*Let's Schmooze*

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# All That Money

The puzzling question that Greenspan says even he can't answer ~ why don't long-term interest rates follow the short term rates? Greenspan finds it so frustrating. He keeps hiking the short-term rates a ¼% at a time, but the long-term rates stay in the basement. It's as if the Feds have lost control.

Why?

Credit, liquidity, and disenchantment. Let's take a closer look.

Historically, the Federal Reserve Bank obtained its power from two sources. One, printing money ~ actual dollar bills. Two, controlling the rate of interest banks charge each other, i.e., the short-term rates.

This worked well for a long time, but recently the credit industry has robbed the Feds of their 1st source of power, controlling the nation's money supply by controlling the printing of actual dollar bills.

Money is electronic now. We really don't need actual dollar bills to transact business. Electronic transfers do the job very nicely. This has permitted banks to "make" money themselves.

Think about it.

Whenever a bank extends a line of credit to someone, "money" is created, without the actual printing of a dollar bill. Ergo, control of the money supply has increasingly passed from the Feds to the financial markets. And, everyone is busy extending credit to everyone else, and in so doing, increasing the "money" supply. There's lots of it out there now. How many offers of credit did you get in your mailbox today?

That's liquidity. Awesome liquidity. We are literally afloat in a sea of money ~ electronic money. Very spendable. Don't need the Feds printing the green stuff anymore. Just whip out that plastic.

So, why are long-term interest rates so much lower than short-term rates? Why is so much money being placed in long-term investments that pay so little? Doesn't make sense, does it?

The answer, unfortunately, lies in the public's obvious lack of faith in the future of our economy. It's simple. If we really believed that the future is going to be better, we would put our nest eggs in the high short-term investments, expecting that by the time we bailed out of the short-terms, the long-terms would have passed them up.

However, if, on the other hand, we really believe that the economy is going to soften, and interest rates plummet further, we would put our nest eggs in current long-term investments, wanting to tie into those rates before they went even lower.

Guess what everyone is doing? Long-term investments!

And now the Chinese are beginning to take very long-term bites at our corporate apples.

Another time . . . those Chinese

~ 'til we meet again ~