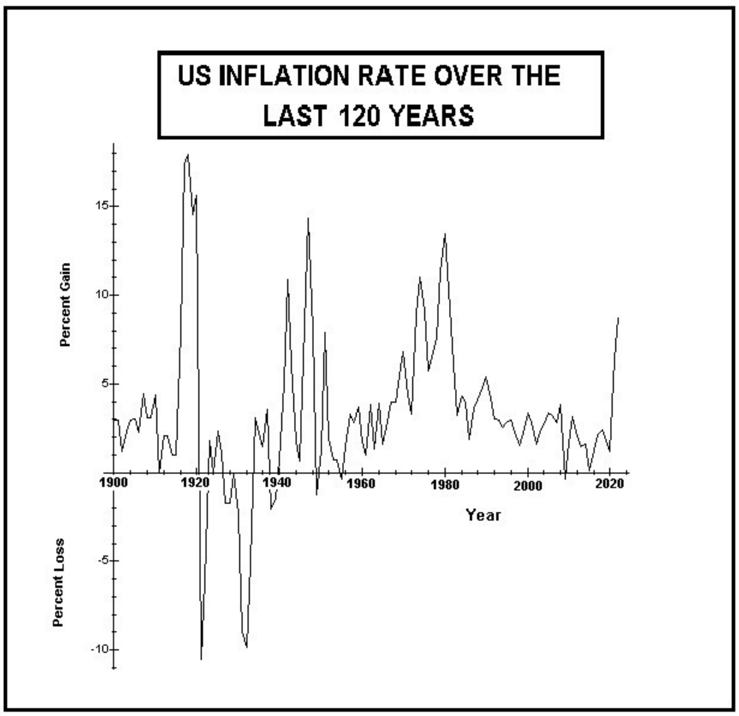
120 YEARS OF INFLATION IN THE USA

Recently The US has registered an overall inflation rate of 8.7%. At first glance this number is bit scary as it exceeds by a lot the average value of 3.15% since the founding of the Federal Reserve back in 1913. However, when compared over the last 122 years since 1900, there have been a total of three earlier periods when rates have been this high or higher as shown in the following graph-



I constructed this graph by looking up the average yearly inflation rates on Google for each year since 1900. The latest number is 8.7% and is probably twice as high when looked at via earlier measures. You can see from the graph that wars such as WWI and WWII plus Vietnam drove up inflation rates considerably in excess of the average value. Periods of deflation are seen to have occurred in 1920 and in the early years of the great depression. The latest rise in inflation is however not due to wars but mainly due to the Federal Reserve's policy during the last couple decades of excessively printing fiat paper money(quantitative easing) with their efforts to keep interest rates near zero.This printing of fiat money without proper backing became possible after 1971 when

Richard Nixon ended the conversion of dollars to gold as originally agreed upon at the Breton Woods 1944 monetary conference.

To combat this latest inflation one needs to-

(1) Have the stock markets continue to fall. This seems to be working over the last six months when some 10 trillion dollars have been wiped out from individuals and corporate portfolios just by the threat of slowly rising interest rates. The large market bubble created in the last decade by the Fed needs to be partially or entirely deflated before inflation will subside.

(2) Raise interest rates much more rapidly and in larger increments causing a continued drop in stock and bond market prices and a rise in mortgage rates. It should be possible for the Federal Reserve to accomplish this by bringing things down to the desired 3% inflation rate in a couple of years without their actions producing a severe economic recession.The dilemma the Federal Reserve finds itself in at the moment is that although large increases in interest rates will bring down the inflation it will also slow down the economy putting the country into a recession. This recession will start this fall at the latest. The best route would be for <u>the Fed to quickly raise interest rates in large chunks before the resultant recession takes effect</u>. Once a drop in inflation rates occurs, they should then rapidly decrease interest rates again to prevent the economy from sinking into a larger recession. The process can be repeated with the final intent being to bring the inflation rates down while skirting any heavier recessions.

Finally let me say a few words concerning worsening economic conditions occurring throughout world. In most cases the problems are caused by government overspending and trying to pay for it with fiat money. This may work for awhile but eventually will fail. The basic law of finance must always be kept in mind. It is that the return on capital depends only on effective interest rates present and the number of years such investments are held. That is-

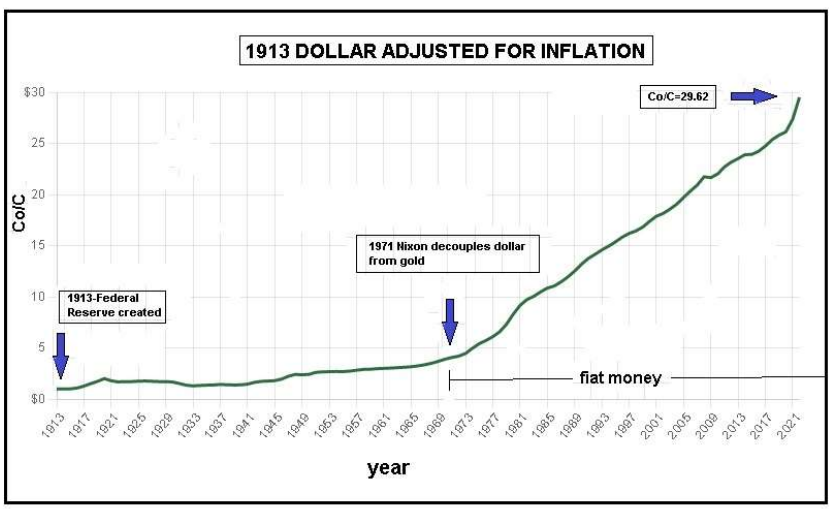
$$C/Co=(1+i)^n$$

So at i= 7% true interest return on one's capital will essentially double in ten years. On the other hand a 7 percent inflation rate will half ones capital in the same amount of time. A more accurate formula (upon neglecting taxes) is -

$$C/Co=(1+\text{percent return }-\text{inflation rate})^n$$

To have a net gain requires that the return rate exceeds the inflation rate. This is not the case at the present time, meaning that people and especially seniors, who have saved all their lives are presently being deprived of any net positive return on their savings. Instead their savings are being slowly but surely confiscated.

The policy of the Federal Reserve since its founding has been to support job growth while at the same time keeping the inflation rate low at less than about 3% per year. Even with such a relatively low inflation rates the loss in dollar value over the past 120 years has been large as shown in the accompanying graph-



Reading off of the chart, we see that the inverse capital value for 2022 produces-

$$C/Co \approx 29.62$$

over the n=109 years since the founding of the Federal Reserve.The dollar has thus been reduced by a factor of 29.62 in value meaning that a present day dollar buys only what 3 cents would have bought back in 1913. This loss in dollar value over the years is a highly undesirable record for the Federal Reserve to have. One can blame the accelerated poor performance in recent years on the later day quantitative money easers especially Greenspan, Bernanke, Yellen, and now Powell. They sold the country down the road through their extreme quantitative easing resulting in ultralow interest rates and eventually producing the high inflation rates which we are now seeing. An immediate raising of interest rates in large segments of a percent or so is called for to fight the present growing inflation scourge.

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