The U.S Federal Reserve Isn't Fighting Inflation, It's Fueling It

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The media would like to believe the Fed is doing everything in its power to fight inflation, but it's not true.

Yes, the Fed raised rates by 50 basis points in May and, yes, the Fed is trying to sound as "hawkish" as possible. But these things are designed to dupe the public not to reduce inflation. Let me explain.

The current rate of inflation in the US is 8.6%, a 40-year high.

At its May meeting, **the Fed raised its target Fed Funds Rate to 1%**. Here's the scoop:

> "The Federal Reserve recently announced that it's raising interest rates by half a percentage point, bumping the federal funds rate to a target range of 0.75-1.00%." (The Spokesman-Review)

Got that? So the Fed's rate is still a measly 1%. That's what the media is trying to hide from you, and that's why you might have to read 9 or 10 articles before you find a journalist who provides you with the actual rate.

> Why are they hiding the rate?

Because the **rate is 7.6% below the rate of inflation, so it doesn't do a damn thing**. It's another public relations travesty dolled-up to look like serious monetary policy. But it's a joke, and you can see it's a joke.

Think of it like this: If I loaned you $100 at 1% interest– but inflation was running at 8%– I would lose 7 bucks per year, right?

Right. And that's what the Fed is doing. When interest rates are set below the rate of inflation, then the Fed loses money on every loan. In other words, the Fed is providing a subsidy to the banks for borrowing money. Have you ever heard of anything so ridiculous?

How would you like a deal like that? How would you like it if the Fed paid you interest on your credit card debt? You'd probably like that, right? But—if you were honest with yourself—you'd admit that it was a "gift", because that's what it is, a gift. **The big banks are getting another handout from Uncle Sugar.** That's the whole deal in a nutshell.

Meanwhile, you and I and the other 300 million serfs, continue to pay a hefty 18% to the banks that are being subsidized by the Federal Reserve. Sound fair?

So, **how much would the Fed have to hike rates if it really wanted to do its job?** Check out this clip from an article at the Chicago Booth Review:

> "The usual wisdom says that to reduce inflation, **the Fed must raise the nominal interest rate by more than the inflation rate**. In that way, the real interest rate rises, cooling the economy.
>
> At a minimum, then, according to the usual wisdom, **the interest rate should be above 8.5 percent.** Now. The Taylor rule says the interest rate should be 2 percent (the Fed's inflation target), plus 1.5 times how much inflation exceeds 2 percent, plus the long-term real rate. **That means an interest rate of around 12 percent.** Yet the Fed sits, and contemplates at most a percent or two by the end of the year." ("Why Hasn't the Fed Done More to Fight Inflation" Chicago Booth Review)

So if the Fed was serious about fighting inflation, they would have raised rates to roughly 12%. Instead, they have decided to use their allies in the media to pull the wool over everyone's eyes. That's what's going on. It's another big snow-job. Here's more from the Chicago Booth Review:

> "… the inflationary shock we just experienced, whatever its source, together with today's low interest rate, gives us a large negative real interest rate. **That negative rate is itself additional "stimulus": it raises output and lowers unemployment. Higher output and lower unemployment, however, raise inflation even more**, relative to the large past inflation. Higher inflation means an even lower real interest rate, and more inflation still, in a never-ending spiral—until the Fed gives in, raises interest rates to much above inflation, and contains the mess with a large recession." ("Why Hasn't the Fed Done More to Fight Inflation" Chicago Booth Review)

So, when the Fed's rate is lower than the rate of inflation, then inflation rises, the opposite of what we want to achieve.

Bottom line: Ultra-loose monetary policy fuels inflation and creates gigantic economy-destroying asset bubbles that wipe out trillions and ruin lives. Sound familiar?

It should. We've been through this drill many times before.

Here's something else you should know: The Fed has had its foot on the gas since Lehman Brothers blew up in 2008. That's when Fed Chair Ben Bernanke dropped rates to zero and put the printing press on "full throttle". From that point on, the Fed has been flooding the zone with low-price liquidity that has inflated the biggest asset-price bubble of all time.

Why does everyone need to know this?

Because inflationary pressures are forcing the Fed to raise rates, but even the slightest rate-hike can touch-off firesales that impact other shadow lenders that are equally overextended triggering a daisy-chain of defaults that can domino through the system causing another financial crisis. In other words, the asset-price bubble the Fed has created with its low-rate mania is so gargantuan and unstable, that any tightening of policy can ignite a system-wide meltdown. That's why Powell is so skittish about raising rates. It's because he doesn't know who the weak players are and where they are hiding. If one giant investment bank– that is drowning in red ink– suddenly goes belly-up after interest rates rise, then that bank is going to take down 20-or-so counterparties along with him. That's the problem with today's grossly-entangled market; the web of debt stretches across the entire system endangering even the stronger players. The last thing Powell wants to do is prick the bubble the Fed has been inflating for the last 14 years.

> Did you know the Fed has purchased $9 trillion in mostly US Treasuries and Mortgage-Backed Securities since 2008?

What that means is that stock and bond prices have risen not on their growth-potential or due to basic supply-demand dynamics, but because **the Fed has been actively distorting market prices to enrich its investor friends. This is how wealth is transferred to other members of the investor class, not in great bags filled with money, but through the underpricing of credit that is further amplified through dodgy debt instruments**. That's the name of the game.

Recently, the Fed has indicated that it wants to reduce its balance sheet to a more manageable size. The problem is that– just as stock prices rose when the Fed purchased USTs– so too, they will fall sharply when the Fed sells. And, that is precisely what has happened everytime the Fed has tried to shrink its balance sheet; stocks have fallen off a cliff. So, while the Fed has succeeded in pushing stock prices higher, (by purchasing $9 trillion in financial assets), it will not succeed in keeping stocks high while rolling off its prodigious asset-pile. In other words, the Fed will not be able to repeal the laws of physics.

Do you remember The stock market crash of 2020? Do you remember how it ended? Here's a little background from an article at The Balance:

> "The stock market crash of 2020 began on Monday, March 9, with history's most significant point plunge for the Dow Jones Industrial Average (DJIA) up to that date. Two more record-setting point drops followed it on March 12 and March 16.
>
> The stock market crash included the three worst point drops in U.S. history. The drop was caused by unbridled global fears about the spread of the coronavirus, oil price drops, and the possibility of a 2020 recession.
>
> Although the 2020 market crash was dramatic, it didn't last. The stock market experienced a surprising recovery, even as many areas of the U.S. economy continued to experience trouble…" ("How Does the 2020 Stock Market Crash Compare With Others?", The Balance)

So, stocks plunged thousands of points in response to a fast-spreading pandemic that was shuddering businesses and decimating economies around the world. The media dismissed the sell-off as a "panic" but that cretainly wasn't the case. Investors rationally concluded that economic activity was going to be gravely impacted by the virus and simply sold while they could. With no sign of a remedy or vaccine, there was no reason for optimism.

But why did the sell-off stop? That's what we want to know. What caused investors to rethink their approach and dive back into the market headfirst?

The Fed stopped the selloff. And the announcement that stopped the bleeding was probably the most extraordinary event in the Central Bank's long and checkered history. Because, in essence, what Fed chairman **Powell said was that he would put a bottom under stock and bond prices to prevent them from falling too far**. Think about that. Here we had the Fed– who poses as an impartial regulator of market activity– telling us to our faces that he plans to intervene whenever he thinks prices do not align with his expectations? In other words, **the Fed promised to prevent the market from functioning according to normal supply-demand dynamics. The free market had to be sacrificed in order to prevent the inevitable losses from the pandemic.** Naturally, investors loved hearing that the Fed "had their back" and stampeded back into the market money-in-hand.

And how did the Fed's announcement impact the market?

Let's look at the Dow Jones Industrial Average during that period.

On March 16, 2020, the Dow ended the session posting a close of 20,188.

Two years later on Jan 4, 2022, the index closed at 36,799.

In other words, **the Fed's promise to support stock prices triggered a 16 thousand point rise in the Dow in the middle of a pandemic.**

Would you call that manipulation?

I would.

At the same time, the Fed expanded the range of its purchases from risk-free" Treasuries and government-backed MBS, to any manner of dodgy corporate debt or ETF that needed propping up to support the broader market. This unprecedented and dramatic intervention dispelled whatever confidence any objective observer might have had in US markets in which the manipulation is so in-your-face, that one cannot avoid the foul stench of corruption that stretches from "sea to shining sea". The Fed has in fact become a price-fixing agency that has abandoned any restraint whatsoever. Former Fed governor Kevin Warsh anticipated this development years earlier and delivered a warning that was published in the Wall Street Journal. Here's what he said:

> "The Fed's increased presence in the market for long-term Treasury securities also poses nontrivial risks. **The Treasury market is special. It plays a unique role in the global financial system. It is a corollary to the dollar's role as the world's reserve currency. The prices assigned to Treasury securities–the risk-free rate–are the foundation from which the price of virtually every asset in the world is calculated. As the Fed's balance sheet expands, it becomes more of a price maker than a price taker in the Treasury market.** And if market participants come to doubt these prices — or their reliance on these prices proves fleeting — risk premiums across asset classes and geographies could move unexpectedly." ("The New Malaise", Kevin Warsh, Wall Street Journal)

Once again, the Fed's balance sheet is currently $9 trillion which means that stock and bond prices are probably inflated by two or three times that amount. Why do you think stocks continued to hit new highs in the middle of a pandemic while employment, production, manufacturing, services and growth were are on life-support?

Answer—The Fed. The Fed promised to support the markets, and investors responded by buying up everything that wasn't bolted to the floor. The plan worked like a charm.

Here's something you won't believe. The New York Fed– which has its own trading desk– released its annual report that includes one eye-popping paragraph "that took our breath away," says Wall Street on Parade editor Pam Martens. Here's more from Marten's article:

> "It reveals that **the New York Fed's trading operation … currently owns 38 percent of all outstanding U.S. Treasury Securities with 10 to 30 years remaining until maturity…**.
>
> There are multiple reasons that this detail takes our breath away. First of all, **the U.S. Treasury market is massive – at $22.6 trillion as of year-end 2021. That any one entity controls a big chunk of the market is deeply concerning.** (The same report showed that the New York Fed's trading desk owned 25 percent of all maturities of outstanding Treasury debt.)
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> The New York Fed's trading desk owning 38 percent of the 10-30 year Treasuries is also deeply alarming because it is that maturity range that has a dramatic impact on the interest rate of the 30-year fixed-rate residential mortgage, the most popular mortgage among first-time homebuyers historically. It means t **hat the New York Fed's gobbling up of these 10-year U.S. Treasury Notes and 30-year U.S. Treasury Bonds, to the tune of 38 percent of the market, has created artificial demand for these instruments that would not otherwise exist. That, in turn, means that mortgage rates have been artificially held lower – much lower – than they would otherwise have been….**" ("New York Fed Stuns with New Report: At Year End Its Trading Desk Owned 38 Percent of All 10-30 Year U.S. Treasuries", Wall Street on Parade)

So, interest rates are rigged? Is that what she's saying?

Sure looks like it.

If—as Marten says—"the New York Fed…currently owns 38 percent of all outstanding U.S. Treasury Securities with 10 to 30 years remaining until maturity", then the rates on those bonds are being suppressed by an entity that is supposed to be a neutral referee not a market participant. And the implications of that are huge because these rates effect everything from buying a house to purchasing a car. But what's more disturbing is how this activity relates to the Kevin Warsh comment:

> **"The Treasury market …plays a unique role in the global financial system…. The prices assigned to Treasury securities… are the foundation from which the price of virtually every asset in the world is calculated."**

What happens when Central Banks and investors around the globe realize that the world's premier risk-free asset—the 10-year UST—is built on a foundation of pure sand? Wouldn't that put the Treasury market and the US dollar in the crosshairs at the very same time?

It would.

Then why would the Fed engage in such risky activity?

We have to assume that they want to keep interest rates artificially low whatever the cost.

But, why?

The Fed is trying to preserve the zero-rate regime so it can continue its ultra-accommodative credit expansion that allows its wealthy constituents to rake in bigger profits than ever before. That appears to be the goal. But as inflation rises and the massive asset-price bubble grows more unstable, it's only a matter of time before the bubble bursts and all hell breaks loose. As economist Ludwig von Mises said:

> "There is no means of avoiding the final collapse of a boom brought about by credit expansion. The alternative is only whether the crisis should come sooner as the result of voluntary abandonment of further credit expansion, or later as a final and total catastrophe of the currency system involved."

Well said.

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