

The Fed's Historic Gamble: Pre-Bailing Out the Banking System

By [Dr. Jack Rasmus](#)

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[Jack Rasmus](#) 9 May 2020

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There's a historic experiment underway among US capitalists and policy makers. That experiment may or may not succeed. It's the Federal Reserve PRE-BAILOUT of not only the US financial system but the entire business economy as well.

The Fed has introduced at least \$9T in liquidity (money) injections into the system in the goal of heading off a massive wave of potential and forthcoming debt defaults, deflation, and bankruptcies via various measures: new QE, trillions of \$ to Repo markets, funneling trillions more via recent bailout funds for large, medium and small businesses through the private banks, ending financial regulations on the banks, liabilities for corporations, guaranteed loans, and so on. It's all about fattening bank and non-bank balance sheets to weather the loss of revenues required to keep paying interest and principal on the tens of trillions of excess business and household debt (latter held by investors). The continuing payments on that debt is necessary to prevent a massive historic wave of debt defaults that will eventually sink bank balance sheets, creating a credit crash and a further and deeper collapse of the real economy—i.e. a depression.

The Fed succeeded in 2008-09 in preventing a second banking crash by injecting \$5-\$6T into the banking system. The cost of that was to set off massive financial asset market speculation and bubbles, enriching investors as never before. The cost was also chronic low interest rates for 8 yrs that resulted in corporate binging on new business debt accumulation.

Now the consequences are coming home once again. The Fed's bailout of 2008-09 created a fragile system highly susceptible to another crash. The Fed's solution in 2008-09 has become the Fed's nightmare of a repeat, even greater, in 2020. So the Fed is throwing even more money at the system to prevent another crash. History will tell (soon) if it will be successful in staving off another financial crash, that will all but ensure a collapse into a bona fide depression.

The US economy is today unstably between a 'great recession 2.0' in the real economy and a bona fide great depression a la 1929-34. Whether the future trajectory is more like 2008-2017 or whether it slips into a 1929-34 scenario depends on whether the Fed's \$9T (and rising) money injections can prevent a financial crash in 2020-21, as defaults and bankruptcies rise and expand throughout the US economy in 2020-21.

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