Congressman Ron Paul
U.S. House of Representatives
Financial Services Committee
Full Committee Hearing on "Implications of a Weaker Dollar for Oil Prices and the U.S. Economy"
July 24, 2008

Mr. Chairman,

The root of our current economic malaise, the weak dollar, the high price of oil, and the collapse of the housing market, comes about because almost no one understands what inflation is. Inflation is an increase in the money supply, which occurs by various methods, the printing of currency, low reserve requirements, Federal Reserve open market operations, etc.

In Germany in the 1920s, South America in the 1980s, and Zimbabwe today, everyone recognizes that inflation was caused by the government running the printing presses non-stop, with the resulting exponential rise in prices being the necessary result of monetary growth. Yet somehow, both the empirical and theoretical reality of inflation as a rise in money supply is ignored in this country. Inflation is conflated with price inflation, the increase in the overall price level, and is viewed as something both endogenous to the market economy while at the same time influenced by exogenous price shocks.

Because no one understands that inflation is growth in the monetary supply, no one is able to combat it effectively. We hear all sorts of hand-wringing about increasing inflation, and all sorts of explanations about how rising oil and food prices will make inflation worse. At the same time, the fact that MZM, the closest approximation to total money supply that still is reported by the Fed, is still rising by almost 15% per year and that M2 is rising significantly as well is quietly ignored. The pundits have causation backwards, it is inflation that leads to rising prices of oil and food, and not vice versa.

Until the cause of inflation is understood, no effective strategy can be undertaken to combat it. The problem, however, is that the government does not want inflation to be done away with. Inflation benefits debtors and harms creditors, and the United States government is the biggest debtor of all. The United States government, the banking monopoly under the Federal Reserve System, and politically-connected firms and industries are the first entities to take advantage of new money injected into the system, before prices increase. As the increased supply of money begins to chase the same number of goods, prices rise, and the average American suffers. Poor and middle class Americans are always the hardest hit by inflation, as the weakening dollar makes the imported goods that many Americans depend on more expensive.

As Chairman Bernanke admitted last week, inflation is a tax, and it is the most pernicious because of its hidden nature. It taxes the very purchasing power of money, and because the inflation rate in recent years has generally been low, its effects often take a while to manifest themselves. Now that inflation is beginning to rise, more and more rhetoric is being spun to hide the government's role in creating inflation. I applaud Chairman Frank for holding this hearing, as hearings such as this one investigating the link between the weak dollar and the high price of oil are more important now than ever.