The Fed's Latest Welfare Payout to the Crooked Wall Street Banks

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On March 12, the Federal Reserve announced its biggest market intervention to date, a massive $1.5 trillion injection into the short-term funding markets ("repo") aimed at preventing grossly-inflated stock valuations from resetting at lower prices.

There should be no misunderstanding about the Fed's real intention or whether its meddling will work. When financial assets are purchased in bulk, prices rise, that is the immutable law of the market. Stocks and bonds do not differentiate between day-traders and Central Bankers. What matters is the amount of money and what securities are purchased. What we know from 3 iterations of Quantitative Easing (QE) is that, when the Fed buys financial assets (USTs or MBS) stock prices climb higher. Friday's trading will undoubtedly produce the same result.

We also know that the Fed's circuitous blabbering never explains their real objectives. The Fed is not trying to ease "ominous trading conditions" or "counter signs of market dysfunction " or "address highly unusual disruptions in Treasury financing markets associated with the coronavirus outbreak." That's all diversionary mumbo-jumbo. The Fed's real goal is to prevent the markets from working the way they are supposed to work, to prevent basic price discovery, because price discovery will dramatically reduce valuations leaving banks and other financial institutions deep underwater.

Price discovery is the means through which an asset's price is set by matching buyers and sellers according to a price that both sides find acceptable. It is largely driven by supply and demand. It is a useful mechanism to gauge whether an asset is currently overbought or oversold. **Price discovery is the central function of a marketplace and is the process of finding out the price of a given asset or commodity**. (Investopedia)

When an outside actor, like the Fed, intervenes in the market and creates fake demand for financial assets that investors have shunned, it is destroying the "central function" of the free market. **It is asserting power over the market to set prices and, by doing so, assumes the role of Central Planner**. That is what the Fed is doing by stopping the market from clearing. It is "price setting". It is pushing stock prices higher than their true market value by loading up on mainly US Treasuries which dramatically distort rates while inflating the price of government bonds. We can only guess what the yield on the benchmark 10-year Treasury would be if the Fed had not purchased $2 trillion of them to save the insolvent banks from bankruptcy in 2008? And, in case there is any doubt about that matter, here is a straightforward admission by former-Fed chairman Ben Bernanke during the post-Lehman congressional hearings:

> "As a scholar of the Great Depression, I honestly believe that September and

October of 2008 was the worst financial crisis in global history, including the Great Depression. If you look at the firms that came under pressure in that period. . . only one . . . was not at serious risk of failure. So **out of maybe the 13 of the most important financial institutions in the United States, 12 were at risk of failure within a period of a week or two.**"

Think about that. They were all broke, all the biggest banks on Wall Street were completely busted. But they were brought back to life by Lazarus Bernanke's emergency rates, giveaway loan programs and lavish liquidity injections. At the same time, the American people were deliberately misled about the process that was underway, just as they are being misled about today's intervention. What is actually taking place is another multi-trillion dollar bailout that is going to seriously undermine confidence in US Treasuries as a reliable barometer of financial asset value. Here's an excerpt from an article by Bernanke's right-hand man during the last crisis, Kevin Warsh, who underscores the risks the Fed is taking by intervening in the markets:

> "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 shock that hit the financial markets in 2008 upon the imminent failures of Fannie Mae and Freddie Mac gives some indication of the harm that can be done when assets perceived to be relatively riskless turn out not to be." ("The New Malaise", Kevin Warsh, Wall Street Journal.)

Here's more from Warsh on the unintended consequences of the Fed's interventions that create powerful incentives for risky behavior that undermine investment, inflate asset values, and damage the real economy.

> "Extremely accommodative monetary policy, including the purchase of about $3 trillion in Treasurys and mortgage-backed securities during three rounds of "quantitative easing" (QE), pushed down long-term yields and boosted the value of risk-assets. Higher stock prices were supposed to drive business confidence and higher capital expenditures, which were supposed to result in higher wages and strong consumption. Would it were so.
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> Business investment in the real economy is weak … In 2014, S&P 500 companies spent considerably more of their operating cash flow on financially engineered buybacks than real capital expenditures for the first time since 2007 … **We believe that QE has redirected capital from the real domestic economy to financial assets at home and abroad.** In this environment, it is hard to criticize companies that choose "shareholder friendly" share buybacks over investment in a new factory. But **public policy shouldn't bias investments to paper assets over investments in the real economy.**" (The Fed Has Hurt Business Investment, Michael Spence And Kevin Warsh, Wall Street Journal)

The Fed is destroying the system it is entrusted to safeguard. It's acting as a stooge for the banks instead of an impartial referee whose job is to oversee and regulate the financial system so capital is efficiently deployed to productive investments that benefit the American people. Does anyone think the Fed is acting within its mandate by pumping the system with liquidity so crooked banks can cream bigger profits off their casino operations?

No one, and yet it continues.

There's no way to know the true value of the benchmark 10-year Treasury (which is the "the foundation from which the price of virtually every asset in the world is calculated") because the Fed's relentless mucking-around has distorted prices beyond recognition. Imagine for a minute if the central banks had not purchased trillions of dollars in sovereign bonds during the financial crisis? Imagine where rates would be today?

Rates would not only be positive, they'd also be "normalized" which was the Fed's stated goal when it tried to reduce its $4 trillion dollar balance sheet last year but then suddenly slammed on the brakes when stocks fell and the crybaby banks began howling. So now the Fed has abandoned normalization altogether while its balance sheet remains permanently submerged in red ink.

But how is capitalism supposed to work if rates are stuck at zero or go negative? Interest rates are the jet-fuel that energize capitalism. The "marginal efficiency of capital" refers to the returns that are expected from a capital asset during the time it is held by an investor. If those expected returns are reduced to zero, then the incentive to invest vanishes, the system is stood on its head, and capitalism no longer works. What is left is not productive investment, innovation or socially-beneficial development. What's left is rampant speculation, asset prices that are completely divorced from reality, and the endless build-up of paper claims on imaginary wealth. Isn't this an apt description of today's Fed-generated market?

And now the Fed is at it again, tilting the system so the bulk of the nation's wealth continues to flow upwards. Here are some of the shocking details about this latest bank bailout:

> "**The New York Fed said it will offer its primary dealers another $500 billion in a 3-month loan and another $500 billion in a one-month loan….Both 3-month and 1-month loans will be offered weekly "for the remainder of the monthly schedule." That means $1 trillion a week will be available at below-market interest rate**s **until the middle of April.**
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> That will be on top of the $175 billion the Fed is offering daily in one-day loans and the $45 billion it is offering each Tuesday and Thursday in 14-day loans. This is a dramatic expansion of the Fed's balance sheet to support Wall Street — all without one vote, or debate, or hearing occurring in Congress." ("Federal Reserve Announces Unprecedented $1.5 Trillion in Loans to Wall Street Today and Tomorrow" Wall Street on Parade)

In one fell swoop, the Fed has become the market, the whole market and nothing but the market. **This new bailout is not $1.5 trillion, it is more than $1 trillion per week for the remainder of the monthly schedule.** This explains why "risk-free" US Treasuries sharply rose during yesterday's selloff, it's because the banks moved into cash so they would have the resources they needed to lend to all the desperate businesses (Cruise lines, airlines etc) that have been whacked by the coronavirus.

Wall Street Bankers Visit Trump on Wednesday

Some readers may have noticed that, on Wednesday, the CEOs from Wall Street's biggest banks visited Trump in the White House to tell the president how well capitalized they were. Why would they do that? Why did they need to visit Trump to tell him how great they were doing?

It's because they knew that, in less than 24 hours, the Fed was going to announce that it was dumping trillions of dollars in to the repo market and they'd be back on Easy Street. That's why.

It was all a set-up. The fleecing of the American people is just one big freaking set up after the other. It's infuriating.

Are the banks in trouble again? Is that why we're being subjected to this latest sheering?

Of course they're in trouble. Do you think you can slash $10 trillion off stock valuations and shove oil off a cliff and not have the banks in trouble?? The banks are heavily invested in oil, just as they are in derivatives trades, loans to shaky hedge funds, and stocks that are currently in freefall. Which is why the Fed has wheeled in the heavy artillery.. Check out this excerpt from an article at The Wall Street Journal:

> "**The deepening Wall Street rout is adding to pressure on U.S. banks, as the retreat of investors from risky assets saddles lenders with securities they are struggling to sell at desired prices.** The crunch has been evident in the share prices of the largest U.S. financial firms, which have fallen 30% or more in many cases over the past month. Citigroup Inc. dropped 8.6% on Wednesday, extending its decline to 36%, nearly doubling the drop in the S&P 500…
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> When markets come under duress as they have over the past couple of weeks, **asset prices are pushed to levels where you begin to see margin calls and other internal activity that is not always visible on the surface,**" said Daniel Deming, a managing director at Chicago-based KKM Financial.
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> The most surprising development for traders Wednesday: the sharp decline in the price of U.S. Treasury securities, which until this week had consistently risen significantly on days when U.S. stocks were falling. **The price declines sent yields higher after dropping to record lows and were fueled in part by banks selling U.S. government securities to reduce inventories and raise cash**. Rates are low enough that Wednesday's action itself didn't hurt banks, but the unusual nature of the move raised eyebrows."
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> …**People familiar with some of the largest securities-dealing banks said many firms bought corporate bonds as prices fell last week, but those purchases resulted in some banks having balance sheets that executives deemed too large.** With prices barely having recovered in many markets, some banks chose to sell Treasuries instead, in part reflecting their significant appreciation in recent weeks." ("Wall Street Plunge Stresses Banks, Treasury Markets", Wall Street Journal)

Let's recap: Why are the banks selling Treasuries?

Because they need the cash.

Why do they need the cash?

Because–according to the author– the banks are stuck with a bunch of stocks “they are struggling to sell at desired prices.”

But that just means stock prices have dropped, it doesn’t explain why the banks need cash?

True, the only reason they would need cash is if they borrowed the money to buy the stocks in the first place, which is what the author suggests when he refers to “margin calls and other internal activity that is not always visible on the surface.” In other words, the banks need cash because their portfolio is underwater and they are leveraged up to their eyeballs.

According to the article: “People familiar with some of the largest securities-dealing banks said many firms bought corporate bonds as prices fell last week, but those purchases resulted in some banks having balance sheets that executives deemed too large.”

Corporate bonds?!? The corporate bond market froze last week, no activity at all, a complete graveyard. If the banks were dabbling in that garbage, then they must’ve gotten burned bigtime which would explain why they want another bailout from Uncle Sugar.

It’s worth noting that none of this has anything to do with the Fed. The banks were playing the stock market and lost their shirts. Who cares? Break ’em up, auction off the good assets, ring-fence the bad, install new management, and start over. That’s how the system is supposed to work. You roll the dice, and if you come up snake-eyes, you go home. End of story. That’s what we should have done in 2008 instead of keeping these parasites on life support so they could take us all over the cliff for a second time in 10 years. It’s ridiculous!

Keep in mind, **the Trump administration has only allocated a lousy $8 billion** to fund its response to coronavirus. So the American people –all 330 million of them– will get a whopping $8 billion **while the crooked Wall Street banks get regular multi-trillion dollar infusions** that allow them to swap their crappy, dog-eared securities for cold-hard cash. The banks will then roll over these 3-month loans indefinitely turning their short-term debts into perennial welfare payouts. Does that sound fair to you?

This is why people despise the Federal Reserve. They don’t see the Fed as an impartial arbiter fulfilling its mandate of price stability and full employment but an evil puppetmaster that wants to rule the world. That, of course, is a gross exaggeration. In truth, the Fed is no different than the FAA, a thoroughly corrupt and unreformable “rubber stamp” agency that is entirely controlled by the corporations it’s supposed to regulate. This latest multi-trillion dollar travesty just proves what we’ve known for a long time, that the Fed always operates in the exclusive interests of its reprobate constituents, the crooked Wall Street banks.

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