Central Bank Easing Misses the Point

He made it clear that "nothing has been solved in Europe. The Europeans are not yet helping themselves. Why should the ECB (the European Central Bank) write a trillion-dollar check to near-bankrupt governments?" The real problem isn't liquidity. There's plenty of money sloshing around in the banks of the world. The instant problem is the type of money. The banks want to hold dollars, not euros, and the costs of holding dollars was rising to levels not seen since the collapse of Lehman Brothers in 2008.

And the reason dollars were getting increasingly expensive? One main reason was that American money market funds were pulling their dollars out of European banks: Between May and October those funds reduced their holdings in European banks by 42 percent, while their holdings in French banks were cut by two-thirds.

When demands were made on those banks for dollars, the banks had to sell euros to get them. As Capital Economics explained:

> Until Wednesday, banks were willing to loan euros in exchange for dollars for three months and receive an interest rate of Libor [London Interbank Offered Rate] less 150 basis points on the euro, versus paying an interest rate of Libor flat on the dollars. That spread shrunk following the central bank's latest pledge but remained around 130 basis points — far higher than the old rate which banks were prepared to lend dollars.

So the central banks' intervention reduced, for the time being, the cost to banks of converting their euros (which lenders were shunning) into dollars (which they preferred). But as Capital Economics noted: "We do not think [the move] signals a turning point in the crisis.... Even if the banks in the Eurozone [now] have less of a liquidity problem on their hands…they have a greater solvency problem."

And that is what the markets and many commentators conveniently overlooked when trying to explain why equity markets jumped 4 to 5 percent on the news. Witness this from the announcement from the Fed:

> The purpose of these actions is to ease strains in financial markets and thereby mitigate the effects of such strains on the supply of credit to households and businesses and to help foster economic activity.

With all due respect, it was not. The purpose was to relieve strains on banks that had loaned too much money to insolvent governments and investors were taking their money out before the banks failed. It was the start of a run on the banks for dollars and that's why the cost to borrow them rose so much. It had nothing to do with "households and business and to help foster economic activity." If loaning money to deadbeat governments who took advantage of low interest rate loans to build unneeded and unnecessary "infrastructure" projects actually stimulated their economies, where was the proof? The real world is, albeit slowly, discovering that these governments have overspent to such an extent that they can't even pay the interest on those loans, much less any principal.

Italy is the largest but certainly not the only case in point. It just happens to be the one most likely to set off the chain reaction of defaults that eventually will reach all the way to France and yes, even to Germany.

Occasionally, a few commentators noted the real problem but then propose the wrong solution. Masaaki Shirakawa, a governor of Japan's central bank — guilty on all counts of trying to stimulate a dormant Japanese economy for two decades without success — said: "The European sovereign debt problem will not be solved only with liquidity." Correct. But he added that he "strongly expected [the European Union] to push through economic and fiscal reform" to solve it. Wrong. What is needed is less "fiscal reform" and more economic freedom. And the best way to get that, according to economist Gary North, is through more austerity — *government* austerity.

The lack of any restraint on government spending and the continued protection of banks that get in trouble lending to insolvent governments will only result in default. It's already happening as entitlement programs are having their promises modified through higher "premiums" and "contributions" along with the raising of retirement ages. These are properly called defaults, on the installment plan. However, from the interventionists' view, an outright default by governments like Italy must be prevented at all costs, or else the game, the sham, the fraud of the European Union, will be exposed.

All this recent move by central banks did was buy time. Somehow, it is thought, time will eventually come up with a cure for the problem. Mohamed El-Erian, the co-CIO of PIMCO, which is the world's largest bond fund management company, and a reliable spokesman for the central banking cartel, was clear about what this move was all about:

> The hope is that central banks are acting because … they feel confident that other policymakers [in the euro zone] will finally catch up with a big and spreading debt crisis.

Nick Kounis, head of research for ABN Amro, almost got it right: "This is not a game changer for the debt crisis. It's relieving some strains but it's not meant to tackle the actual sources of these problems."

Of course not. The macro-picture is the hope that the leaking, creaking, weakening system of paper money will stay together just long enough for the "policymakers" to stitch together a sovereignty-ending regional superstate with a single government supporting a single currency by a single central bank.