# *Kaput*

It has been customary to draw attention to America's problems (well documented a hundred times over, most recently by the Germans who trashed QE2) but it may well be that Euroland blows up first. The European Central Bank (ECB) may be more sanctimonious than the Fed, but it's not much different. Today the problem is Ireland; tomorrow, who knows? Euroland's paroxysms are sad, the finger pointing is sad, and the efforts taken to portray the Irish bailout as a loan are pathetic. Are banks in thrall to governments or are governments in thrall to banks? Both, we are sure. And it's pretty clear Euroland is more concerned with its banks than the inhabitants of its weaker member states.

Above all, however, Euroland *fonctionnaires* are concerned with Euroland *fonctionnaires.* There are jillions of them, they provide the economic drive (using the term loosely) for Brussels and Belgium, the EU has 137 "embassies" around the world, it is working on a space project GPS system ("Galileo") at a cost of billions, it is building a lavish new European Council headquarters (whatever that is) and it appears oblivious to the austerity sweeping Europe. If the Euro experiment goes *kaput,* who will pay the hordes of deadbeats on the EU payroll? Frau Merkel?

Is the business press complicit in misrepresenting unhappy realities? Generally, yes. They are on message, but it's the policymakers' message, structured to confuse insolvency with illiquidity, cures with palliatives. If Ireland or anybody else borrows *x* tens of billions of Euros at *y%,* is it any less broke? Going to the loan sharks may buy a little time but it will only exacerbate the indebtedness.

But woe to the journalist that suggests the Euro may be coming to the end of the road, the situation is terminal. Rather, play the game and support the issuance of ever more sovereign bonds (never mind that they may be worthless) and stuff them down investors' throats, or, more likely, investors' agents' (the banks) throats. More good money (at least new money) after bad.

However, the situation is terminal, or at least, half terminal. Enabling Ireland (or California, Ontario or Greece) to plunge ever deeper into debt is hardly doing their people a favour. The numbers are horrendous. And the bond market seems to be figuring it all out – no matter how many bailouts policymakers engineer, the problems will be recurring in ever-greater magnitude.

Bailing out all today's disasters would be akin to bailing out a thousand Enrons. For the moment they try. But sooner or later someone with political clout will ask "Why?" He might point to Argentina nine years ago, or Iceland* two years ago. Both countries rejected big brotherly advice, repudiated some international debts, devalued, went their own way and are much the better for it today. Put it this way: if a Greek politician were to say "Vote for me, I will repudiate much of Greek indebtedness and I will stop taking orders from the Germans. I will take Greece out of the Euro and bring back the Drachma at about half Euro value. We will get more for our olive oil but pay more for our fuel. Tourists will flock here and life will be good." Sooner or later this (or a similar) scenario will come to pass. Or, with Germany getting stronger (the weak Euro helps) every day, perhaps the German electorate will say "Enough! It's time to cut the anchor ropes." Finally, Germany might try to shrink Euroland and emerge as the dominant partner.

When the Euro was created all the members chipped a bit of gold into the ECB, but the big positions remained with the big countries. Interestingly, Germany and France kept the Bundesbank and the Banque de France as massive, functioning institutions with big gold holdings. Was the ECB not enough? Or did France and Germany have a premonition that the Euro might not last forever?

Anywhere and almost everywhere in the Western World governments are trying to paper over problems, to borrow or print their way out of trouble. For example Ontario, erroneously seen as solid, plans to borrow over

* Iceland is apparently putting the prime minister who presided over the reckless expansion of the banks on trial for negligence.

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$100 billion over the next three years (representing a 40% increase in total debt) presumably just to cover operations. It took markets a surprisingly long time to recognize the sub-prime mess and the Irish mess, and markets are certainly taking their sweet time recognizing the Canadian mess. But loss of confidence in policymakers is spreading – just look at the recent collapse in the US municipal bond market.

Countries without a focus on wealth creation will soon be unable to borrow their way to prosperity, or even subsistence. Most people work to live, whereas Germans (the story runs) live to work. They don't just make steel, they make the machines that make steel, whereas, on the other hand, Canada taxes jobs, revels in a strong currency and (in Ontario) moves electricity (the lifeblood of industry) prices ever higher. Ontario builds condos the way Spain and Florida used to build vacation villas.

The US, interestingly, may emerge from the pending monetary shakeup better than expected. Amazingly, the dollar remains the world's reserve currency, holding its position at least partly by default. But after decades of eat, drink and make merry, America appears to have recognized the need for wealth creation. Nearly every big American corporation has closed its Canadian subsidiaries and brought the jobs, the trade and the tax base back to US. America still produces half its oil (more than many others) and drilling has returned to the Gulf of Mexico. America produces huge quantities of food, consumer and industrial products and (for better or worse) armaments. Exxon and Chevron together earn more than most countries and the list of other fat, healthy companies is as long as your arm.

America does not have enough going for it to deal with unemployment or an economy lopsided with the service sector. And, like the weak Eurozone countries, America's real estate problems cannot go away any time soon. Nevertheless America probably does have enough going for it (everything being relative) to benefit from both Euroland's problems and developing inflation (towards which it is contributing more than its fair share).

The recent floating (re-floating?) of General Motors may be a triumph of hope over experience, but the good news is that it signals a return of the public to the stock market. That is hugely significant. Having been scared stiff since 2008, they are now putting a toe into the equity pool. In time they will be leaping in fully clothed screaming "no more cash, get me in stocks!"

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