Milton Friedman: We Didn't Deserve Him !

by Earl P. Holt III

For most of the 21st Century, the ***Federal Reserve*** (the *Fed)* has actually worked *against* the well being of most Americans. Its theoretical independence from political influences was often a **green light** for highly-partisan appointees to engage in political acts to benefit the party which appointed or confirmed them to their cushy sinecures at the Fed.

For example, as Fed Vice Chairman and eventual Chairman, Janet Yellin oversaw the *Fed's* purchase of an estimated $9 Trillion in *Electronically Traded Funds* (ETFs) to artificially stimulate the feeble economy of Barack Obama. Funds used to purchase those ETFs made their way into capital and consumption streams, which gave false signals that Obama's socialist experiment to *"transition"* the U.S. economy was succeeding. In fact, ***REAL*** GDP growth never exceeded the tepid rate of two percent. On the other hand, the cost of funding those Fed ETF purchases added trillions to our National Debt, and required the printing of trillions of inflationary new dollars from thin air.

Likewise, Wall Street and most investors now realize that current Fed Chairman Jerome Powell's sole agenda is to obstruct President Trump's economic policies. Powell is a lawyer who may know less about monetary theory and policy than he knows about brain-surgery. Powell has kept the ***federal funds*** rate at historic highs, which has halted both private sector investment and growth. (The federal funds rate is the interest rate that member banks charge each other for overnight loans to satisfy their weekly reserve requirements.) This has left U.S. entrepreneurs on the sidelines, *champing-at-the-bit* to take advantage of Trump's lower tax rates, accelerated depreciation schedules, and dramatically reduced regulatory environment.

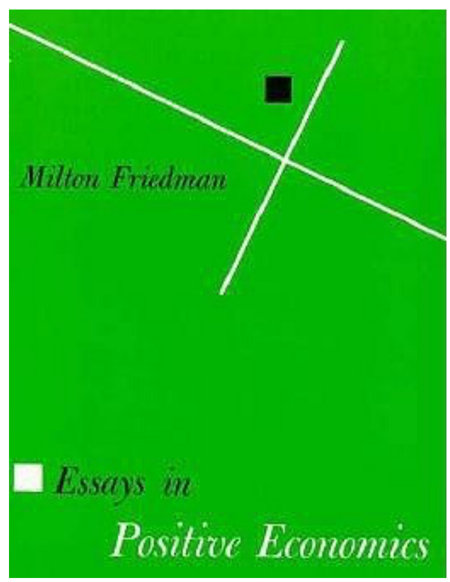
 

Fed Chairs: Janet Yellin & Jerome Powell

In contrast to these two fools, the greatest social scientist who ever lived, and the man who enabled Diogenes to retire his proverbial lamp, already gave us the solution for ending Fed politicization and its staggered, *stop-and-start* approach to monetary policy. For decades, Nobel Laureate Milton Friedman proposed a ***Constant Monetary Growth Rule*** (CMGR) to maintain predictable and consistent growth of the money supply. (Fools didn't listen.) This would immunize the Fed from internal or external events that might prompt it to intervene in ways that are counterproductive to the economy. With the high-speed computers available today, that task would be even simpler than in Friedman's day.

Friedman proposed a **3 to 4 percent** rate of monetary growth, which he assumed to be the long-term growth rate of the U.S. economy. However, after the Trump Administration dramatically accelerated depreciation schedules, lowered federal income tax rates, and eliminated many federal regulations in the ***"Big, Beautiful Bill,"*** the long-term growth rate of the U.S. economy may be significantly higher. (We won't know until Jerome Powell is gone.) Although many different definitions of *"money"* exist, Friedman recommended that the broadest possible definition be used to maintain the CMGR's proposed 3-to-4 percent growth rate. (Milton Friedman. ***"****Essays in Positive Economics."* ***University of Chicago Press***, 1953.)

In Friedman's words, his proposed CMGR would eliminate ***"both the private creation and destruction of money, and the discretionary control of the quantity of money by the central bank authority."*** This would necessitate a 100 percent reserve requirement, where lending institutions would be required to retain one dollar in reserves for each dollar in the form of a commercial or personal loan. It would replace the Fed's current, *"fractional reserve"* system, in which each *"free"* dollar of reserves can be converted into as many as six or seven dollars in loans. This reform would allow the Fed to **instantly and precisely monitor the money supply** and its growth rate *in real time*.

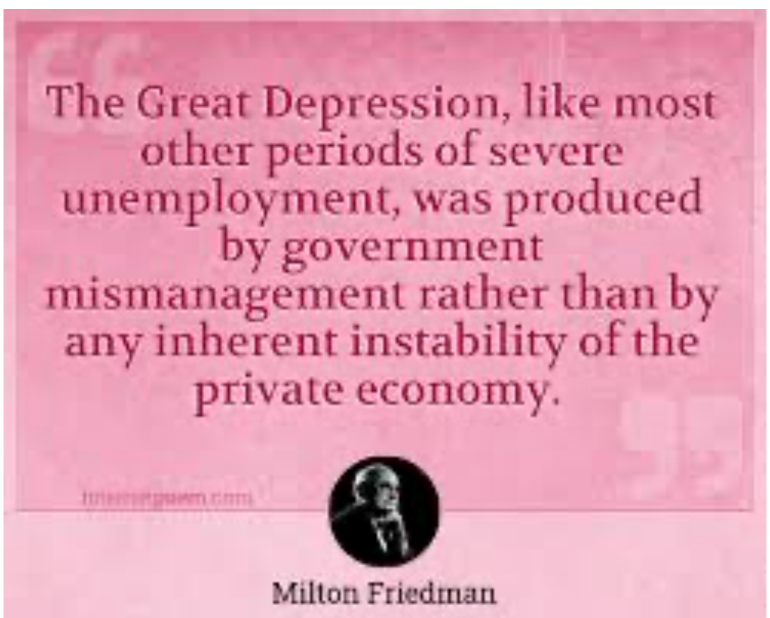


Diogenes' Honest Man: Nobel Laureate Milton Friedman

Interest rates are the *"price"* of borrowing money. If the economy were growing rapidly, then an increased demand for loans would trigger an

increase in interest rates charged to borrowers, serving as a natural brake against extreme cyclical fluctuations. If the economy were cooling, interest rates would decline as a result of less demand for loans. In either case, these signals would arise spontaneously from self-regulating market forces, rather than the arbitrary and capricious interventions of the Fed. This would permit interest rates to achieve what is often referred to as their *"natural level,"* created exclusively by supply and demand in credit markets.

The most egregious example of disastrous Fed intervention occurred when Herbert Hoover caused the *Great Depression*. Anticipating a recession following the Stock Market crash of 1929, in good faith he foolishly encouraged the *Fed* to reduce the money supply so as to avoid inflation on top of an impending recession. The result was a profound **monetary contraction of 33 percent**, and a depression that lasted a decade. Aside from war, monetary contractions may be the most destructive of economic events because they strangle economic activity, and force buyers and sellers to abandon markets and resort to bartering. Hoover's influence on the Fed had disastrous and lasting consequences.



In contrast to the goal of the CMGR, for much of the post-Depression era the Fed has exercised a great deal of **discretion** in creating money. Often, this has been done to minimize the painful consequences of declines in the business cycle, or external *"supply-shocks"* such as the *Arab Oil Embargo* of 1973. It has most often done this prior to national elections to artificially stimulate the economy in order to benefit a preferred political party. These attempts to *fine-tune* or manipulate the economy have helped to generate progressively severe bouts of inflation, recession, massive trade deficits, and a National Debt of $37 Trillion.

The benefits from a CMGR would be greater economic stability in business cycles, and increased certainty and predictability in the private sector. It would also act as an anchor to discourage the growth of the federal government and its voracious appetite. Under a CMGR, monetary policy could never really be contractionary, which was what precipitated the Great Depression. And, at the same time, the Fed would no longer have the discretion to indiscriminately print new money out of thin air, generating inflation and adding to our crushing National Debt.

As the French Mathematician Henri` Poincare` once facetiously quipped, ***"Money is too important to be left to the central bankers."*** The CMGR is a system that would remove this critical function from politicians and *dilettantes* like current Fed Chairman Jerome Powell.