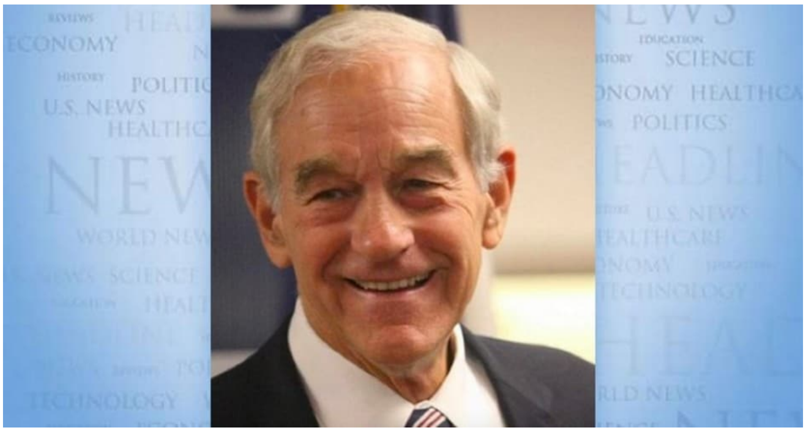
Inflation Even Hurts the Penguins



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A recent video shows penguins at a Japanese aquarium rejecting the cheap fish the aquarium has substituted for the higher quality fish the penguins are used to receiving. The reason the aquarium switched fish is because rampant inflation has made it impossible for the aquarium to afford the higher quality fish. The penguins' reaction illustrates the flaw in governments claiming that even if inflation makes it impossible for you (or penguins) to eat steak (or higher quality fish) your quality of life has not been diminished as long as you can afford hamburger (or cheap fish).

Minimizing the impact of inflation by taking a "let the penguins eat lousy fish" approach is the basis of the "chained CPI" that is one of the ways the government underestimates price inflation. According to John Williams of Shadow Government Statistics, the real inflation rate (calculated without the government's "modifications") is over 15 percent! While they continue to understate the true rate of price inflation, government officials have been forced to admit at least that price inflation has reached levels not seen in forty years.

This has led the Federal Reserve to raise interest rates. But, so far, the Fed's rate increases have not stopped price inflation. This is why the Fed's next rate increase may be a rare full percentage point increase. Yet, even if the Fed raises rates by a full percentage point, rates will still remain well below what they would be in a free market. The Fed cannot raise rates anywhere close to market rates because doing so would make it impossible for debt-ridden consumers, businesses, and the federal government to manage their debt.

Fear of causing the bursting of the many bubbles it has created — especially the federal government debt bubble — means the Fed's efforts to halt price inflation will fail. However, the Fed's actions will increase unemployment and obstruct economic growth. This will lead to, if it hasn't already, a return to the 1970s phenomenon of "stagflation," although this time it will be even more painful.

The problem with the Federal Reserve is not that it pursues "bad policies." The problem is the very existence of a secretive and unaccountable central bank with the power to manipulate the money supply and interest rates. Money's function is to provide an objective unit of account, so market actors know the value of goods and services. When the central bank manipulates the money supply, it arbitrarily changes the value of money, making it impossible for market actors to determine those values. The Fed's manipulation of interest rates also creates economic chaos by distorting the signals sent regarding economic conditions. This leads to widespread malinvestments, resulting in booms followed by busts. Since this system leaves elements of the market intact, it can survive and even appear to thrive for an extended period of time. But eventually the fiat money system will collapse.

Since the fundamental flaw with the Federal Reserve is its very existence, reforms, such as making the Fed follow a rules-based policy, will not "fix the Fed." The only way to return to a rational economic system is to end the Fed. If there is not sufficient support to end the Fed, Congress should still audit the Fed and create competition by repealing the legal tender laws and ending all capital gains taxes on precious metals and cryptocurrencies.

Ron Paul is a former U.S. congressman from Texas. This article originally appeared at the Ron Paul Institute for Peace and Prosperity and is reprinted here with permission.