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The Fed and Manufactured Crises

The Politics of Economic Redistribution

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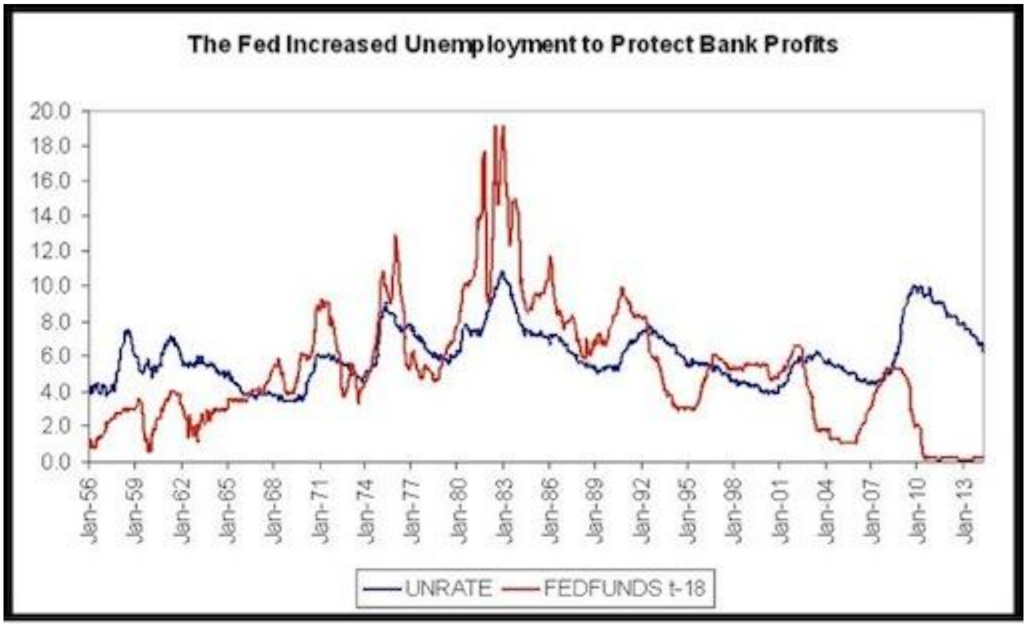
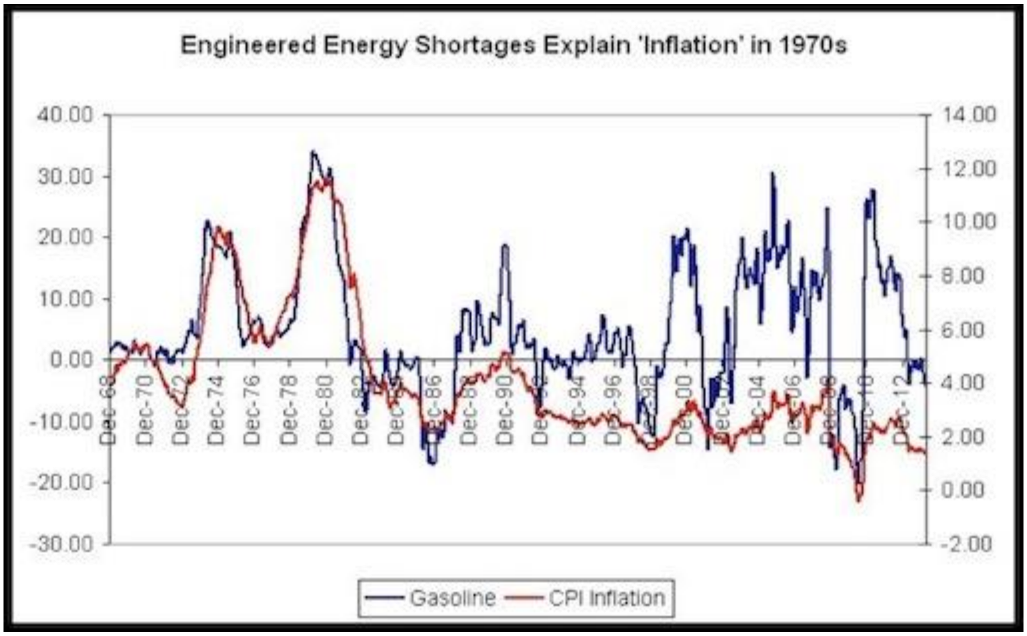
The ascendance of finance in recent decades has oriented understanding of 'the economy' toward financial terms and policies. The Federal Reserve at the heart of 'monetary' policy in the U.S. is a public- private consortium run by bankers in the interests of Wall Street. The history of Fed policies in the modern era, from the end of WWII to the present, is of engineering periodic recessions to protect bank 'assets' from depreciation through inflation. The social cost of these policies has been regular bouts of unemployment salved until the 1970s by unemployment insurance that covered a significant portion of the unemployed for about as long as these engineered recessions lasted. Toward the end of the 1970s rising 'inflation' was used to justify Fed Chairman Paul Volcker's purposeful creation of what at the time was the worst recession since the Great Depression. Wide scale and persistent unemployment was the result. When considered in historical context Mr. Volcker's actions were at the vanguard of the corporate-capitalist coup that goes far in explaining present circumstance.

Graph 1: Using a combination of economic theory and questionable 'empirical' methods to measure inflation the Federal Reserve regularly engineered recessions by raising interest rates. The Fed would raise rates and unemployment would rise 12-18 months later. The Fed would then lower rates and unemployment would fall. The manufactured 'inflation' of the 1970s was used to break the power of organized labor under the contrived misdirection that rising wages *tied to cost-of-living-adjustments in union contracts were the cause of inflation. The actual cause of the 1970s 'inflation' is explained below.*



That Fed Chair Volcker was appointed by Democrat President Jimmy Carter in the midst of broad moves to 'de-regulate' the U.S. economy and the wholesale abandonment of the Keynesian policies that had guided the U.S. since the Great Depression is more than an accident of history. The epic that followed, finance capitalism, is still under way and it represents a series of manufactured crises in support of a financial plutocracy. Mr. Volcker was a former banker and the confluence of circumstances that contributed to public acceptance of barely plausible explanations of the events of the 1970s, the roots-genesis of current circumstance, were contrived and sold with the goals of breaking organized labor and creating-recreating the system of economic expropriation through finance that preceded the Great Depression. The first 'tool' used was the sequential energy 'crises' that began with multi-national oil companies holding oil supplies offshore under the misdirection that an 'Arab oil embargo' was the cause of suddenly reduced energy supply. The Iranian Revolution later in the decade was a real but geopolitical, not economic, explanation of energy shortages. The OPEC 'cartel' members initially in favor of withholding oil from the U.S., Iran and Venezuela, were supporting U.S. geopolitical interests in the early-mid 1970s. (Oil prices have international consequence). The engineered energy 'crises' did cause a rise in 'inflation,' but the term is wholly misleading as economic explanation.

Graph 2: The 'inflation' of the 1970s attributed to outsized wages of labor is well explained by rapidly rising oil prices from engineered oil 'crises.' Agricultural policies that restricted production also contributed. The 'inflation' that resulted was used to break the bargaining power of labor through moves to eliminate collective bargaining 'rights' and through the promotion of 'market' economics claiming that labor market 'flexibility' was the solution. The role of 'liberal' economists in mystifying 1970s inflation and in subsequently promoting 'market' economics as the solution to it places them as effective facilitators of this right-wing coup.

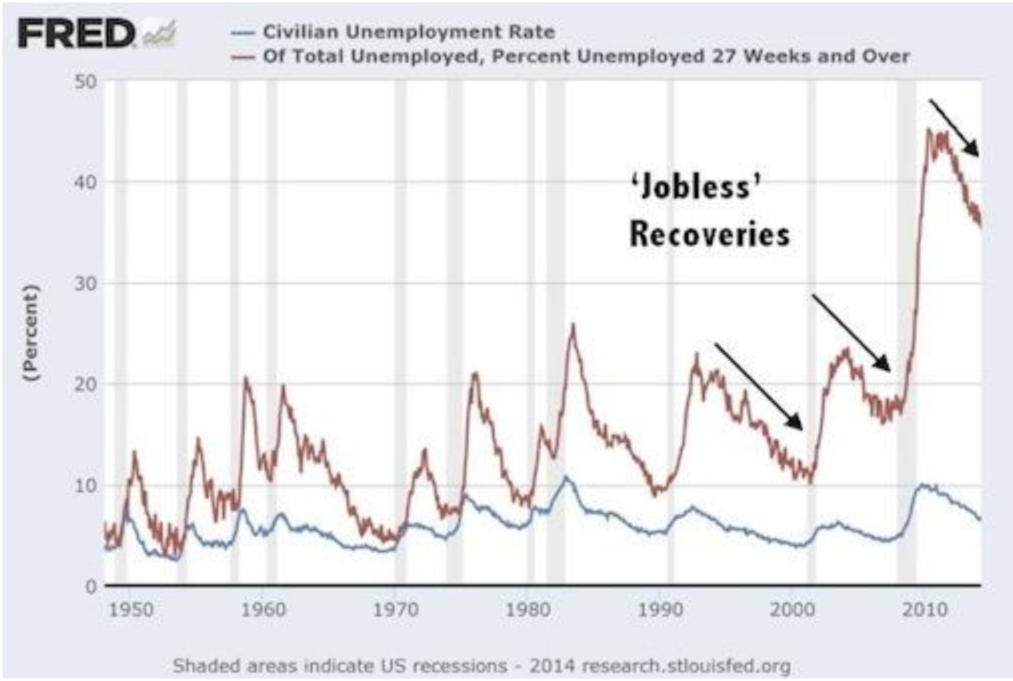


With the last energy 'crisis' of the 1970s the result of the Iranian Revolution, having Fed Chair Volcker sink the economy by raising interest rates to their highest level in modern history successfully associated one set of manufactured crises— the energy 'embargoes,' with another, 'inflation,' to recontextualize political failures and contrived emergencies as products of 'the economy.' Mr. Volcker could have waited for the energy 'shocks' to abate and the problem of 'inflation' would have been solved without creating widespread unemployment. (Richard Nixon had already addressed agricultural inflation by the mid-1970s but the 'solution,' odious as it is— the ascendance of industrial agriculture, took a few years to fully implement). By raising interest rates Mr. Volcker attracted international capital chasing high yields on U.S. assets and raised the value of the U.S. dollar. In conjunction with sequential energy 'crises' Mr. Volcker effectively killed the industrial economy by making U.S. goods more expensive overseas. The massive industrial unemployment that resulted took place at the precise time of pivot toward financialization of 'the economy.' The misdirection put forward then and now was that factories were closing because U.S. labor was too expensive and that U.S. factories were no longer 'competitive.' To be clear, the currency exchange rate determined the 'price' of U.S. labor relative to overseas labor and this is the 'price' that was dramatically raised by Mr. Volcker. Upon Ronald Reagan's election the process of financializing the economy was moved further forward through Mr. Reagan's appointment of ex-Merrill Lynch banker Don Regan as Secretary of the Treasury.

The political result that conflating manufactured energy shortages with inflation accomplished came through the 'Phillips Curve,' the theorized tradeoff between inflation and employment. In the immediate post-War period when the Federal Reserve raised interest rates unemployment rose and 'inflation,' narrowly defined, fell and vice versa. Since the 1980s the relationship has become more ambiguous (Graph 1 above). But considering the experience of the 1970s, where contrived and 'accidental' crises were placed into economic terms to pose a 'natural' basis for inflation, the entire enterprise is suspect. The confluence of rising inflation driven by contrived oil 'shocks' with economic weakness— 'stagflation,' only appears a great mystery to those determined to see a great mystery. Actual 'inflation' as the economic mainstream has it can be traced in many instances to policy decisions like the structure of agricultural subsidies, oil geopolitics, wars and trade policies. Financial asset price inflation is nowhere to be found in mainstream theory because money is 'neutral.' In case this isn't yet clear, at the nexus of Fed and mainstream economic policy prescriptions labor causes inflation— a problem for lenders, not necessarily for labor. The frame might be inverted— that rising inflation 'causes' employment and vice-versa, the 'liberal' Phillips Curve interpretation. But the political economy coming out of the 1970s was clearly of industrial and finance capitalists working to end the bargaining power of organized labor—the wages of labor must be restrained for the benefit of 'the economy,' to prevent 'inflation.' But the rising 'wages' of capital, profits and capital gains, are economically 'neutral' — they don't contribute to 'real' inflation because money is neutral and financial asset price inflation doesn't occur because yes, money is neutral.

What many liberals and progressives don't appear to understand is that mainstream Western economics is narrow capitalist ideology— there is no capitalist 'left.' New Keynesian economics incorporates Milton Friedman's critique of the Phillips Curve from the frame of distinguishing 'natural' from 'unnatural' unemployment when specific government policies such as supporting, or not supporting,' collective bargaining 'rights' have direct bearing on the institutional 'facts' of employment and unemployment. Germany makes it prohibitively expensive to fire workers rendered 'redundant' through corporate mergers thereby greatly reducing the incentive for mergers and strengthening the hand of labor. The distinction between 'natural' and 'unnatural' unemployment is a dim hoax designed to convince workers who are being screwed that it is 'nature' doing the screwing when it is specific industrialists and financiers who are doing it and particular economists who are mystifying the process. While New Keynesians are writing endlessly about a 'zero lower bound' what is being left unsaid is that the Federal government could create a job for everyone who wants one at a living wage with health care benefits and pensions. Proposals for a milder version of such a program put forward in 2009 were met with a wall of charges that 'inflation' would be the result. Through Fed policies financial asset prices have more than doubled since 2009 with nary a word about 'inflation' from the economic crowd in full-blown panic over people getting jobs in government programs.

Graph 3: Since the 1970s the Federal Reserve has continued to raise and lower interest rates from sequentially lower levels (Graph 1 above) in response to the perceived threat of rising inflation. Raising interest rates has 'successfully' raised unemployment while lowering them has had muted impact in reducing it. The result is 'jobless recoveries' where it took much longer for employment to return to previous levels. Given three decades of stifled median wage growth worry over inflation caused by 'excess' employment is delusional, the result of embedded ideology.



It might seem that the economic left and the 'concerned' mainstream that wants to see unemployment fall and labor wages rise are 'on the same side.' However, the difference is partly of analysis and partly of intent. By placing the 'stagflation' of the 1970s in an economic context that left the overwhelming effect of geopolitics, cartel economics and agricultural policies out of its explanation 'labor' was effectively blamed for a decade of economic turmoil because that was all that the mainstream 'frame' could assert. And by putting forward discussion of 'inflation' framed as a relationship between 'real' prices and employment the mainstream has supported the banker economics of the Federal Reserve in regularly and needlessly increasing unemployment and it has directed attention away from the role of bank money, leverage and financial asset price inflation in the massive concentration of 'wealth' that has taken place since the 1970s. Framed differently, financial markets have leapt from one bubble to another while 'real' inflation has been falling for three decades now. But financial inflation is de facto inflation for those on the 'losing' side of it, the 99.5%, by raising and shifting the quantity of financial claims outstanding without an offsetting increase in 'real' economic production. Were this not the case discussion of income and wealth inequality would be meaningless because they would have no consequence, no claim on social resources. This leaves the economic mainstream viewing Federal Reserve policy as a 'solution' to high unemployment and falling wages based on a demonstrably bogus 'model' that relates rising inflation to labor.

It requires real determination to look at the totality of economic policies undertaken since Wall Street killed the economies of the West in the mid-2000s and not see that policies that benefited finance and the already rich have been aggressively moved forward while those that directly benefit everyone / anyone else have gone nowhere. Federal Reserve policy has been unhindered by institutional constraints— the Fed has spent four trillion dollars buying assets from Wall Street at inflated prices (per Ben Bernanke in 2009). The incomes and wealth of the very richest have been fully restored, as has Wall Street's capacity to once again kill the economies of the West at a moments notice. At what point do liberal monetary 'solutions' run up against the reality that the only sure-fire result of negative interest rates, or policies to get around their implausibility, would be to further benefit the already rich and Wall Street? Until capitalism is over and done with the way to put people to work in the face of market 'failure' is through government jobs programs that are independent of Fed policies. That doing so is politically infeasible while saving Wall Street and the wealthy is feasible illustrates the basis of social power in economic power. In other words, radical economic redistribution schemes are not only feasible, we've seen one of the greatest demonstrations of radical redistribution in human history over the last thirty or so years. Rarely in human history have so few 'owned' so much. And the Federal Reserve has been at the heart of that 'success' story.