QE∞

Ben Bernanke [announced a third round](http://www.telegraph.co.uk/finance/economics/9541857/Federal-Reserve-announces-QE3-to-aid-US-recovery.html) of monetary easing on part of the Federal Reserve this week. While some have called it QE 3 (quantitative easing 3), I call it QE ∞ (quantitative easing infinity). Bernanke announced that the Fed would purchase $40 billion of mortgage backed securities each month for the foreseeable future. Unlike the first two rounds of monetary easing (money printing) this one does not come with a final count of how much money will be printed. Robert Mugabe would be proud.

Here are some key questions to be asked regarding monetary easing: What will be its impact on the economy? What will be its impact on asset prices? Who will be hurt and who would be helped? Is the Fed truly independent of politics? Is the Fed now in charge of fiscal policy and monetary policy?

If you believe the credit rating agency Egan-Jones, more quantitative easing will be bad for economic growth. They just downgraded the US [credit rating again](http://www.cnbc.com/id/49037337). The value of the US dollar will continue to slide while commodity and asset prices will continue to climb. US stock prices spiked on the quantitative easing news. Expect gas and gold prices to go up as well. That’s great if you own assets or an electric car. [Quantitative easing helps the wealthy](http://www.cnbc.com/id/49031991). That’s not so good if you don’t have assets or want to drive anywhere in the future. Median family income has now [fallen four years running while income inequality has risen](http://www.usatoday.com/money/economy/story/2012-09-11/median-household-income/57757352/1). Quantitative easing will further push down real median household income while further increasing income inequality.

The Fed is hoping that increased nominal asset prices will make wealthy people feel wealthier. Perhaps if their retirement portfolio is worth more, the argument goes, they will open up their wallets and spend. This spending then is supposed to generate new jobs. We’ll call it trickle down monetary policy. It is very much a demand driven policy. The idea is that the economy is not growing because people do not want to buy enough stuff. If only we can convince people to spend money they do not have or trick people into thinking they have money that they do not, then we would be set.

If this sounds familiar, it is exactly what the Fed did following the 2001 recession that caused an asset bubble in housing. We sure did trick millions of Americans into thinking they were wealthy enough to buy homes they could not afford. How is that working out for us? Monetary easing always leads to bubbles and bubbles burst. When bubbles burst the economy gets hurt.

Bubbles form because money is not evenly injected into the economy. In this case, by buying mortgage backed securities, the Fed is increasing the price of those assets first. Anyone who owned mortgage backed securities before Thursday’s announcement got a windfall of profit. Imagine that, Fed policy makes private bankers wealthier. By purchasing any asset the Fed is monkeying around with relative prices and conducting fiscal policy.

Standard monetary policy would mean the Fed would buy more US government debt. This would work to lower interest rates in the economy and spur investment. The problem is that interest rates cannot realistically get lower, so the Fed has moved onto conducting fiscal policy. Doing so two months before a national election certainly seems like odd timing for a politically independent central bank. Such policy is exactly what politically connected third world central banks would do – try to print the incumbent back into office. Maybe it has not helped that Mitt Romney has said he would not reappoint Bernanke to chair the Federal Reserve.

As long as politicians and the Fed focus their attention on trying to increase consumer demand they will continue to harm the economy. The Keynesian answer to every macroeconomic slowdown has always been to take on more debt. Now countries around the world are choking on debt. Yet, the Keynesian answer is still to trick people into spending money they do not have. For those Keynesians who believe that in the long run we are all dead, the long run has arrived. Ignoring that fact puts the anemic global economy in danger of being placed on life support.

On a lighter note, while we at Capitalism Today do not believe that monetary policy can trick people into becoming wealthier, we still could come up with better monetary easing than Uncle Ben. Rather than buy mortgage backed assets, the Fed should announce that for every dollar of wages (not capital gains) people earn in 2013 the Fed will send them a check for ten percent of that amount. If you make $100,000 you get an extra $10,000. Rather than try to trick people into buying stuff they cannot afford, trick them into working more and they will be able to afford more. Why try to trick people into conspicuous consumption when you can entice them to work more? Work, after all, creates wealth while consumption destroys it.