Free Money, Inflation And Unemployment

If nineteenth century economist and philosopher Karl Marx could state, "Religion is the opium of the masses," would a twenty-first century successor say the same about the stock market? Judging from the stated intentions of Federal Reserve officials including Ben Bernanke and Janet Yellen the answer has to be, "Yes." Both cite the wealth effect in justifying money-printing, which they deny they are doing. Yellen even offered that completing the current round of money-printing would lead to the creation of 700,000 new jobs.

I thought the $787 billion American Reinvestment and Recovery Act of February 2009 was supposed to bring unemployment down below 8%. Hmm; I am always the last one to get the memo.

Let's do a little back of the envelope math here. The American workforce has shrunk by 3.6 million since we went to zero percent interest rates back in December 2008 and 1.36 million since the first round of money-printing began in March 2009. Now let's stipulate monetary policy operates with long and variable lags, which sounds so much more scientific than saying we do not have a clue as to what will happen and when; aboriginal members of cargo cults can say their dances on the runways of some South Seas island also operate with long and variable lags and be equally correct.

QE1 as it is known affectionately as it sounds so much more scientific than Monopoly Money involved $300 billion of Treasury purchases and another $1.25 trillion (How much is a trillion? Lots; thanks for asking) in mortgage purchases which are being run off into Treasuries as they mature. The total coughed up to-date in QE2 is $208.374 billion. What used to be thin air is now more than $1.7 trillion (1,700,000,000,000) and seven quarters into the deal employment is lower. Please remember the recession ended in June 2009.

And we are supposed to believe the next $400 billion will trigger a stampede to hire American labor when a quarter-century of evidence suggests you discourage the use of labor by making capital cheaper and technology more efficient?

NAIRU And You

There's a Keynesian concept called the "non-accelerating inflation rate of unemployment," mercifully abbreviated to NAIRU. The Organization of Economic Cooperation & Development, mercifully abbreviated to OECD, estimates this to be 5.38% (gotta love those two decimal points) for the U.S. If we added the 700,000 jobs forecast by Yellen that would put, depending on the overall size of the labor force at the time, the U.S. to NAIRU.

Restated, the Federal Reserve will create inflation either by spraying so much money into financial markets here and abroad that it will come out of our ears and perhaps elsewhere or by (stop laughing) being so successful in creating jobs by printing money we will reach and exceed NAIRU.

What about that trickle-down from a stock market rally? We do have evidence money-printing has helped push stock prices higher; the total return on the Russell 3000 since the August 27, 2010 date when Ben Bernanke announced his intentions has been close to 22.9%. The total return on 7-10 year Treasuries has been -3.06%, but not to worry: The FOMC stated rates are lower than they would have been in the absence of money-printing. Whatever they do is right, and just as Humpty Dumpty could define words to mean what he chose them to mean, no more and no less, the FOMC gets to measure its own successes.

Did we mention ten-year TIPS breakeven rates of inflation have increased from 1.627% to 2.39% since the Jackson Hole pronouncement and the "real" yields of 15-year+ TIPS have increased while only those of less than five year maturity have decreased? This is a novel theory of capital markets, is it not, that you can encourage investment in job-creating plant and equipment by increasing its cost?

Memo to file: Employment is created in the real world by real entrepreneurs making real investments, not by government programs. A factory or an office or a mine demands labor; a stock certificate demands only excess funds regardless of the source and no questions asked.