

ARMSTRONG ECONOMICSTM

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WHY THE FEDERAL RESERVE IS ESSENTIAL

There is much hatred and misconception about the Federal Reserve that centers around the theme that it is owned by the bankers. Much of this real confusion stems from the fact that the Fed was transformed by politicians who didn't understand its purpose and once more they are altering its role making it into a "too big to fail regulator" stripping all real power to protect the banking system.

In 1913, the Fed was only to do what JP Morgan did in 1907 - prevent bank failures. Each of the 12 branches set their own interest rates to attract and deflect cash on a regional basis. The NY Fed saw itself equal to the central banks of Europe and lowered US rates trying to deflect capital back to Europe in 1925 that failed and merely confirmed there was a crisis. Faced with massive capital inflows that helped drive the US stocks dramatically higher, the Fed raised interest rates to no avail. Everything backfired and by 1931, there was a global collapse in the gold standard. By 1935, the Fed design was altered usurping all power of 12 branches into Washington. Regional management vanished. Now, the head of the NY Fed will be political and the Fed will only monitor the big banks.

What began as an industry solution to prevent bank runs, has been taken by Congress and distorted into something it was not intended to do, and will only set the stage for a massive banking crisis ahead. In part, it was the confiscation of gold by FDR who then had the Fed issue Federal Reserve notes replacing the old large notes. The Fed held gold, not private banks, but then there was the birth of the idea that inflation was defined as too much money chasing too few goods. Merge that with deficit spending, and the perception became Congress just spent, and the Fed was supposed to negate that spending. Congress was free to do as it liked & the Fed was now the manager.

I have been a supporter of returning the Fed to its role as JP Morgan defined himself. The Fed should have no inflation "target" nor be in charge of interest rates or anything of the sort. The repeal of Glass-Steagall was the worst thing Rubin sponsored and it set the stage for the collapse we have gone through. The SEC and CFTC are a joke. Investment banks were their domain not the Fed's. They are responsible & instead they get more power and the Fed is carved up. This is ass-backwards. SEC & CFTC must be merged and the Fed restored over Commercial Banking. Drop the title "Investment Bank" for it is a glorified Broker-Dealer. The term confuses Congress & the people for they are at best a Investment Broker-Dealer who does underwriting, which is why they were regulated by the SEC - not the Fed.

Like NASDAQ, the Fed was a private banking collective. It added money by buying commercial paper. When WWI came, politicians wanted the Fed to support the Government by buying its paper. Overtime, the Fed was usurped into supporting gov't debt at par until 1948 by law.

The Fed was only suppose to protect us from banking failures. The SEC is incapable of comprehending the economy no less the evolution of financial Alchemists. It blew it in 1998 & the Fed had to stem in to bailout a hedge fund LTCM because its creditors were banks. The Failure of Bear & Lehman were SEC once again - NOT Fed. What is taking place, the SEC screws up the world and points the finger at the Fed who is beaten by Congress and more power is given to the SEC.

We are now in the backseat of a runaway cab driven by a monkey whose hat says "Fear Not - I'm the SEC." If there ever was a prelude to disaster, we are in it. Congress has simply spent whatever it likes & blames the Fed for all the problems. Just put the Fed back to 1913, the Treasury to controlling money supply & interest rates to the free market, Congress to accept responsibility for its spending, & restore Glass-Steagall. Is it that difficult?

America's #1 Political Prisoner - Martin A. Armstrong