Stock Market Suspiciously Healthy. The Federal Reserve Does All It Can to Keep Economic Reality From Setting In.

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Despite 33 states with over 10 percent unemployment rates, gross domestic product quarterly dives of over 50 percent, and a resurgence of COVID-19 infection numbers making both those conditions seem unlikely to turn around soon, the stock market as a whole remains strangely healthy. The Dow Jones Industrial Average is actually up over 1,500 points since mid-March when the coronavirus shutdowns began in earnest (though still down more than twice that number of points from the optimistic beginning of 2020).

While ultimately the only sure reason why the stock market does what it does is "the people buying and selling stocks make decisions that lead to those prices," one very likely reason those making such decisions seem to think staying in and even buying more is a good idea right now is a concerted government effort to socialize the risk inherent in buying stocks across the economy.

The establishment market-watchers at *The Wall Street Journal* spelled out this thesis yesterday: "Expectations that the U.S. Federal Reserve will keep injecting liquidity into the market have helped fuel rebounds each time fallout from the coronavirus pandemic have sparked selloffs," with one analyst insisting that because of Fed policy, "There's a safety net under the bond market and the equity market."

This judgment that government policy wants to get stock buyers and sellers to ignore grim economic reality via what amounts in part to special favors to big corporations is widespread. One of the reasons why is the Federal Reserve's eager buying up of corporate debt this year.

CNN reports some of the implications of that:

In a note to clients Monday, Goldman Sachs said the Fed's announcement that it would buy corporate bonds in the primary and secondary markets was enough to quickly provide relief. "The mere presence of the backstops helped to restore the flow of private credit," chief economist Jan Hatzius said.

Lip service to the idea that these policies create problems for those not getting the help is given, as CNN notes. ("There are fears that an ongoing commitment to corporate bond purchases could create a so-called 'moral hazard,' encouraging companies to borrow more from less-selective lenders on the expectation that Fed intervention would limit risks.") But such considerations almost never stop the government from doing what it can to help out Big Money.

Hussein Sayed, chief market strategist at FXTM, was warning his clients this week, CNN reported, that "monetary policy stimulus which explains most of the recovery in asset prices from the March lows will become less effective going forward if it doesn't translate into a rebound in economic activity and better prospects for corporate earnings."

The Washington Post reminds us that the "central bank has said it launched the corporate debt program to support the markets," although it's "unclear what the implications of its actions will be" as "the Treasury Department has devoted $75 billion to the Fed's two corporate credit facilities as part of a pot of money allocated by the Cares Act….The Fed has bought almost $429 million in individual bonds," buying them both directly from the company and from investors or funds that already owned previously issued bonds.

Aaron Klein, policy director of the Center on Regulation and Markets at the Brookings Institution, is quoted in the *Post* asking: "Why is the solution buying Apple, Microsoft and Comcast debt? Or eBay or Google?…Is the problem in America that the holders of Apple stock need more help? Is the problem that investors in Google debt are likely to suffer catastrophic and unexpected losses from the covid shutdown?"

As *Politico* reported regarding this latest round of Federal Reserve corporate debt buying, "most of the debt has to be considered investment-grade by credit ratings services, meaning it carries minimal risk to investors. But otherwise eligible firms that have been downgraded a notch to junk status since late March will still be included in the program." Even if no actual straight-up losses to the government (read: all of us) arise from such debt buying, their very existence distorts where investment and growth goes, to the advantage of big business' being temporarily propped up.

As James Dorn of the Cato Institute further explained:

The promise of supporting corporate bond prices and making loans to highly leveraged companies undermines corrective market forces: real markets are supplanted by pseudo markets in which the central bank will be subsidizing distressed companies and politicizing the allocation of capital. Initially private investors may purchase more corporate debt, but if corporations use that credit to pay off existing debt, and do not invest in productive capital, losses may continue. Private investors then will have an incentive to offload their holdings to the SPV [the Fed's "special purpose vehicle" for such debt buys], effectively socializing those losses. Those who value private, free markets recognize that the Fed's promise to revitalize corporate debt markets is, in reality, a step toward market socialism.

The Federal Reserve has since the 2008-09 economic crisis become more and more a holder of financial assets of all sorts, a change whose risks are detailed in this 2014 *Reason* feature, "How the Fed Got Huge," by Jeffrey Rogers Hummel.