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Aggressive Fed-Rate Increases: Is Powell Doing A Volcker?

After being arbitrarily accommodating, then in a relatively sudden fit of increasing administered rates, is the current Fed Chair, Powell, trying to replicate Chairman Volcker's "success" in ending inflation in 1980? Perhaps, but since the Fed opened its doors in 1914 the US dollar is only worth, well, 3 cents on the dollar – which is an indelible record of deliberate depreciation – otherwise known as policymaking. And just what drives chronic depreciation? Generations of central bankers pushing the concept that the Fed can prevent recessions, which was understood by the original backers. Recessions followed financial crises and as "lender of last resort", such crises would be prevented, therefore no recessions. The theory is still appealing, but with 19 recessions, including one Depression, it has never worked.

In more rigorous fields of study such as physics only one failure is enough to condemn a hypothesis. But going the other way, the quickest way to raise your perceived IQ is to be appointed Chair.

Nevertheless, central banking has become a bureaucratic ritual with each generation of participants essentially responding to major market forces in the same way. Ease credit! U.S. CPI inflation soared to 14 percent in 1980, when Chairman Volcker by aggressively raising administered rates "ended inflation". So, the legend goes, but it was another global boom in commodities that drove inflation everywhere. And suffering speculative exhaustion, the global boom collapsed.

Now in responding to the most severe global price-rise since then and backing it with forceful words and rate increases, is Chairman Powell striving for Volcker's celebrity?

Whatever, but an instructive comparison is the Fed's policy during the 1920s. Accompanying World War I, the global commodity boom drove US inflation to 24 percent. The global crash in commodities drove it down to (no typo) – 6 percent and the Fed became chronically concerned that inflation was not high enough and was chronically "easy" with the supply of money and credit.

Not understanding that world financial history was on another great financial bubble, called the "Roaring Twenties", when individual recklessness was exacerbated by central bank recklessness. In adding fuel to the fires of speculation, the Fed seemed not to understand the consequences of rampant inflation in financial assets. Which has always been a severe contraction.

A change in the course of a generation event.

Huge global commodity booms completed in 2008 and 2011, which any review of financial history would suggest another great financial mania would climax about a decade later.

However, unaware of this the Fed again became concerned that inflation was too low and kept the "peddle to the metal", adding fuel to speculative furies. Again, official recklessness added to financial hyperactivity.

Virtually, propelled by the same market forces through the decade, the Fed did what it was compelled to do. And as if a switch was turned on commodities soared natural to the last phase of a bubble, compounded by the global "Lockdown". Now in a 180-degree shift, Fedsters have been galvanized from boosting inflation to now quelling rising prices. Only to be soon faced by most asset prices heading down – as with the completion of any great financial bubble.

Less than five years ago they arbitrarily stated that inflation was too low and pushed the money out the window.

This errant policy is made clear by reviewing the great events in financial history, which has been a serious war funded by inflation, accompanied by huge global commodity boom, resulting in the cost living exceeding the advance in wages. With the collapse of commodities setting up a fabulous bull market for stocks and bonds – in so many words a great financial bubble – that as it completes includes hot action in real estate and commodities.

And it is global.

And about a decade later, the financial mania climaxes and 1929 being the fifth example since the first in 1720. The action is on the path to another severe contraction that will again place the abilities, or inabilities, of central bankers in perspective.

Volcker did not personally "end" the natural global inflation. It was a global boom in commodities that, quite simply, exhausted itself in 1980. And if Powell is trying to garner unearned fame Mother Nature and Mister Margin will soon declare him a loser. Severe deflation of most asset prices has naturally followed all five previous bubbles.

The essay published upon Volcker's death follows:

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Debunking the Volcker Myth

Paul Volcker, a famous economist and central banker has passed away. Indeed, *The New York Times* headlined: ***"Fed Chairman Who Waged War on Inflation, is Dead at 92"***. This is a legend that is regrettably not supported by history. When he was in the Treasury Department, he strongly supported President Nixon's 1971 decision to take the US dollar off gold convertibility. Indeed, William Silber quoted Volcker as saying it was ***"The single most important event of*** [his] ***career."*** https://www.amazon.ca/Volcker-Persistence-William-L-Silber/dp/1608193926 Ironically, this opened the door to the ultimate in central bank ambition. Credit inflation has continued to today's outright recklessness in money markets. Spectacular bubbles in commodities and then in financial assets followed, with collapses in between. Paul Volcker was instrumental in enabling unprecedented credit inflation and its inevitable dislocations.

Of course, financial history itself is a due diligence on every speculative scheme ever floated. Including the original notion that the Fed, as "lender of last resort" would prevent the money market setbacks that precede recessions. There would be no recessions. But there's been 18 recessions since the Fed opened its doors in January 1914. Appealing theory, but it does not work. https://www.nber.org/cycles.html

As to his ending inflation – not so. The public choses when to speculate in commodities and when to crash them.

The modern world of financial markets with a central bank (BoE) was established in the late 1600s, including the first market letter in English that began publication in 1692. There have been five great booms in commodities from then until 1920. Each was associated with important countries at war and the dates have been 1711, 1763, 1816, 1864 and 1920. Naturally, these were accompanied by high rates of CPI inflation and soaring interest rates. Each completed with a speculative climax and the end to hostilities. For those interested, the internet provides adequate description of each war.

The point being, that soaring commodities and inflation and the social distress that goes with it eventually and naturally burns out. And collapses as the social strains of inflation slowly ease. As U.S. inflation was soaring to 14 percent in the late 1970s it was accompanied by considerable household distress as costs were rising faster than wages. Thus, Nixon's naive experiment in price and wage controls. Within this, inflation was considered so bad that policymakers dreamed up theories to avoid blame. One distraction was the debate about whether it was caused by "cost push or wage pull". Another explanation was that aggressive credit expansion did not cause rising prices. These were due to a sudden rise in the public's "inflation expectations". Yes, it helps to have a degree in Tautology.

When inflation was a widespread concern, the Fed avoided blame. It now worries that there has been not enough inflation, replicating it's behavior the conditions in the 1920s.

In 1981-1982, this writer's presentations to financial institutions included a controversial line: "No matter how much the Fed prints, stocks and bonds will outperform commodities." Why? Because each of the great booms in commodities had been followed by a great bubble in financial assets.

And speculation in financial assets has been the main game ever since.

It is worth reviewing America's history of outstanding examples of inflation.

With the Civil War, the rate of inflation soared to 27 percent. With no central bankers to start or end that example, inflation was accomplished by the printing of "greenbacks". The war ended and speculation in global commodities collapsed. Then the greenback was made convertible and concerns about inflation ended.

Businessmen and most people understood that inflation was not a tool to "manage" the economy. Of course, some were hooked on inflation and there was a political party formed – the Greenback Labor Party.

Next was the Great War that engaged much of Europe and was accompanied by a run-a-way global boom in commodities. With this example, the U.S. rate of inflation got as high as 24 percent. That was in 1920, and quickly now, who was the genius at the Fed who "ended inflation"?

On the overly ballyhooed 1970s inflation, the rate got to only 14 percent. As it was a global boom in commodities, the Fed had little to do with ending it. Nor did it have anything to do with any of the other the transitions from inflation in tangible assets to the wonderful world of inflation in financial assets.

Paul Volcker was not in office during any of the previous such endings of inflation. Nor was he in office with the huge commodity boom to 2008, which set up the current "New Financial Era". At extremes, Mother Nature and Mister Market rule.

By way of summary, market forces have set and ended each example of soaring inflation. As the action has been global, local central bankers have merely been along for the ride. The trick has been to "look in charge" while avoiding responsibility for contractions.

Ironically, in 2018, he published *Keeping At It: The Quest For Sound Money and Good Governance*.

And Volcker's career has been remarkable in supporting Nixon's turn to unconstrained central banking that has evolved into today's unprecedented recklessness. And even more remarkable is his being acclaimed for "ending inflation". Not so, Paul Volcker has been this generation's "father" of unrelenting and increasingly dangerous credit inflation. Whereby the Fed has been attempting to provide unlimited funding for another experiment in unlimited government. Unsound and not good.