Stanley Fischer Spills the Beans

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Last week Stanley Fischer (Vice Chairman of the FRB) surprised if not shocked many, especially those with a contrarian view of current economic policy, by saying he thought that NIRP (Negative Interest Rate Policy) seemed to be working pretty well. About six central banks have made it part of their program. He wondered about its efficacy in Japan, didn't mention the ECB, and pointed a positive finger at smaller countries that use it – like Denmark and Sweden. The third largest economy and the European Union – nothing. The smaller countries – wonderful. To many it seemed crazy to say it was working when there were no indications of improvement in the most significant economies, yet he clearly stated just why he felt it was a good thing – because it boosted equities. The central banks' easy credit policies made it easy for investors, speculators and businesses to accumulate massive sums from equities and securities purchases. NIRP punishes them if they choose to park their take, thus – Don't stop, keep getting richer (reminiscent of Stalinism during its pro-kulak days). How on earth did an unseemly policy become such a critical part of the *recovery* process?

The economy suffered its first stroke in August of 2007. The Fed immediately jumped into the breach with its medicine bag full of tricks. It seemed to work so quickly and effectively that in 2008 Bernanke confidently declared the crisis over and full recovery on track. Victory was no sooner declared when the economy was laid low by such a massive stroke that its very existence was hanging by a thread. The traditional curative would be to stimulate the real economy, but that would take too much time although Obama did implement a "spade in the ground" pump priming public works program by speeding up the start of those projects that were ready to go. The government also tried an early "helicopter money" test flight by sending three to six hundred dollars to most Americans. When someone is at the point of dying they need Adrenalin, not a cup of coffee. The real economy in crisis is much like a person in desperate need of assistance – industry has to make commodities to sell, people have to earn money to buy. The unreal economy, the financial sector, sells things that can be made in a flash because they aren't real – pieces of paper purportedly secured by a real asset that may be so vitiated as to only exist in homeopathic amounts. The easy credit led to easy borrowing and massive purchases of paper assets, which of course increased their value and generated massive profits. Thus the Fed was able to strengthen the tail enough so that it could feebly wag the dog.

When a person has an accident or falls seriously ill the first thing done by those coming to their aid, whether they be just common folks or a physician, is to attempt to communicate with the subject – to get them talking. Being able to respond in that way is a vital sign of hope for survival and recovery. The Fed jolted the economy into showing signs of life. That must be judged an accomplishment, but that it has not managed to get the real economy up from its sick bed and onto its feet has so far been a total failure.

This week the markets have been approaching new all time highs on the basis of a

slew of negative economic reports. That makes it less likely there will be a rate hike (even though such a thing is hardly likely prior to the election). Surely it must be a stunning turn of events for anyone observing the economy for a significant length of time that market highs achieved when the real economy was really booming are being breached when the real economy has barely made it above comatose. It's no wonder that many are expecting a collapse rather sooner than later. But for those who consider the Fed as some sort of enemy they should understand that the best way to understand or even to defeat an enemy is to not underestimate its strength. The Fed has power, and power itself is the solution of last resort to be pulled from its bag of tricks.

The previous paragraph was written before Friday's close which registered a significant rout. The S&P500 had traded between 2157 and 2190 for 40 days -- the longest streak of stasis ever recorded. Today it lost 52 points. Most indexes were down about 2.5%. The causes are said to be Draghi saying yesterday that further accommodation is not being considered, and today Boston Fed President Eric Rosengarten said a case can be made for raising rates in order keep the economy from overheating. The economy has been sliding downward for the past two years but Rosengarten thinks we must throw some cold water on the over stimulated economy before the over stuffed full employment economy becomes too tight. Needless say, if we really had such great employment the economy wouldn't be so weak. If hiring is growing by leaps and bounds, why isn't that reflected in the total aggregate hours worked which has shown minuscule growth?

The real concern is credibility. After last December's rate increase six more were projected for 2016. Then it was reduced to four. So far there has been none which according to the Fed has nothing to do with what's happening to our wonderful economy. Today Rosengarten merely repeated what he said in China last month. Last week the San Francisco Fed chief said something similar. Could it be that today's shock drop signals a paradigm shift? The pros know that what Yellen, Fischer, Rosengarten and the rest have been saying is BS, but what if that becomes the consensus opinion? If raising the rate before the election shatters the crumbling feet of the current "recovery" it would most seriously affect the party of Wall Street, the Democrats. I'd love to see the Fed chance it, but still maintain December as most likely.

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