From Austerity to Prosperity:
How Dealing with a Meltdown Can Lead to a Universal Basic Outcome

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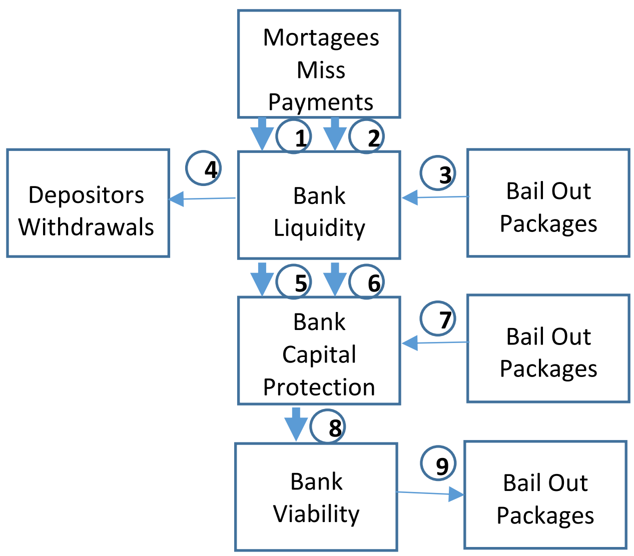
It is said that a crisis brings out the best in humanity as well as the worst. In the case of a financial meltdown, it has so far inspired the worst. Just as the best of economic times lavished rewards concentrated to a few who claim credit for the phenomenon, their downturn socializes the costs of excesses through austerity for the many in order to preserve the wealth of the few largely responsible for the profligacy.

Figure 1: How the Corporate Bailout Worked



1. Banks receive less cash to service depositors, who panic;
2. Banks, who also panic, call on loans & foreclose properties
3. Banks apply & receive bailouts
4. Banks are able to serve deposits
5. Banks' foreclosed assets deteriorate in value
6. Banks assets deteriorate with its capital
7. Banks apply & receive bailouts to preserve value of assets & shore up capital
8. Banks are able to recover &
9. Pay back bailout packages

When one examines how mainstream economics deals with the crisis in Figure 1, one cannot help but notice something amiss.

Because mortgagees have been remiss on mortgage payments on homes whose values with which they speculated had failed to produce the desired cash rewards, banks inherited a two-fold problem: illiquidity or lack of cash and an erosion of its capital base by foreclosed real estate sharply diminished and still declining in their market values.

Thus, the government rescues them with very mercifully generous bail out packages so that banks may serve deposit withdrawals and additional financial assistance so that banks' net worth may be protected from the "toxic assets" they foreclosed. These ways, the financial system may assure badly shaken clients that their money is safe in their banks and preserve confidence in the system in general.

However, while the financial institutions have received succor, government polies have dealt a cruel hand to the victims of the crisis – the evicted residents and the displaced workers from an economy rendered vulnerable to insecurities, on the altar of the markets. In order to save the banks, less money becomes available for welfare services and the competition for scarce resources further degrades the dignity and humanity of the growing number who need them in a recession. Nevertheless, the general consensus remained that austerity has been the bitter pill necessary to prevent a total breakdown of the financial system on which the economy of goods and services hinges.

John Maynard Keynes once exclaimed that the challenge economics faces is responding to the three pronged demand of economic efficiency, social justice and individual liberty. It appears mainstream economics has so far failed in its defined mission but is there any other way out from financial meltdowns that does not lead to the continuing prosperity of the many at the cost of increasing the misery of the many?

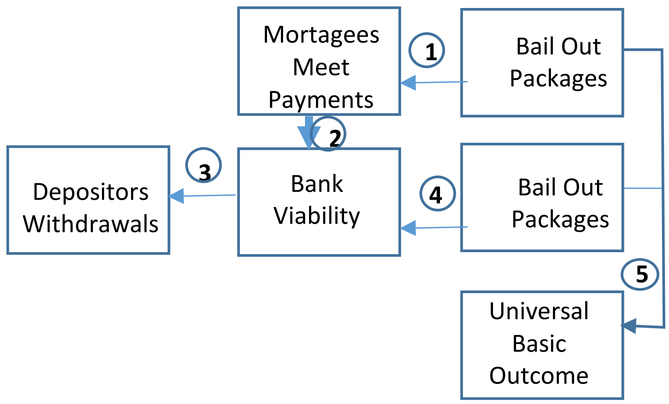
The key lies in understanding the fundamental purpose of money that has, so far, been forgotten – the facilitation of the production of goods and services necessary for societal function. In the hands of an individual it becomes one's ticket to participation and freedom in a civilization and a democracy. However, instead, its creation has relied on an entirely different mechanism, credit – largely by financial institutions – so that money has been reduced and treated as debt. To whom does is the debt owed, one may naively ask. The answer is simple: to those who created the money.

Unless there is a reasonable alternative, the history of repetition of crisis will continue, as well as the enslavement to a system that renders the many users of money in inevitable debt and a select few hoarders, the masters of destiny of the many.

Isn't there?

A proposed option requires more simplicity than complexity and fidelity to a principle of finance often taken for granted – the matching of sources and uses of funds,

Figure 2. A More Elegant and Just Approach

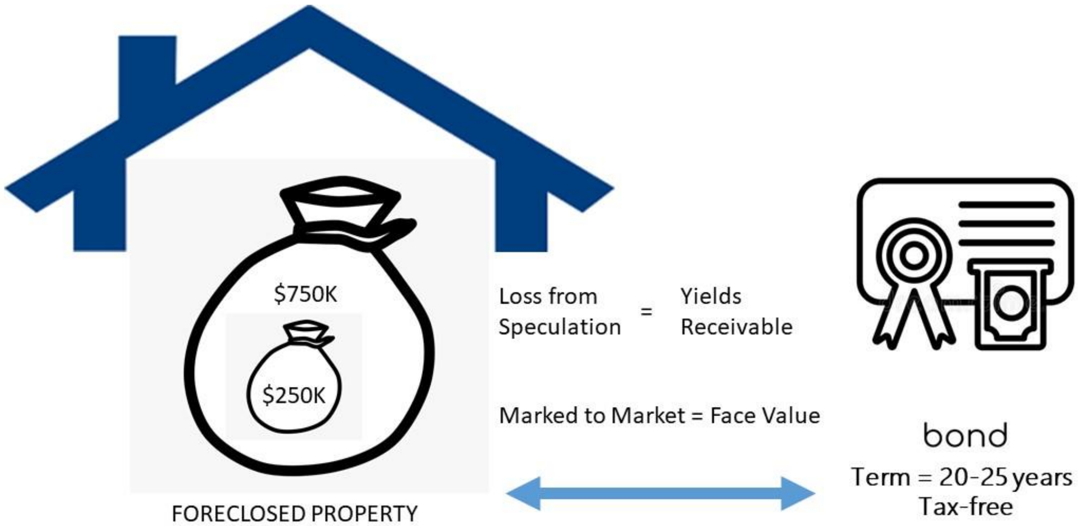


1. Bail Out Package help delinquent mortgagees/ residents under the same generous terms
2. Mortgagees repay the banks instead of missing payments.
3. Banks are able to serve depositors
4. Bail out for banks for capital buttressing that will entice banks to dispose of foreclosed assets
5. Proceeds for leverage-financing a Basic Income.

Figure 2 begins with government not bailing out the banks directly but through its imperiled customers, those who use their homes as dwellings and not investments. The bail out (1) must be as generous to the homeowners as they have been to the banks during the GFC that began in 2008. Thus, both the mortgagees (2) and banks (3) are able to meet their obligations.

What of the speculative investors whose properties were foreclosed? (4) The bail out for this case must be on the basis that will enable to protect the capital from booking any losses by stretching the monetary recovery of the property over a 20-25 year period. This, however, will compel the banks to sustain a time value of money/net present value reduction in value unless they are able to dispose the foreclosed homes as soon as possible and marked to market value at the time. That way, the banks can use the cash to engage in other lending and investment that will deliver a quicker recovery of the time value lost (see Figure 3)

Figure 3. Capital Buttressing Bail Out Bond



By receiving its principal and interest from the two bail out packages, the government is able to generate a cash flow for paying for a Universal Basic Income. (5)

The model has its basis on the following practices in history.

Monetary authorities have long exercised its power to provide liquidity through open market operations. By issuing bonds, banks can sell them for cash while the bearer continues to service the debt instrument.

The capital buttressing mechanism is based on debt-to-asset swaps that incentivized and facilitated the privatization of state properties in many countries. There is no fundamental reason why it cannot be applied in this situation to rescue homeowners who would have otherwise ended on the streets.

The Wörgl Experiment restored the fundamental role of government to provide the public goods of a citizenry of an Austrian city in 1932. Caught in a grip of a severe economic crisis, the local council issued a scrips backed by cash in its treasury &required a monthly stamp of 1% its face value for to continue its use and accepted it as legal tender of the local government as well as payment of taxes. It turned around the fortunes of the city in just one year.

By reassembling these components into a coherent logical and strategic policy as an alternative to austerity, a society distressed by a financial meltdown, it has redeemed the discipline of economics to its duty of achieving economic efficiency where gain does not result in any harm, realizing social justice is realized where each receive their due & carry out their rightful responsibilities and enhancing individual liberties by delivering the resources necessary for upholding the dignity of everyone – a universal basic outcome.