

On This Day - 11 August 2010

## Fed corrects debt problem with more debt

Ouzilly, France,

The big news yesterday was that the Fed decided to do about what we expected - not much.

Bloomberg has the report:

*Federal Reserve officials decided to reinvest principal payments on mortgage holdings into long-term Treasury securities, making their first attempt to bolster growth since March 2009 to keep the [slowing U.S. economy from relapsing into recession](#).*

----- FREE Newsletter -----

### **Straight from the Hip - A Weekly E-Letter**

*"This weekly stock market column written by me has run for over 19 years on various platforms. I invite you to subscribe today for a fresh and thought-provoking perspective."*

*- J Mulraj*

*Available exclusively to readers of Equitymaster. [Sign-up Now!](#) It's Free!*

-----

*"The pace of [economic recovery](#) is likely to be more modest in the near term than had been anticipated," the Federal Open Market Committee said in a statement in Washington. "To help support the economic recovery in a context of price stability, the Committee will keep constant the Federal Reserve's holdings of securities at their current level." The Fed retained a commitment to keep its benchmark interest rate close to zero for an "extended period."*

*With growth weakening in the second quarter and company job gains in July falling short of estimates, today's step signals that risks of a downturn have increased enough for the Fed to delay its exit from unprecedented stimulus. Chairman Ben S. Bernanke told Congress last month that the Fed was "prepared to take further policy actions as needed."*

*The Fed's last move in favor of easier policy came in March 2009, when policy makers agreed to buy \$300 billion of Treasuries and more than double planned mortgage-debt purchases to \$1.45 trillion while starting a pledge to keep the benchmark rate close to zero for an "extended period."*

So, the Fed has made another mini-move. And the markets reacted appropriately, in a mini-way. Stocks went down a little - minus 54 on the Dow. Gold went down a bit too - off \$4, to bring the price to \$1,198.

Barron's was not wrong. Just early. You'll recall the newspaper says the Fed will "Print \$2 trillion." Yes, it probably will. But not now...not yet. Not as long as the Treasury can finance federal deficits by borrowing and the stock market hasn't collapsed..

But the Fed is in a trap of its own making. It doesn't really understand what is going on. It

thinks there is a problem in the economy caused by consumers who are unwilling to spend. It believes it should use its policy tools to help pry the money out of their pockets. Trouble is, consumers don't have any money in their pockets. And if they did have some, they wouldn't want to spend it.

Of course, the Fed knows this much. But they think that if they can get people spending again, the economy will take off, employment will rise, incomes will go up and everything will be hunky dory again.

They don't seem to wonder why - if things were so hunky dory in the bubble years - there was a crisis in the first place. Never once have we heard anyone of them - not Bernanke, Summers, or Geithner -- explain that the private sector had run up too much debt (largely because of their own economic policies) ...and that now it is paying the price.

Instead, they think the economy is sick and that they are all Dr. Schweitzers. The whole thing - meaning, the body of ideas, theories, prejudices, plans and programs of the financial authorities - is really asinine. Which is what is really interesting about this episode in history. So many very smart people have come to believe such absurd things. It's a marvel. And marvelously entertaining to watch. What will they say and do next?

They don't have much choice. Their silly ideas drive them into silly positions...from which there is no gracious exit. The economy is correcting from too much debt. They're determined [to stop the correction with the only thing they have to offer -more debt](#). And funny money, of course.

They're not stupid, though. They also know that they can't go too far or they will do even more damage than they're doing now. So, they'll save that disastrous step for later...when they're really desperate. Then, we'll see them "Print \$2 trillion." Or print \$3 trillion. Or more.

In the meantime, it's 'muddle onwards' for the authorities! One misstep after another. Headlong into one trap...then onto the next!

More news:

And more thoughts...

\*\*\* More zombification...

As an economy matures, more and more people begin to shuffle and drool. They figure out how to use the political system to get something for nothing. The article below, from USA Today, tells the tale of government employees.

They went to Washington to do good....and they've done very well.

*By Dennis Cauchon, USA TODAY*

*At a time when workers' pay and benefits have stagnated, federal employees' average compensation has grown to more than double what private sector workers earn, a USA TODAY analysis finds.*

*Federal workers have been awarded bigger average pay and benefit increases than*

*private employees for nine years in a row. The compensation gap between federal and private workers has doubled in the past decade.*

*Federal civil servants earned average pay and benefits of \$123,049 in 2009 while private workers made \$61,051 in total compensation, according to the Bureau of Economic Analysis. The data are the latest available.*

*The federal compensation advantage has grown from \$30,415 in 2000 to \$61,998 last year.*

*Public employee unions say the compensation gap reflects the increasingly high level of skill and education required for most federal jobs and the government contracting out lower-paid jobs to the private sector in recent years.*

*"The data are not useful for a direct public-private pay comparison," says Colleen Kelley, president of the National Treasury Employees Union.*

*Chris Edwards, a budget analyst at the libertarian Cato Institute, thinks otherwise. "Can't we now all agree that federal workers are overpaid and do something about it?" he asks.*

*Last week, President Obama ordered a freeze on bonuses for 2,900 political appointees. For the rest of the 2-million-person federal workforce, Obama asked for a 1.4% across-the-board pay hike in 2011, the smallest in more than a decade. Federal workers also would qualify for seniority pay hikes.*

*Congressional Republicans want to cancel the across-the-board increase in 2011, which would save \$2.2 billion.*

*"Americans are fed up with public employee pay scales far exceeding that in the private sector," says Rep. Eric Cantor, R-Va., the second-ranking Republican in the House.*

What the data show:

- **Benefits.** Federal workers received average benefits worth \$41,791 in 2009. Most of this was the government's contribution to pensions. Employees contributed an additional \$10,569.
- **Pay.** The average federal salary has grown 33% faster than inflation since 2000. USA TODAY reported in March that the federal government pays an average of 20% more than private firms for comparable occupations. The analysis did not consider differences in experience and education.

•**Total compensation.** Federal compensation has grown 36.9% since 2000 after adjusting for inflation, compared with 8.8% for private workers.