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Quantitative Easing (QE2). Debt Created Out of Thin Air: The Crisis in Banking Has Worsened

By Bob Chapman
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In a futile attempt to keep the economic and financial system afloat, QE2 is underway. It began in early June as banks changed the rules for awarding loans. Their efforts over the past few months have only met with moderate success. Banks had cut back lending by some 25% over the past 16 months mainly to small and medium-sized companies. In the process the economy slowed down markedly and unemployment shot up to levels not seen since the 1930s. These first attempts to restart a sliding economy have so far not met with success. It was not long after that the real decision makers at the Fed that QE2 was going to be needed. We saw the marshalling of financial and economic forces and the tell tale sign of a stock market moving upward for unexplained reasons. That tipped us to QE2.

This interventionism effective for the short term will again on the long-term drive out real investment. The kind that creates jobs and profits, that does not directly reflect the financial system. The policies being put in place by the Fed are the antithesis of a free market not only because they interfere with a natural process, but also because they are borne of debt created out of thin air – debt that will have to be repaid by the taxpayer. Much of the funding being created by the Fed will and has been used to fund the debts of the Treasury and government agencies, which produce nothing but more debt. In this process they also crowd out other borrowers of money, which ultimately leads to higher interest rates and offsets banks' ability to lend. We are currently seeing a perceived flight to quality into US Treasuries from the market and from corporations. The perception that government's cannot go broke, particularly the US government, is pure fantasy. The profligacy of debt has to be paid by citizens. That takes purchasing power out of the hands of the consumer, which in turn pushes the economy deeper into depression.

Just to show you how out of touch with reality the administration and Congress is the Democrats have introduced two new bills, The Debt Free America Act, HR 4646, which would put a 1% sales tax on credit card and securities transactions in the US and the Automatic IRA Act of 2010, which would decree a mandatory payroll tax on all workers of 3%, to be used to purchase government retirement bonds. That tax is expected to rise to 15% within three years.

This Automatic IRA Act is a foot in the door for financing government deficits. It will be followed by legislation that will force present IRA, 401k and all retirement plans to purchase retirement treasury bonds, which will be called, Guaranteed Government Annuities. This has been buried within the Automatic IRA legislation.

The labor department has an agenda coming up next week on September 14th and 15th, which would decide on whether this so-called lifetime annuity should be required for private retirement accounts of all kinds.

The former transaction tax, we are told by our people in Washington, will rise to 3% within three years. This is the worst possible thing that can happen to the economy. Congress is almost totally purchased, so we see little resistance to passage, prior to the end of the year. The elitists are about to bury the economy. The President has been in office 19 months and Treasury has increased debt by $2.74 trillion, or by $144 billion a month. Freddie Mac had a quarterly loss of $6 billion and wants $1.8 billion more in taxpayer aid. You are seeing the nationalization of housing, as we saw in the Soviet Union, as we predicted seven years ago.

Auto=IRA bill formally proposed in Senate

http://www.investmentnews.com/article/20100809/FREE/100809903?template=printart

Debt Free America Act

http://www.snopes.com/politics/taxes/debtfree.asp

The Fed tells us they will not create new money and credit to fund QE2. We do not believe that for one second. They also stated they will use the proceeds from maturing mortgages they bought from GSEs, but they will sell MBS and CDOs to fund the operation. As of now we do not really know what those numbers are, but we do know that the banks that sold them to the Fed are gearing up to buy them back. We can promise you the Fed has every intention of using any avenue to fund QE if necessary. Either that or they pull the plug and go into a deflationary depression. Those within the markets are confused and disappointed because they do not know which way the Fed is headed. That is why markets are so volatile along with the brazen in your face market manipulation by the "Plunge Protection Team." That is why so many investors have headed for the exist.

It has been two years since the Fed took on mountains of GSE paper along with the MBS and CDOs. Had they not done that it all would have collapsed taking the banks, Wall Street, insurance companies and many others into bankruptcy. The taxpayers were left to pay for the losses and at least the holders were saved for now. As this paper matures it will again be used to fund the GSE's and the Treasury, and the MBS and CDOs will be sold to raise funds for QE. That won't be nearly enough and it's our guess that just over the next year $1.3 trillion made up out of thin air will have to be added and that is where the core of higher inflation will come from. These are the plans in the works. Obviously many individual investors have gotten the message. Money has been hemorrhaging out of the market for months and a survey two weeks ago revealed the highest bearish results ever seen. Part of the reason for QE2 is to draw these funds back into the market, so that the Fed doesn't have to spend billions every day propping up the market. It should also be noted that the sale of US Treasuries by foreigners has resulted in domestic invested now holding more Treasuries than foreigners. The flip side is investors see higher inflation and a continuing recession/depression and they see no recovery. They have little confidence in the future of the dollar, yet flock to Treasuries, because they do not as yet understand that gold is now the world's premier currency. Many will finally wake up to falsehood that the dollar is sound and guaranteed by the government. By that time gold will be worth considerably more than it is today. That is why all fiat currencies have been falling for seven years vs. gold. Treasuries are perceived to be safe. Wait until the public finds out they are not.

One thing the 6-month old European currency and debt crisis has showed us is that many nations and banks are not credit worthy and austerity and higher taxes, plus the sell off of national assets has inhabitants outraged and several countries led by Greece may be on the edge of a coup or revolution. As readers know we received reliable Intel this week that we may well be looking at such an outcome by the end of the month in Greece.

The sand is flowing through the hourglass for the world financial structure. There probably isn't a nation in the world worth an AAA rating. We ask what happens when interest rates rise, which must happen eventually? Won't higher rates be destabilizing? Of course they will. When will they come? No one knows, but they will come. A guess might be when investors start to realize that the dollar isn't worth the paper it is written on. We can just see Messrs. Bernanke and Geithner again threatening the populous with depression if they do not continue to hold Treasuries and GSEs. That will fall hollow on the ears of investors in a national and world economy that has already been in depression for 1-1/2 years. History later will verify that. By the end of 2012 the monetary and fiscal experts will almost all be found to be wrong and Keynesianism will be found to be just a device to implement corporatist fascist tyranny.

The crisis in banking now three years old has not abated. In fact it has worsened, as Ben Bernanke admits to Congress that he lied to them in previous testimony regarding the failure of Lehman Bros. Larry Summers is headed for China indicating all is not well regarding the US-Chinese relationship. Summers may be very bright, but he is like a bull in a China shop, full of arrogance and dictatorial attitude. We do not see that working out well. China has foreign reserves of $2.45 trillion, of which 65% is in dollar denominated assets, or $1.6 trillion in dollar denominated assets. Of that some $800 billion is said to be in US Treasuries. That figure has fallen some $100 billion over the past year. China has yet to meaningfully make an effort to increase the value of their currency after years of prompting by the US. China keeps their currency cheap by printing currency and buying dollars, which either go into US Treasuries or is sold for other currencies, or used to buy goods or services.

Banks Tier 1 capital ratios are eroding. The middle sized and small banks are fearful their real estate, business and individual loans are going to get them shut down, or absorbed into bigger banks whose standing is no better. This is part of a plan from behind the scenes to nationalize American banking. The FDIC has dictated that these banks cannot lend to businesses that have lost money for two consecutive years. That leaves very few companies to lend too, and what banks are finding is that those who qualify do not want loans. These companies supply 70% of new job creation, so it's not surprising that unemployment has not improved appreciably. Banks with perfectly good collateral, for in excess of needed loan backing, are being refused as well. The question arises are banks really serious about lending? Some won't even take fully paid for plant and equipment and residences as collateral. As this transpires more and more money is leaving banks and going into treasuries, other bonds and gold and silver. The too big to fail money center, legacy banks are being protected as too big to fail. This method of operation is causing bank failures and mergers and causing the eradication of small and medium sized businesses, which in turn is destroying job creation. The Fed, Washington and Wall Street are well aware of this. Banks in an attempt to save themselves are investing in Treasuries and derivatives, plus share and bond trading with mixed results. They have simply bypassed Main Street and their customer base.

As this tragedy plays out gold and silver continue to move higher as the flight to quality becomes serious. That is in spite of the fact that buyers know full well it has been and is US Treasury and central bank policy to deliberately suppress gold and silver prices. It is only a matter of time before moves in the precious metals are $50 to $100 a day, as years of gold and silver suppression come unraveled.

Again, the Fed either monetizes via QE2 or the financial system collapses. There is no real recovery so the only alterative is to create money and credit. The liquidity trap the banks are in certainly neutralizes their ability to assist in keeping the economy above water. There is no safety in US Treasuries, as investors flock to them and their ridiculous yields. At the same time central banks worldwide are buying US Treasuries to bolster the US financial system. They do not have much choice, because they are already buried in US dollar denominated paper. Although their dollar forex position has fallen from 64.5% in US dollar investments, 18 months ago to 69.5% recently. All the players know the US either monetizes or dies. That was reflected in the stock market in July when the Dow moved up almost 10%, only to be thrown back by reality. It was in early July we predicted QE2 was on the way. That wasn't difficult when we saw all the big time players going long. It was the same M.O. we saw starting last October when the biggies started going long dollars and short the euro. They knew something we didn't know, because in both instances they created the plan for the fall in the euro and well as this summer stock rally. Nothing has changed, even under dire circumstances. They believe they are bullet proof and can do anything they want. There will come a time when their reign will end and the outcome will be devastating.