Dow, S&P hit record highs

Wall Street celebrates Fed decision to maintain pace of money-printing

Patrick Martin
19 September 2013

In a surprise move that sent the US stock market surging upwards, the Federal Reserve Board on Wednesday decided to continue for the present its policy of buying $85 billion a month in Treasury notes and mortgage bonds.

Stock prices, which had declined in morning trading, promptly rocketed upwards, with the Dow Jones Industrial Average closing at an all-time record of 15,676, up 146 for the day. The Standard & Poor's 500 stock index also ended the day at a record high, hitting 1,725 after rising by more than 20 points.

It was a spectacle of unadulterated greed as Wall Street celebrated the Fed's move to keep the gusher of cash flowing into the financial markets, underwriting a huge run-up of share values, bank and corporate profits, CEO pay and the fortunes of the rich and super-rich. The Fed's unprecedented pumping of trillions of dollars into the banking system, essentially by printing money, has fueled a bonanza for the ruling class, even as the real economy remains mired in slump and living standards for the vast majority of the people stagnate or decline.

The policies pursued by the Fed and the Obama administration have exacerbated economic inequality in America to an unprecedented degree. While the army of unemployed remains the largest since the Great Depression, corporate America and the financial elite have seen their wealth surpass pre-crash levels.

In the five years since the financial crisis erupted in mid-September 2008, corporate profits are up 40 percent and the S&P 500 index is up 46 percent. The Dow Jones index is up 150 percent since its post-crash low in March 2009.

The widespread expectation was that a meeting of the Fed's policy-making Federal Open Market Committee (FOMC) September 17-18 would decide to begin reducing the scale of bond purchases. This view was fueled by outgoing Fed Chairman Ben Bernanke's declaration three months ago that the policy of quantitative easing (QE) would be phased out gradually, in all likelihood beginning this year.

At the two-day meeting, however, there was near unanimity among voting members of the FOMC to delay any scaling back of QE. At a press briefing after the meeting, Bernanke cited several reasons for the reversal, including the slowing of US economic growth, uncertain prospects for the global economy, and the possibility of financial shocks generated by the stalemate in Washington over the federal budget, including a renewed crisis over the federal debt ceiling.

The decision to put off scaling back QE was a tacit acknowledgment that the US and world economy, far from recovering, is weakening. Five years after the Wall Street crash, none of the underlying contradictions that led to the disaster have been addressed, let alone resolved. Instead, the global financial system has become completely dependent on virtually unlimited subsidies by central banks and governments, exacerbating the contradictions that led to the crisis in the first place.

The budget and debt crises resulting from the diversion of trillions in public funds to prop up the banks are used, in turn, to justify a brutal assault on the living standards of the working class and the gutting of social programs upon which working people depend.

The decision also illustrated the immense power wielded by the major banks, which largely dictate government policy. On the eve of the Fed meeting,

Wall Street, acting through its stooges in Congress from both parties, engineered the withdrawal of former Obama economic adviser Lawrence Summers from consideration to replace Bernanke when the current Fed chairman retires at the end of this year. The big banks considered Summers insufficiently committed to continuing the colossal public subsidies of their profits, and sent a shot across the bow of the Fed by torpedoing his bid to become the new chairman.

What Bernanke did not say at his press conference—but which was demonstrated by the market reaction—is that Wall Street is utterly addicted to the financial stimulus provided by the Federal Reserve bond purchases. Any significant cutback could trigger a new financial collapse that would dwarf the 2008 crisis that followed the bankruptcy of Lehman Brothers.

The statement issued by the FOMC specified that the Fed would continue the current pattern of buying $40 billion in mortgage-backed securities and $45 billion in Treasury securities every month. The mortgage-backed securities are particularly critical to the financial position of the major banks, which still have vast quantities of largely worthless mortgage paper that they have been unloading on the US central bank for the past five years.

According to the statement, the Fed "reaffirmed its view that a highly accommodative stance of monetary policy will remain appropriate for a considerable time after the asset purchase program ends." In other words, even when the bond purchases are phased out, interest rates will be kept at near-zero levels for a further lengthy period.

The Federal Reserve also issued a revised economic forecast, cutting its projections for economic growth this year to a range from 2 percent to 2.3 percent, down from its prediction in June of growth between 2.3 percent and 2.6 percent. The projected growth rate for next year was also reduced, from a range of 3 to 3.5 percent to a range of 2.9 to 3.1 percent.

This projection—which optimistically assumes no renewal of the global financial crisis—means that the US unemployment rate is likely to remain far higher than the normal level at least until the end of 2016. Any reduction in unemployment will be the result more of discouraged workers leaving the work force than any actual upturn in economic activity.

Besides the need for the financial markets to get their monthly injection of fresh cash, there are other factors underlying the Fed decision. Of particular concern is the state of so-called emerging markets, the economies of countries such as India, Indonesia, Turkey, South Africa and Brazil, which received a sharp blow from Bernanke's hints of a letup in quantitative easing.

In anticipation that the phase-out of Fed purchases would lead to a tightening in US financial markets and a rise in US interest rates, globally mobile capital has begun to flow out of the emerging markets and back into the US. The result has been a sharp drop in the currencies of the affected countries, which has fueled inflation and worsened the position of companies and governments that borrowed in dollars or other foreign currencies and now find their debts more expensive to repay.