Global Recovery Manual

Bill Houston

SAMPLE

Part 3 Chapter 1.
Preparing the State for the Digital Age

"Never in the history of the world has there been a situation so bad that the government can't make it worse"

Anon, quoted from Marc Faber GBD Report

"That government is best when it governs least . . . It finally amounts to this: that government is best which governs not at all!"

Henry David Thoreau

"You can always sense incompetent politicians because they emphasise spurious issues away from the critical factors"

Anon.

In 2012 the reported UK government debt was £1,023 billion and private debt £3,200 billion making a debt to GDP ratio of 272%. However, if unfunded liabilities are taken into account the state debt rises to £2,300 by raising the total to £5.5 trillion and a debt/GDP ratio to over 355%. By 2015, the ratio will be higher.

Summary

Ever since Adam Smith proclaimed that individuals spend their money more responsibly than governments, politicians have tried to prove the opposite and every time they have failed. As the above simple calculation shows, the UK, with a budget deficit of now less than 7% and total debts of 350% of GDP, is technically bust and if it was a company, the directors would be acting unlawfully if they did not call a creditors meeting.

Fortunately for them creditors have other remedies such as refusing to buy or dumping bond or gilt offerings leading to a collapse of the currency, a government default, and a drastic cut in the standard of living. Likewise, governments have the capacity to defraud their creditors as they have done many times in the past and, more recently, in Greece and Cyprus. As this chapter is concerned with preparing for the Digital Age, another simple calculation for a developed nation today will show the actual scale of the problem.

Assuming an equilibrium total debt to GDP ratio of an optimistic 200% and the present levels of around 400%, then the collapse of credit would be twice the GDP; in the US this would be $30 trillion and in the UK £3 trillion.

However, any collapse of credit on this scale would be a likely fall in the GDP of an optimistic 20% (the US GDP declined by 50% in nominal terms from 1929 to 1933 with a debt/GDP ratio half that of today) so that the collapse of credit would be a fall in debt of 2.20 times the GDP. If through inflation, this would be enough to wipe out the capital of every lending and probably also financial establishment in the land; if through deflation this would eliminate many debtors. This could never be achieved in an orderly fashion unless foreseen; it would mean cuts of socialised expenditure to achieve a government expenditure less than one third of GDP.

As the next chapter will show, it is individuals, either separately or in groups, that will propel a national recovery, not politicians. All they need is the environment to take risks. This is why a government spend of less than a third of GDP is needed, accompanied by minimum regulation at a time when politicians' instinct is to control more. Failure to do this would mean crippling debt servicing costs.

Introduction

Several studies have suggested that the Digital Age (DA) would need some 2% of the population in agriculture, 3% in government, 10% in manufacturing and around 50% in service industries. This means that perhaps 30 to 40% of the population will have no regular jobs including the underclass the welfare state has created.

This is quite different from the heyday of late 20th century when the social democratic state was so omnipotent that politicians attempted to provide a safety net through which nobody can fall. At the same time it has become wasteful, inefficient, corrupt, arrogant and incompetent. As the Bumper Book of Government Waste shows the British government wasted over £82 billion of taxpayers money out of a total government expenditure of £519 billion. It is unlikely that this is a singular occurrence.

Yet this very omnipotence probably reached its pinnacle during the Second World War. Then whole democratic states were mobilised to create armies, navies, air forces and the weapons of war. In an age of mass production the Allies, particularly the US, out-produced by around a factor of ten the total output of the Axis powers. In this the state, as never before, controlled much of economic activity and in the name of winning the war, which deprived individuals of their natural freedoms. Most willingly acceded in the name of patriotism and there was no question of unemployment because everyone was involved.

Sixty years on, little has altered in the attitude of the state but the focus and competence has changed. In wartime able people were attracted to positions where they could affect the outcome. Now politicians, many of whom with no managerial experience, aim to stay in power to the exclusion of any contribution they can make either to their constituents or to their nation.

In the UK this has been exemplified by their attitude to the banking crisis. Instead of relating back to the US Glass-Steagall Act of 1933 which separated commercial banking from investment, banks have been socialised without this essential condition of separating the two activities. This has meant leveraging the state to previously unimaginable levels in peacetime to the detriment of future generations and the state taking on totally unknown liabilities that should rightly have been managed by the market.

Unfortunately, the political debate in France and elsewhere has shown little understanding of the underlying dynamics described in Part 1, so that policies are unlikely to change unless they are forced by events. In addition, unfortunately the first reaction to a crisis will be to enlarge state control and restrict freedoms instead of implementing the sort of contingency plans described in this chapter, in anticipation.

Only in rare countries such as Switzerland has the state focussed on the four issues for which they are deemed to be responsible, such as maintaining the value of the currency, external and internal security and maintaining internal finances in equilibrium.

Any remedial policies will not just have to reduce the size of the state, because the welfare state is not working in ways claimed by their proponents. For example, *The Economist* reported that by the turn of the century there was no employment in over one-tenth of British households with children; this figure was nearer one in seven towards the end of the decade. This means presumably that in excess of three million households are underwritten by the state. The National Audit Office commentated that one in ten live in workless households. This is not singular to the countries such as the UK, as other nations such as the US, Finland, Belgium, Australia and Canada had between 10 and 15% of homes without work. This is an appalling indictment on the state's priorities.

This will not be the only problem facing the state. During deflation, it is likely that as the economy shrinks, taxed revenues will also decline which makes it all the more important that other than bureaucratic means are found to manage spending. There could also be additional pressures on the public purse such as the potential crash of housing finance, the bursting of other credit bubbles, food and medical problems, likely wars over water, increasing threat of terrorism, mass refugees and possibly also pandemics.

All these are likely to arise during the first two decades or so of the 21st century against governments already reeling from excessive borrowing. How then is the transition to the Digital Age to be made without leaving millions, at present dependent upon the public purse, destitute?