

Shut Down the Fed (Part II)

[Is Bernanke the new Von Havenstein, head of the Weimar Reichsbank?](#)

Ambrose Evans-Pritchard – Telegraph UK 27th Sept 2010

I apologise to readers around the world for having defended the emergency stimulus policies of the US Federal Reserve, and for arguing like an imbecile naif that the Fed would not succumb to drug addiction, political abuse, and mad intoxicated debauchery, once it began taking its first shots of quantitative easing.

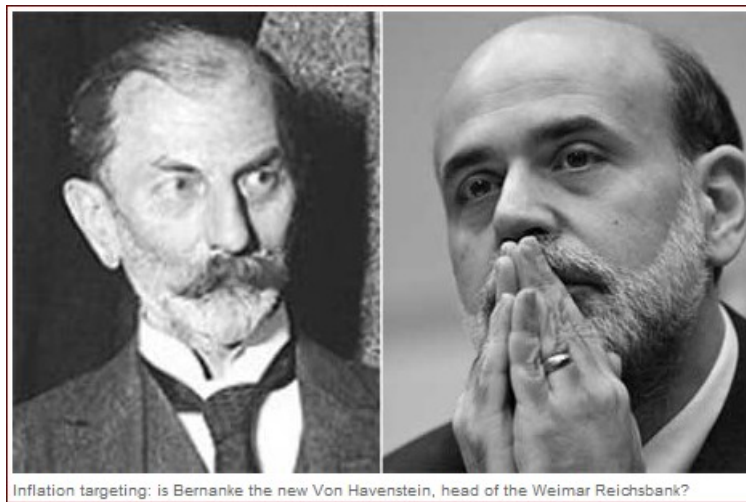
My pathetic assumption was that Ben Bernanke would deploy further QE only to stave off DEFLATION, not to create INFLATION. If the Federal Open Market Committee cannot see the difference, God help America.

We now learn from last week's minutes that the Fed is willing "to provide additional accommodation if needed to ... return inflation, over time, to levels consistent with its mandate."

NO, NO, NO, this cannot possibly be true.

Ben Bernanke has not only refused to abandon his *idée fixe* of an "inflation target", a key cause of the global central banking catastrophe of the last twenty years (because it can and did allow asset booms to run amok, and let credit levels reach dangerous extremes).

Worse still, he seems determined to print trillions of emergency stimulus without commensurate emergency justification to test his Princeton theories, which by the way are as old as the hills. Keynes ridiculed the "tyranny of the general price level" in the early 1930s, and quite rightly so. Bernanke is reviving a doctrine that was already shown to be bunk eighty years ago.



Inflation targeting: is Bernanke the new Von Havenstein, head of the Weimar Reichsbank?

So all those hillsmen in Idaho, with their Colt 45s and boxes of krugerrands, who sent furious emails to the Telegraph accusing me of defending a hyperinflating establishment cabal were right all along. The Fed is indeed out of control.

The sophisticates at banking conferences in London, Frankfurt, and New York who apologized for this primitive monetary creationsim – as I did – are the ones who lost the plot.

My apologies. Mercy, for I have sinned against sound money, and therefore against sound politics.

I stick to my view that Friedmanite QE '*a l'outrance*' is legitimate to prevent a collapse of the M3 broad money supply, and to prevent outright deflation in economies with total debt levels near or above 300pc of GDP. Not in any circumstances, but where necessary, and where conducted properly by purchasing bonds outside the banking system (not the same as Bernanke "creditism").

The dangers of tipping into a debt compound trap – as described by Irving Fisher in *Debt-Deflation Theory of Great Depressions* in 1933 – outweigh the risk of an expanded money stock catching fire and setting off an inflation surge later. Debt deflation is a toxic process that can and does destroy societies as well as economies. You do not trifle with it.

But deliberately creating inflation "consistent" with the Fed's mandate – implicitly to erode debt – is another matter. Nor can this be justified at this particular juncture. M3 has been leveling out. M2 has begun to rise briskly. The velocity of money has picked up. The M1 monetary multiplier has jumped.

We have a very odd world. The IMF has doubled its global growth forecast to 4.5pc this year, and authorities everywhere have ruled out a serious risk of a double dip recession.

Yet at the same time the Bank of Japan has embarked on unsterilised currency intervention, which amounts to stimulus, and both the Fed and the Bank of England are signalling fresh QE.

You can't have it both ways. If the US is not in deep trouble, the Fed should not be thinking of extra QE. It should step back and let the economy heal itself, if necessary enduring several years of poor growth to purge excess leverage.

Yes, U6 unemployment is 16.7pc. But as dissenters at the Minneapolis Fed remind us, you cannot solve a structural unemployment crisis with loose money.

Fed is trying to conjure away the hangover from the last binge (which Greenspan/Bernanke caused, let us not forget), as if to vindicate its prior claim that you can always clean up painlessly after asset bubbles.

Are the Chinese right? Are the Americans and the British now so decadent that they will refuse to take their punishment, opting to default on their debts by stealth?

Sooner or later we may learn what the Fed's hawkish bloc of Fisher, Lacker, Plosser, Hoenig, Warsh, and Kocherlakota really think about this latest lurch into monetary la la land, with all that it implies for moral hazard and debt contracts.

If I have written harsh words about these heroic resisters, I apologise for that too.