Is the Boom Over?

Friday was another day of gloom and doom for the global markets, with the Dow Jones down nearly 400 points, or about 2.4 percent, the NASDAQ falling 126 points, or more than 2.7 percent, and the S&P 500 down 41 points, or almost 2.2 percent. The markets have been on a calamitous, almost uninterrupted slide since the beginning of the new year, historically unprecedented in severity and persistence.

Meanwhile, the price of petroleum — one of the factors supposedly driving the ongoing market correction — has plummeted to levels not seen in more than a decade, declining to $29.42 a barrel by day's end. Analysts predict that crude oil — only two years ago trading at around $100.00 a barrel — may reach $20.00 or even $10.00 a barrel before hitting bottom.

The current catalyst for market angst is said to be the implosion of the Chinese market bubble. Certainly the long-anticipated collapse of China's irrationally exuberant economic growth is a valid contributor to the ongoing turmoil, as is the seemingly irremediable glut of crude oil that has caused prices to drop. But the underlying cause, as with all of the havoc wrought by the vicissitudes of the boom-bust business cycle, is the systemic distortion created by the modern banking system and its reliance on fiat money issued by central banks with the power to manipulate the currency supply.

The roots of the current market instability and decline are traceable to the onset of the Great Recession, when central banks, including the Federal Reserve, began pumping new money into the economy at a furious rate, in a vain, Keynesian-motivated effort to offset the pain of financial and economic collapse. The Federal Reserve in particular gave itself a whole range of new financial tools to create money, above and beyond the four standard methods used for decades (lowering of interest rates, buying and selling foreign currency, open market operations, and lowering reserve requirements for banks). All of the arcane methods used by the Fed to create new money amount to issuing new debt, or creating the demand for more debt. All these methods are inflationary, and all of them favor the wealthy and well-connected few that have primary access to the new debt and new money thus created. Thus the lowering of interest rates encourages more borrowing, for example, and the selling of government debt (treasury bonds, for example) to banks encourages an expansion in the money supply.

But such new money creation favors the megabanks and investment banks with the legal authority to deal directly with the Fed. These organizations flourish under the Fed's monetary largesse, using the new money to purchase assets — stocks, bonds, and real estate, for example. This is the reason for the rapid growth of the stock market following the crash in '08. Even as the American economy shed millions of jobs, businesses went belly-up, and homeowners walked away in droves from mortgages they could no longer afford, the stock market rose to new heights (not, it must be underscored, with anything like the vigor of the great bull market of the '80s and '90s; in a secular or long-term context, the market is still very much a bear market). This artificial bull market was driven almost entirely by inflationary policies; central banks created new money at a furious pace, driving asset prices sky-high.

The by-product of such policies is the systematic impoverishment of the vast majority who do not own the lion's share of the assets; it is they who have seen a steady deterioration of their standard of living over the last eight years, putting the lie to all the breezy assertions in the financial media and in Washington about the economic recovery. Real wages continue to decline, real estate values have been little more than stagnant, and the job market remains anemic. Ordinary Americans continue to tighten their belts while the ultra-rich throw themselves a party. It is true that the rich are getting richer and the poor not only poorer but greater in number. But the ultimate cause may be traced to the policies of the wealthy, well-connected few who run the financial system dependent on central banks and fiat money.

But the party cannot last forever. In the 1970s, the persistent economic malaise eventually produced "stagflation," whereby prices rose as in a normal inflationary cycle, but not even the rich were able to reap the economic benefits. This state of affairs persisted until the long and deep recession that finally ended in late 1982. That last slide, which lasted 16 months (and came on the heels of an earlier six-month recession in 1980), finally cleared out most of the distortions introduced by feckless inflationary policies of the previous decade (most notably, America's going off the gold standard in 1971), and prepared the way for the generation-long period of economic expansion that lasted until 2000.

All indications suggest that we are nearing, and perhaps have already reached, the end of the party. For one thing, the Fed has been forced to begin raising interest rates again, a policy which cannot help contracting the money supply. For another, at the consumer level, Americans simply can no longer afford to purchase oil as they once did, causing a massive backlog in crude oil that producers cannot sell at prices they were once accustomed to. In the end, the little man, ground down by years of economic stagnation, is having his say. High oil prices, a critical contributor to the portfolios of the wealthy, are being destroyed by lack of demand.

Unsustainably high oil prices are one of the most systemically important distortions created by inflationary monetary policy. High oil (and gas) prices drive production of the world's most important market commodity. The huge market sector that contributes to oil production — including not only oil and other energy companies but also those who manufacture the equipment to explore, drill, and refine, and those that transport and sell the oil to the customer — are all adversely affected by declines in oil prices. The grotesque pricing distortions in the energy sector (and other sectors that depend upon it) are in the process of being corrected, which may result in insolvency for many companies that have structured their finances and allocated their capital in accordance with oil prices that are grossly out of line with economic reality. This is the concern driving the collapse of stock prices, and it is a typical "emperor-with-no-clothes" revelatory moment that can trigger the crack-up at the end of an inflationary boom.

By all appearances, another recession — years overdue — is in the offing. Walmart announced on Friday the shuttering of 269 stores, doubtless because ordinary people — the ones who shop at Walmart and fill their cars with regular gas — are no more filling their shopping carts than they are their gas tanks.

And there are other factors that threaten to further undercut the markets' sense of invulnerability: things such as the increasing likelihood of a major war in the Middle East, war on the Korean Peninsula, and conflict with Russia over the Ukraine. Add to that the uncertainty inherent in a major election year, and we are likely to have a rough economic row to hoe in the near-term future.

Photo showing traders at the New York Stock Exchange: AP Images