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Public Debt and Our Investments

Future investment decisions will need to take into account large amounts of government debt and the effect it has upon an economy. In the chart below we can observe every country's per capita debt. The total of these 10 country's debts is over $40 trillion. That is a tremendous amount of money upon which to pay interest every year, and there is no plan to pay back any of the money that is owed. Note that the U. S. GDP is about $14.5 trillion, and our GDP is 30% of world GDP of about $50 trillion.

Ten Countries Deepest in Debt Per Capita (*)

Country	Amount
USA	$48,000
Ireland	$40,000
Germany	$38,000
Belgium	$38,000
United Kingdom	$36,000
France	$34,000
Japan	$34,000
Italy	$32,000
Greece	$28,000
Portugal	$26,000

(*) Total public debt divided by total population (308 million)

None of the above debt was created by war. All borrowed money was for "social services".

David Hume (1711-1776) was one of the great thinkers of the Age of Enlightenment. His writings heavily influenced our Founding Fathers in writing The Constitution. A few things he wrote in "Of Public Credit" concern our current economic predicament:

- "Abuse of the public treasury, either by welfare or military engagements, are certain and inevitable; poverty, impotence and subjugation to foreign powers."
- "War is attended with every destructive circumstance; loss of men, increase of taxes, decay of commerce, dissipation (inflation) of money, and devastation of sea and land".

- "The practice of government contracting debt will almost infallibly be abused, in every government. It would scarcely be more imprudent to give a prodigal son a credit in every banker's shop in London, then to empower a statesman to indebt the country"

David Hume's influence provided the impetuses for three clauses in The Constitution:

1. All debts to be paid in gold and silver;
2. Any war must be voted on by Congress;
3. No increases in debt without the authorization of Congress.

Many other clauses came about as a result of Hume's reasoning, but these apply specifically to the future value of our money, our current debt, and its affect upon investments.

Those three constitutional provisions, having been followed, would have prohibited the creation of The Federal Reserve System. We would not have had inflation (the dollars purchasing power remained stable from the Currency Act of 1789 until the confiscation of gold by the government in 1932). We would not have been able to enter World War I without a federal reserve system to provide the money that would not be provided by Congress. Without the U. S. entering WWI, it would have been just another European confrontation (we were only actively engaged in combat in Europe the last seven months of the war). Without WWI there would have been no WWII, which was a continuation of WWI. Finally, we would not have the huge central government we have today, or any of these debts.

What does this have to do with the stock and bond markets? Understanding how our system was set up to work, and seeing that it is not working, gives us an opportunity to "fix" things and move forward. In the process, we must be mindful of the effect the economy can have on our personal investments. Because there has never been this volume of debt before in history, it's not possible to compare our current economy to history and see a way out. To "fix" our economy, we would have to do away with the Federal Reserve System and have real "free market" banking, not manipulated interest rates like we have today that favor the government at the expense of savers. Most unnecessary government departments would need to be closed, saving hundreds of billions of dollars that's wasted a year. The 10th Amendment of The Constitution states that "all powers not herein provided for are left to the states, and local governments, respectively". We need to privatize broken government programs like Social Security, Medicare, and Medicaid to name a few. We have to get out of everything our federal government is involved in which is not provided for constitutionally.

Realistically, this is not going to happen. We have been talking about it for decades; politicians have promised us satisfaction for decades, and the opportunity to 'right the ship' during this Congress has been lost. Interest rates are fixed by the Fed at a rate below inflation, just like Japan did 20 years ago. Japan has been mired in an economic mess for more than two decades—since we have adapted the same solutions, it is likely we will end up the same way: stagnation.

Given the assumption that we are really not going to do anything politically, our next question is how to protect investments from increasing taxes, inflation, and stagnant growth. We know that bonds do not pay anything, cash does not pay much, and inflation continues to run at least 3-5% annually.

What to Do?

Gold and silver are always great hedges, but more than 5-10% of that in a portfolio is too much for most investors. Gold and silver, does, however, protect against inflation and the loss of the purchasing power of the dollar. Bonds, as noted above, are a bad investment because they don't pay anything, coupled with the fact they are deteriorating in value with inflation. Cash is good if one wants to remain liquid and try to find good investments as they become available in terrible markets like this. The only stock investments that make sense are AAA-rated companies that pay more than 3% in dividends annually, whose dividends are increasing annually, and whose cash flow is significant enough to continue to pay the dividends and weather the storm of increasing taxes and inflation. There is too much risk in owning the vast majority of stocks and bonds available today.

There are two types of assets currently deteriorating in value: real assets (land, buildings, and other hard assets), and paper assets like stocks, bonds, and cash. The value of hard assets, particularly real estate, gold, silver, and so forth, is that they are not replaceable. Real Estate and a few selected stocks seem to be likely to provide future economic growth. They are also the assets that have done well in Japan the last 20 years of Japan's stagnation. With continuing borrowing and inflation likely to produce some kind of future large currency re-evaluation, hard assets will maintain relative value.

The whole country needs income, and income is going down. What used to be "income" is now going to pay interest on the country's debt. There will not be a resolution to this deterioration of our private sector income until the public sector income stops going up. And this is likely to be highlighted by the stock market continuing to trade in the same range it has for the last few years, going nowhere.

Caveat Emptor.
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