

# Bernanke's Fake Economic Recovery

By [Mike Whitney](#)

Global Research, December 12, 2009

[Counterpunch](#) 11 December 2009

Region: [USA](#)

Theme: [Global Economy](#)

Economic recovery” is a term that has no fixed meaning. But it’s worth mulling over to determine whether aggregate demand is strong enough to keep the economy from tipping back into recession. In normal times, the Fed slashes interest rates to increase the flow of capital to the markets and to consumers via lending at the banks. That’s the traditional method of “jump starting” the economy.

The Fed has never initiated policies which provide unlimited guarantees for underwater financial institutions. Nor has it ever poured more than a trillion dollars directly into the financial system by creating excess reserves at the banks and direct purchases of long-term assets. (Quantitative Easing) All of this is new. Naturally, this ocean of liquidity has produced price distortions which have been confused with real recovery. The S&P has soared more than 60 percent in the last 9 months, even though the yield on short-term Treasuries are at historic lows.

What does it mean? It means that investors are still fearfully shoving money into safe/conservative bonds, while speculators—who have access to the Fed’s zero-rate capital—are loading up on high-risk assets and pushing stocks into the stratosphere. This doesn’t tell us anything about organic growth in the economy or whether consumers—who make up 70 percent of GDP—will be able to sustain demand going forward. It’s mostly just hype.

On Thursday, Gallup released a new report titled “Upper-Income Spending Reverts to New Normal”. Here’s a clip:

“In a sign that the new normal in consumer spending continues unabated, upper-income Americans’ self-reported average daily spending in stores, restaurants, gas stations, and online fell 14 per cent in November, reverting to its relatively tight (\$107 to \$121) pre-October 2009 average monthly range. Middle- and lower-income consumer discretionary spending increased by 7 per cent last month but remained in its tight 2009 average monthly range of \$52 to \$61. Still, consumer spending by both income groups continues to trail year-ago levels by 20 per cent, even as those comparables have gotten easier to match — possibly dashing hopes that upscale retailers and big-ticket-item sales will do better this year.”

The bottom line: Self-reported spending is still down across all age groups, all regions and all genders. Surely, high unemployment and job insecurity feature large in the Gallup report, but reduced spending can also be attributed to the “wealth effect” and the shocking loss of household equity (\$12 trillion) since the beginning of the crisis. For households and consumers, the Bernanke’s experiment in monetary easing has largely been a failure.

Here's David Rosenberg with a bit of cold water:

"The credit collapse and the accompanying deflation and overcapacity are going to drive the economy and financial markets in 2010. We have said repeatedly that this recession is really a depression because the recessions of the post-WWII experience were merely small backward steps in an inventory cycle but in the context of expanding credit. Whereas now, we are in a prolonged period of credit contraction, especially as it relates to households and small businesses ...The defining characteristic of this asset deflation and credit contraction has been the implosion of the largest balance sheet in the world — the U.S. household sector. Even with the bear market rally in equities and the tenuous recovery in housing in 2009, the reality is that household net worth has contracted nearly 20 per cent over the past year-and-a-half, or an epic \$12 trillion of lost net worth, a degree of trauma we have never seen before. (David Rosenberg, "Breakfast With Dave", Gluskin Sheff)

Rosenberg correctly assumes that "frugality is the new fashion" and that baby boomers who are unprepared for retirement will continue to cut back on discretionary spending and increase savings in the years ahead. This will put more downward pressure on demand resulting in a "slow growth" sluggish economy. This week's Flow of Funds report from the Fed, reaffirms that, while the Fed has had some luck reflating "household net worth" by an estimated \$2.7 trillion; all of the gains are directly attributable to the uptick in the stock market which reflects the Fed's blatant market manipulation. Our question is whether positive growth (2.8 per cent GDP) is an accurate measure of "economic recovery" if it is produced by printing presses and parlor tricks?

The Fed's monetary intervention has created a bifurcated market. Stocks rise on an ocean of central bank liquidity while the real economy continues to languish in a small "d" depression. The disparity between financial markets and the underlying "productive" economy has never been greater. Nor has the "wealth gap", the gross inequality exacerbated by decades of "monetarist" supply side policies. Bernanke simply has no other choice but to try to inflate another gigantic bubble that will lift the economy from the doldrums on a speculative wave of zero-rate liquidity. The problem is, according to Bernanke himself, the strategy is not working. Here's an excerpt from Bernanke's speech this week to Economic Club of New York:

"The flow of credit remains constrained, economic activity weak, and unemployment much too high.... (We face) some important headwinds—in particular, constrained bank lending and a weak job market—likely will prevent the expansion from being as robust as we would hope.

"The ultimate purpose of financial stabilization, of course, was to restore the normal flow of credit, which had been severely disrupted....However, access to credit remains strained for borrowers who are particularly dependent on banks, such as households and small businesses. Bank lending has contracted sharply this year, and the Federal Reserve's Senior Loan Officers Opinion Survey shows that banks continue to tighten the terms on which they extend credit for most kinds of loans...The fraction of small businesses reporting difficulty in obtaining credit is near a record high, and many of these businesses expect credit conditions to tighten further.

"...securitization markets remain impaired... Unfortunately, reduced bank lending may well slow the recovery by damping consumer spending...and by restricting the ability of some firms to finance their operations." (Bernanke

speech, Reuters)

No one makes a better case against the Fed, than Bernanke himself. Reread his comments to appreciate the magnitude of the failure. As he admits, “The ultimate purpose of financial stabilization was to restore the normal flow of credit.” That says it all.

Now the economy is flatlining even while equities are still climbing. Consumer spending is flagging, credit lines are being cut, and unemployment has leveled off at 10 percent; still much too high for any meaningful rebound. Monetary stimulus has not been effective, because it doesn't get to the people who can generate the most activity. The Fed's increase in excess bank reserves keeps long-term interest rates low, (because the money is recycled into government debt) which keeps Wall Street flush with low interest capital. But it does nothing for households, consumers or workers who find it harder and harder to get a loan. The broken banks have created a credit bottleneck that is choking off the recovery. Without a direct lifeline to consumers (Jobs programs, state aid, extended unemployment benefits) the situation will only get worse.

The economy is sinking and the remedies are politically unpalatable. Obama's fiscal stimulus has reached its maximum impact. When the stimulus runs out, and the Fed ends its Quantitative Easing program (which is scheduled to wind-down by March 30, 2010) liquidity will drain from the system and the economy will tumble back into recession. action.

Financial system stability is largely an illusion created by explicit government guarantees on money markets, commercial paper, TBTF institutions, and toxic assets. (whose real value is still unknown) This is the scaffolding which holds the so-called “free market” upright. (In less PR-oriented societies; it's called “central planning”) Financial markets have become a ward of the state. It's not the integrity of US markets that attracts foreign investors, but the resources of the American taxpayer who has become the de facto guarantor of all Wall Street's speculative bets.

By usurping powers not granted under its charter, the Fed has resuscitated insolvent institutions and helped them continue the transfer of wealth from one class to another, in the traditional direction: up.

**Mike Whitney** lives in Washington state. He can be reached at [fergiewhitney@msn.com](mailto:fergiewhitney@msn.com)

The original source of this article is [Counterpunch](#)

Copyright © [Mike Whitney](#), [Counterpunch](#), 2009

---

[Comment on Global Research Articles on our Facebook page](#)

[Become a Member of Global Research](#)

Articles by: **[Mike Whitney](#)**

**Disclaimer:** The contents of this article are of sole responsibility of the author(s). The Centre for Research on Globalization will

not be responsible for any inaccurate or incorrect statement in this article. The Centre of Research on Globalization grants permission to cross-post Global Research articles on community internet sites as long the source and copyright are acknowledged together with a hyperlink to the original Global Research article. For publication of Global Research articles in print or other forms including commercial internet sites, contact: [publications@globalresearch.ca](mailto:publications@globalresearch.ca)

[www.globalresearch.ca](http://www.globalresearch.ca) contains copyrighted material the use of which has not always been specifically authorized by the copyright owner. We are making such material available to our readers under the provisions of "fair use" in an effort to advance a better understanding of political, economic and social issues. The material on this site is distributed without profit to those who have expressed a prior interest in receiving it for research and educational purposes. If you wish to use copyrighted material for purposes other than "fair use" you must request permission from the copyright owner.

For media inquiries: [publications@globalresearch.ca](mailto:publications@globalresearch.ca)