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Our inflationary spiral into stagnation [1]

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An interesting bulletin came in from my friend Richard Jeffrey, economist at Cazenove Capital Management, on the state of the economy. The conventional (Keynesian) wisdom is that a little dose of inflation will stimulate (lasting) growth. Richard thinks that right, now, inflation is actually undermining our economic growth. But should we counter inflation with a rise in interest rates? Well, our economic masters worry that such a move could flatten our faltering growth even more. A conundrum.

Richard is certainly right to be worried about inflation. Inflation is an evil that makes sensible investment impossible. Who can tell which goods and services are really in demand when the price of all of them is shooting up? The 'noise' of inflation drowns out the 'signal' of the price system.

It now seems that quantitative easing ? a smart name for printing money ? gave the UK economy a boost, but a pretty brief one. The trouble is that the more money you create, the less people value it. So our devalued pounds now buy less abroad. That means higher energy and commodity prices. And energy and commodity prices have been rising anyway, as many of the world's economies recover from the crash.

So there you have it. Growth is being slowed by rising raw material and energy prices, which are the direct result of quantitative easing. Which in turn pressures the monetary authorities to keep interest rates low and stoke up the same inflation that is causing the low growth. Sounds to me that we are in a downward spiral unless we bite the bullet and move back to money and credit reality soon.

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