2/7/13 Why interest rates held down don't help.

It has been thought that if the end of a period of lowered interest rates caused the cessation of expansion and boom then logic would argue in favor of reinstituting it to correct the recession. The reason that a low interest rate cannot return us to the boom of the expansion is that the expansion was a period of ongoing ever-worsening alignment of complementary productive processes, elevated measures of employment, and GDP notwithstanding.

Austrians have emphasized the folly of thinking of the economy as either enjoying more or less economic activity. Their more sophisticated model complies with common sense. We can consume capital on the one hand and invest in the wrong capital projects on the other. Each of these keeps up the GDP. But each of these subtracts from the ability to deliver supplies of usable goods and services in the future.

The correction not only must re-value these misappropriations, but it must liquidate them at a loss and terminate whole enterprises the most out of line with balanced production. The workforce must be relocated and retrained.

A community could begin a project to build a tunnel to access what requires a difficult journey over a mountain. It could employ plenty of engineers, train workers in demolition and excavation, and invest in heavy equipment. But if halfway through the mountain the community runs out of the means to support its workers, then when they go back to their original activities they have nothing to show for their work and are worse off from having depleted their resources. Yet, while engaged in the project they were experiencing a boom in employment and economic activity. Their economists said they were on the right track because they enjoyed a high level of aggregate demand, but they were misled as to their provisions because the authorities dispersed provisions at a rate that would deplete the granaries faster than they could be supplied. Artificial credit stimulation can have similar results.