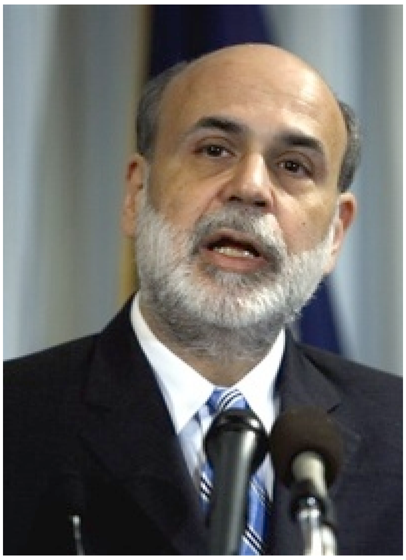
Money for Nothing, and Blue Chips for Free



In the long run — say, a week or two at the most — the Fed's latest action will likely have the same effect as its other recent moves, moves intended to soften the effects of an economic calamity the Fed itself has been largely responsible for creating. In point of fact, the federal funds rate — the average interest rate that Fed member banks charge one another to make short-term (usually overnight) loans of reserves kept at the Fed — is not "set" by the Fed at all.

Instead, the Fed encourages interest rates within the target range by the purchase or sale of government securities (so-called "open market operations"). If the Fed wishes to depress interest rates, it will buy more securities, thereby injecting more money into the banking system and encouraging lower interest rates. That, at least, is how the system works in theory.

But as the New York Fed's own website admits, "the results of the Fed's monetary policy actions cannot be predicted with precision. The Federal Reserve's influence over short-term interest rates can create conditions conducive to economic growth, but ever-changing market and political conditions, here and abroad, also heavily influence the millions of economic and financial decisions of households and businesses."

And this is but one of the many problems with the inflationary fiat money system overseen by the Federal Reserve and other central banks abroad: it assumes that central bankers are capable of knowing how much or how little money is needed in circulation. In reality, of course, even an individual as brilliant as Ben Bernanke undoubtedly is cannot possibly know what an optimum money supply should be at any given moment, or even over time.

Modern central banking is just the grand fallacy of socialism — that enlightened planners can somehow make better economic decisions than millions of producers and consumers can — applied to the money markets. And just as central planning has failed miserably in every other economic sector where it has been tried, so also it has failed and will continue to fail in money and finance.

It has frequently been the case that, try as it might, the Federal Reserve has been unable to increase the money supply to a desired level because banks and consumers are unwilling to lend and borrow. Such was the case in the early years of the Great Depression, and such appears to be the case now. Even if credit is offered on terms far below any rational calculation of interest, people and institutions still will not borrow if they see no reason to take on debt. After all, even at zero percent interest, debt must still be repaid, and banks already teetering on the brink of insolvency may be more interested in merely surviving than in taking on more debt, even at absurdly low terms of credit.

On the other hand, a very real likelihood exists that, at some point, the Fed's irrational monetary largesse could trigger a binge of credit and money creation that will ignite an inflationary firestorm. Such are the hazards of entrusting the money supply to the "experts."

(*AP Photo*)