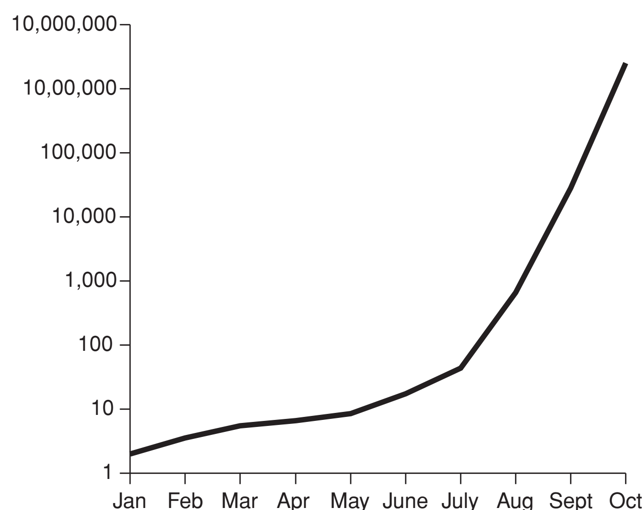
The mood rapidly turned to hysteria on June 24, 1922, when Foreign Minister Walter Rathenau was assassinated, only two months after signing the Rapallo Treaty with the Soviet Union for improved trade and economic relations. Rathenau had been a symbol of a democratic Germany, and one of the most vocal proponents of the policy of fulfillment, which sought to solve the reparations impasse by concession and agreement. Under fulfillment, Rathenau and others believed they could, by demonstrating a good-faith effort to pay, at the same time convince the Allies that the burden of reparations was impossible to meet, and thereby get suspension or relief. His assassination marked a decisive turning

point in the German inflationary process.

Inflation suddenly became runaway inflation, as the German population panicked. Ordinary Germans suddenly realized that it was not "prices" which were rising, but the mark which was collapsing in value. In the four weeks after Rathenau's murder, the mark went from 320 to the dollar to 538. By August, it was at 1,426. The cost of living index shot from 41 in June 1922 to 685 by December. (Recall, that it was 1 in 1913 on the eve of the war, or a 68,500% rise in less than a decade.)

This rate of currency depreciation and price inflation meant that the real, inflation-adjusted value of the state tax revenues was able to cover only a diminishing fraction of necessary costs, meaning the Treasury had to issue yet more bonds and bills to cover the deficit, further fuelling inflation. The entire population, no longer only a handful of the wealthy, attempted to convert their paper marks into something more secure. Any German able to get his hands on foreign currency hoarded it, further forcing the mark down. The Wirth government passed 40 laws, in a vain effort to forbid purchase of foreign currency by citizens, and to force those with legitimate trade-related foreign currency to turn it over to the Reichsbank. The laws were ignored; confidence in government itself had vanished.

FIGURE1
Hyperinflation in Weimar Germany, 1923
(trillions Reichsmarks outstanding)



Source: *Zahlen zur Geldentwertung in Deutschland 1914 bis 1923.*

Occupation of the Ruhr

The final phase in the now awesome rate of German inflation came when French and Belgian troops occupied the Ruhr industrial heartland in January 1923. The hard-line Germanophobe government of the newly elected French Prime Minister Raymond Poincaré, determined to show its resolve to impose the Versailles dictates with "utmost rigor," as part of French policy to deliberately keep Germany economically weak and to neutralize any future military threat.

Ironically, the French policy set off events which a decade later led toward the actions of the Montagu Norman-Hjalmar Schacht-Baron Schröder cabal, Hitler's legal coup détat, and the beginning of just that French nightmare of a resurgent, militaristic Germany.

The pretext for the French occupation was a dispute over delivery to France of telegraph poles and coal. Claiming that the German government was cheating on the precise amount of its Versailles obligations, Poincaré ordered the occupation. At the moment that French and Belgian troops entered the Ruhr, the government of Chancellor Wilhelm Cuno ordered a stop to further reparations to France and Belgium, and forbade any German official from following the orders of the occupying forces.

Poincaré responded by evicting all German officials from the Ruhr, setting up French administration, and economically cordoning off the region from the rest of Germany. Bank and regional Reichsbank funds were seized, along with inventories of mines and factories, to meet the French reparations demands.

A German policy of encouraging passive resistance brought the factories and mines of the Ruhr to a virtual halt, despite French efforts to bring in French personnel to keep them running. The economic impact of the loss of Germany's industrial heartland was devastating. With 10% of Germany's population, the Ruhr produced 80% of its coal and steel and accounted for 70% of its freight traffic. In addition, the Cuno government had to maintain financial support to the striking workers in the Ruhr. The printing presses went into even higher gear.

The policy of passive resistance in the face of the Ruhr occupation, pushed German inflation to the now infamous hyperinflationary levels (**Figure 1**). As the resulting social chaos and unrest grew, in August 1923 the Cuno government resigned, and was replaced by that of Gustav Stresemann, who at once ordered an end to the passive resistance and halted support payments to workers. In late November, at the peak of the hyperinflation, an agreement, encouraged by the Stresemann government, was signed by the French and Belgian government forces and the Ruhr industrial representatives, according to which the German industries would pay taxes and deliver their products directly to the Allies. The agreements remained until the Dawes Plan was signed in August 1924. The end of Weimar hyperinflation coincided with the end of the French occupation of the Ruhr.

The social impact of hyperinflation

The social and psychological impact on the population were incalculable. In June 1922, German unemployment

TABLE 2
Dollar exchange value of the Reichsmark

Year	Value
1913	4.20
1914	4.28
1915	4.86
1916	5.52
1917	6.58
1918	6.01
1919	19.80
1920	63
1921	105
1922	1,886
1923	534,914,000,000
Nov. 23, 1923	4,200,000,000,000

Source: Lombard Street Research, Brian Reading.

stood at a low 1%, rising to 2.8% only by December of that year. Export industry, under the cheap mark, was booming. Ruhr coal miners worked overtime to fill export orders. The mine workers were forced to work more, simply to try to compensate for the disastrous decline in their purchasing power. A similar situation prevailed in steel and other export industries.

The trade unions could gain only an ever-diminishing share of the price inflation through wage increases from their employers. Strike pressure had won the concession of a sliding wage scale to reflect the price rises, but the rise was so rapid that, by the time the official cost of living index data could be gathered, announced, and applied to wage rates, the inflation had galloped ahead, depleting the real value of the wage.

By 1923, the rate of inflation was so high that the value of a paycheck sank between the time it was handed out in the factory and the time the worker could race to the shop to buy something with it (**Table 2**). A sliding scale of wages was introduced in the attempt to bring order to this situation.

The result of the sliding-scale wages, however, was to add a savage wage-price cycle of inflation. Prices increasingly reflected the collapse of the mark. From an index level of 100 in July 1922, just after Rathenau's assassination, prices rose by 30-fold, to 2,785, at the time of the Ruhr occupation in January 1923. By July, prices had soared to the unbelievable level of 74,787 compared to the level of 100 a year before. By September, it had reached 23,949,000, and by November, 750,000,000,000.

Most citizens' savings were destroyed. Living standards collapsed. While a few industrialists, such as Ruhr steel and coal baron Hugo Stinnes, were able to accumulate immense fortunes at the beginning of the inflation, the majority of the population was pushed into poverty.

To compensate for the skyrocketting prices of necessities, white-collar workers, unable to secure wage hikes, turned to stock market speculation in hopes of winning enough to survive. As German industrialist Richard Merton noted in 1921, "A very large portion of German consumption among the middle-income groups, for example white-collar workers, is paid for by speculation on the bourse."

The past five years in the United States have mirrored this trend, where households put all their savings into stock mutual funds or 401-K pension plans.

Ironically, low-skilled, white-collar workers were in high demand because of the exploding volume of paperwork in the final phase of the inflation, to carry out the enormous administrative calculations caused by the constant change of money values, counting, and moving of money itself. One of the largest employers became the Reichsbank, where the money was being turned out in gargantuan volumes.

To most Germans, however, the inflation became an unimaginable disaster. Anyone who was unable either to push prices up, as industrialists did, and repay old debt with an increasingly worthless currency, or to demand wage gains, as trade union members could somewhat, lost. Indeed, the French accused the German government of deliberately pursuing inflation in order to get out of their reparations obligations.

Most of the middle class, who relied upon holdings in money, rather than tangible goods on productive assets, saw their life savings wiped out. Pensioners saw the value of their retirement payment, fixed in a stated amount of marks, become worthless in a matter of months. Citizens, mostly middle income, who had been persuaded, out of patriotism, to buy the flood of war bonds, found the value of their fixed-income bonds vanish. As the value of their fixed income from investments vanished, the government continued to tax their "capital gains" from the bonds.

More than half of all German university students were forced to take on extra work on farms or in factories to survive, as their fixed stipend, or family support rapidly became worthless. While the cost of a university education was not high, most students depended on family savings to get through, and most middle-income families drew on their bonds or other savings to put their children through school, not unlike many U.S. families who count on mutual fund earnings today.

Even the once-prosperous small and middle-sized entrepreneurs of the *Mittelstand,* the heart of German economic life, were forced to sell off personal valuables and household possessions to survive. By 1922, such sales were organized on a mass scale through formal housewives' associations, who centralized the disposal of peoples' cherished possessions. Salesrooms were set up in local savings banks to make the process as efficient as possible.

One observer noted, "A walk through the small salesroom with its tables and glass cases is heart-rending. There lie

spread out so many lovely things so pleasing to the eye—silk shawls, fine linen, old porcelain, silver . . . everything that once decorated a house."

Physicians asked their private patients to pay in goods, as money had become worthless. A consultation fee would be paid with a pound of butter or a sack of potatoes. Doctors would set out on house calls, only to return because they hadn't enough money for trolley fare. While not all middle-income families were ruined, and some actually were able to profit from the misery of others, a large minority was utterly ruined by the collapse of the mark in what was termed "the vastest expropriation that has ever been effected in peacetime."

Pensioners, whose survival depended on life insurance annuities or on small coupon payments from their investment in "safe" Reich bonds, i.e., with claims against "debtors," found that they were paid "mark for mark," that is, a mark of 1913 nominally equalled a mark in 1923.

Entire home mortgage debts were repaid in worthless marks. In one case, a full mortgage repaid gave the recipient only enough to buy a two-week vacation in a cheap boarding house. Small rental apartments were a common source of added income for many middle-income Germans of the day. While many such small landlords benefitted from paying their mortgages with worthless money, they also found that their rental income was equally worthless. The landlord was legally responsible for maintaining his property, whose cost remained high. Neglect of property maintenance during the war years was often compounded by theft of door-handles, stair carpets, metal fixtures, light bulbs—anything which might be bartered by someone desperate. Thus, property often fell into disrepair, and slums grew up. Tenants began to resent "greedy" landlords.

The broader social effect of the expropriation of the middle class in Weimar Germany was a festering resentment toward the democratic regime of the Weimar Republic. That resentment was exploited by a new radical party of the "little man," the NSDAP of Adolf Hitler, who first burst on the scene in the depths of the hyperinflation in 1923 in the failed Munich "Beer Hall Putsch."

Omens for today's crisis?

"All well and good," a reader might say. "But what does this all have to do with us? Where is the hyperinflation today? There are no war reparations on the United States or other major industrial economies."

In fact, prices over the recent past have fallen to the lowest levels since the early 1970s. Central banks, from the Federal Reserve under Alan Greenspan to the European Central Bank, constantly remind us of how benign inflation has become. It almost does not exist. True, recently the U.S. Consumer Price Index showed a slight rise, 0.7% month-on-month, and the Fed tilted toward possible future rate rises to "preempt inflation." But this hardly constitutes hyperinflation of the Weimar era.

And in Japan, the problem is a collapse in prices, i.e., deflation, not inflation. Where, then, is the hyperinflation?

The answer is that it is not only being created by deliberate government policies, but that, when least expected, at some point in coming months, it will explode with a fury comparable to that Germany's in 1921-23. Consider the following. Lyndon LaRouche's *Feature* story, "The Economics I.Q. Test" (*EIR,* May 14), lays out clearly the process of today's imminent hyperinflation. As LaRouche explains, its roots go back to the misguided policies of the U.S. Federal Reserve and successive U.S. administrations, particularly following the August 1971 decision of the Nixon administration to decouple the dollar from gold. As with the Reichsbank in 1914, that decision opened the door to inflation.

However, unlike in Germany in the 1920s, the United States was in the unique position that its currency, the dollar, was not a mere national unit of account, but the foundation of the entire postwar global trade and payments system. The inflationary effects of the 1971 abandonment of the Bretton Woods agreements of 1944, were spread across the globe. It was not until the oil price explosion of 1973-79 that the world began to be aware of "inflation problems."

Time after time during the 28 years since August 1971, governments have backed off from addressing the fundamental problems of a monetary system run amok. For politicians who wanted to get reelected, it was far easier to turn on the printing presses, and to increase public debt, to hold the strained system together until after the "next election."

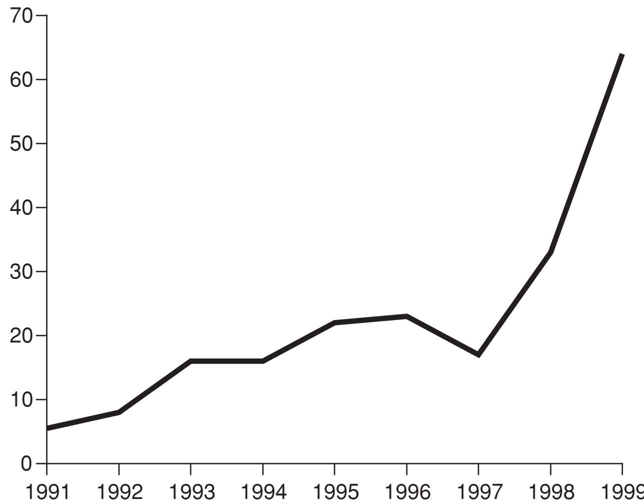
In 1995 that process reached a qualitative new phase, just as in the early phases of Weimar inflation. Japan was the center of this phase. During the 1980s, Japan underwent significant inflation. Its effects, however, were not manifest as they were in Weimar. Because of the very high rate of personal savings, the rising savings of Japanese went into speculative investment in the Nikkei stock market, or into real estate in Japan, and later in the United States and Europe. Japan saw an "asset inflation," which, by 1990, had reached alarming dimensions, as the Nikkei Index of stocks soared past 39,000.

The total capitalization of the Tokyo Stock Exchange had surpassed that of the United States. Paper assets of Japanese banks made them the world's largest.

This asset inflation in Japan came to a bitter end in late 1990-early 1991, when the Bank of Japan tried to stop the speculation and bring the frenzy under control. The Japanese financial system crashed. The Nikkei plunged to 16,000, where it remains, eight years later. Prices of real estate, the main collateral for the Japanese banking system, fell more than 60% from their peak, and continue to decline today.

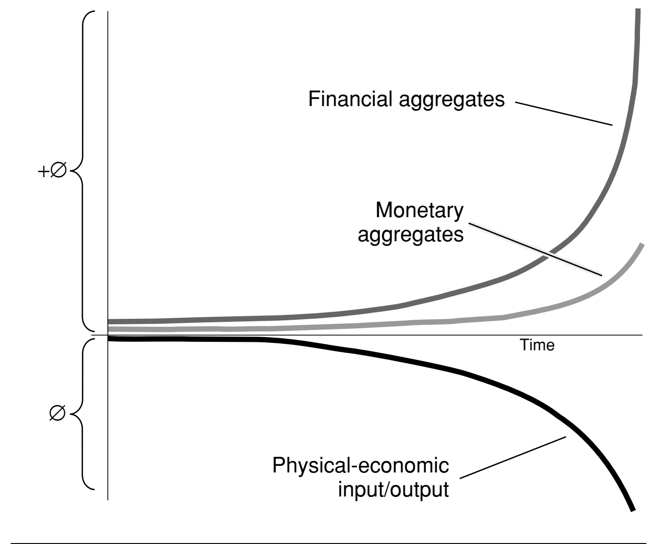
Then, in spring 1995, as the Japanese yen soared to a postwar high of 80 to the U.S. dollar, Japan faced a meltdown

FIGURE 2
Japanese government bond issues
(trillion yen)



Source: Japanese Ministry of Finance.

FIGURE 3
A typical collapse function



of its banking system, which would have pulled the United States and the rest of the world with it.

At that point, a new form of Washington-Tokyo "crisis management" took hold. The Federal Reserve made available an emergency liquidity line of $500 billion, should any Japanese bank in New York have liquidity problems. The Bank of Japan began to push down Japanese interest rates, to force capital out of the yen and ease the inflated currency, which was killing exports. Japanese funds began to pile into the U.S. bond market as never before, pushing U.S. interest rates abnormally low, and kicking off the latest unparalleled bout of "irrational exuberance" on the Dow.

At the same time that the Bank of Japan was printing yen to push the discount rate to a peacetime low of 0.5%, the Ministry of Finance was issuing record levels of public debt to finance "public works" as fiscal stimulus projects to stabilize Japan's economic free-fall (**Figure 2**).

Yet, the asset inflation of the 1980s and the political inability of Japanese politicians in the early 1990s to forge a consensus to reorganize the entire system, meant that the public works was pouring so much money down a hole. Bridges were built to nowhere in rural provinces, where the Liberal Democratic Party needed votes. The real economic potential of Japan, only a decade earlier the technological giant of the world, was rapidly falling into obsolescence.

The bad debts of the banks in real estate and other projects were quietly rolled over to save face. Their nominal value rose to the point that today, total non-performing loans of the Japanese banking system, including the giant Postal Savings Bank, KAMPO, exceed $2 trillion, according to the best private estimates. Japan has thus been the first major sector of the global system to reach the point defined in LaRouche's "Triple Curve," or "Typical Collapse Function" (**Figure 3**), in which the divergence in the size of monetary aggregates in relation to the collapse of real economic aggregates is so extreme that all efforts to spend out of the crisis merely aggravate the crisis, just as in Weimar Germany in 1921-23.

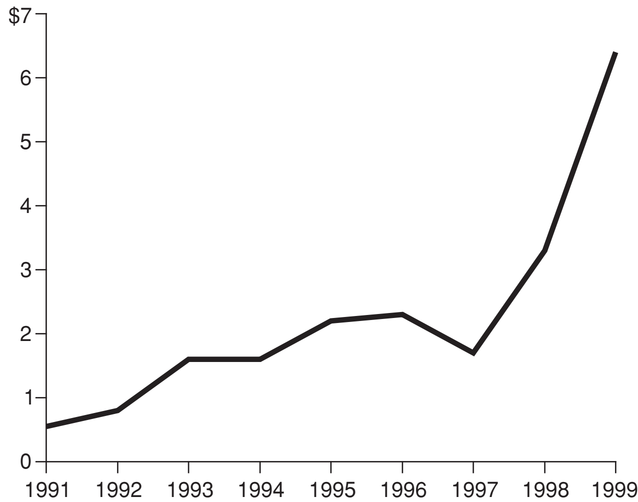
The collapse of Asian markets beginning in May 1997 dealt the fragile Japanese system a crippling blow, as some $253 billion in Japan bank loans to Asia alone suddenly became worthless, adding to the hidden losses of Japanese banks.

Early this year, in a desperate effort to counter the effects of the "Asia crisis," the Bank of Japan pumped sufficient liquidity into the system to put interest rates at effectively zero. Today they are slightly higher, but the government faces a pre-programmed debt explosion over the next 3-5 years, at least.

Since the beginning of the crisis in 1991, Japan's public debt has soared to historic highs. But by 1998, the crisis had so deteriorated that the Obuchi government forged emergency programs on a scale never seen. A bank "restructuring" bill was passed, creating a fund of up to $500 billion to bail out Japan's insolvent banks. It is reliably reported that only one of the 19 major Japanese banks is technically solvent today.

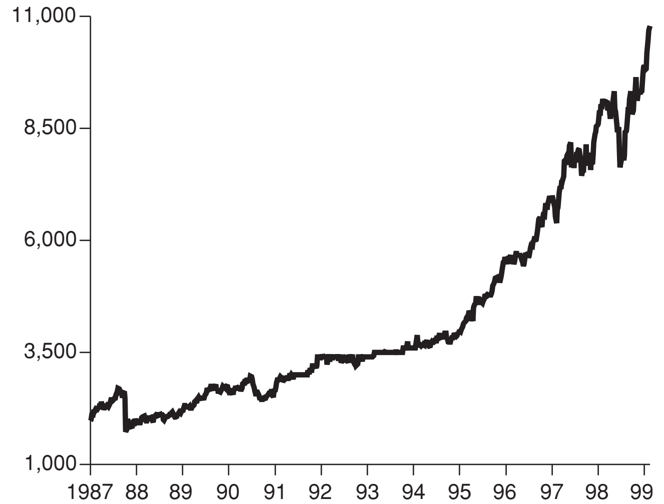
Already in 1998, as compared with 1997, the rate of new public debt issue, Japanese Government Bonds (JGBs) and short-term paper, was double, or more than 30 trillion yen (about $250 billion) a year. Beginning in July 1999, the

FIGURE 4
U.S. money supply (M3)
(trillions $)



Source: Federal Reserve.

FIGURE 5
Dow Jones Industrial
(Average weekly closings, 1987-99)



Source: Dow Jones.

annual level of new government debt issue will again double, to near $500 billion. Soaring unemployment, as private companies slash jobs for the first time since the 1930s, adds to government costs, and the demographic pressures from the world's fastest aging population, combined with hundreds of billions in pensions already owed, for which companies have no funds in reserve, owing to the collapse of the stock market and real estate assets, all create the preconditions over the coming 12-18 months in which the only conceivable policy course, whatever the government, will be to deliberately inflate out of the debt.

That acceleration of the printing press creation of new money in turn will collapse the yen, as well as any vestiges of credibility in the mythical Japanese "recovery." Thus, in many respects, Japan's post-1995 policies to create a cheap yen also laid the basis for the crisis which erupted during 1997-98, starting in Asia and, by last August, spreading to Russia and other emerging markets. The default of Russia last August and the collapse of the $3 trillion Long Term Capital Management hedge fund in late September led Greenspan's Fed to embark on the greatest liquidity operation in postwar Fed history (**Figure 4**), to provide artificial life support to the dying global dollar system.

In addition to a series of interest rate cuts between September and November, and the direct injection of money into the banking system, the Fed provided banks directly with a level of bank free reserves as never before. The government mortgage agencies, Fannie Mae and Freddie Mac, were deployed to buy up a record $128 billion in mortgage bonds to prevent the collapse of the $635 billion collateralized mortgage market. Liquidity flowed as never before, all in the name of "saving the system."

The consequences of this last round of money printing and liquidity creation by the Greenspan Federal Reserve, together with the new phase of Japanese debt creation about to be unleashed, are giving an inflationary impulse to the global system which, barring a fundamental Chapter 11 reorganization and write-off of trillions in unpayable debt, will make the 1921-23 Weimar experience appear mild by comparison.

Currently, the effect of the Fed's money-printing, easy-liquidity policies since last September has shown up in what can be identified as the onset of hyperinflation. But, unlike that of Weimar Germany, its negative consequences so far have been less obvious, as the liquidity has gone into the only place in the economy where double-digit paper profits can be had—the stock market (**Figure 5**). Today, the combined paper value of all stocks traded on public exchanges in the United States—the New York Stock Exchange, NASDAQ, etc.—exceeds $13 trillion. Any number of triggers are likely to pop the bubble, and, aided by the presence of tens of trillions of dollars in the stock index derivatives, the reverse-leverage effect on stock values will take the savings of most of middle America down with it, just as the collapse of the reichsmark took the savings of Germans with it. The fact that today's imminent hyperinflation crisis takes a different form from that of Weimar Germany, in no way makes it any less threatening to the world.