Fed Pumping Billions Per Day as 'Plunge Protection' for Markets

by William Engdahl

Over the week Nov. 6-13, the high-tech Nasdaq stock index in the United States lost a full 17% of its value, while Asian, South American, and some European markets suffered even greater drops. In paper terms, more than $1.7 trillion in share values had evaporated since the all-time Nasdaq high of 5,123 was reached in March 2000. In real terms, the fall represents a disappearance in personal wealth of the investors in that market, which is almost equal, for example, to the total Gross Domestic Product of Germany: some 3.7 trillion deutschemarks.

Many American families in the past several years had shunned traditional secure forms of saving, in favor of the stock market, and much of that into the high-flying Nasdaq stocks. As the savings ratio of American families fell, month after month, since 1997, economists waved off this result, claiming that households were simply "saving in a new way," putting their income into the stock markets.

The Federal Reserve and academic economists developed a term for this stock investment rush by some 60% of all American households. It is called the "wealth effect." The idea is that families which see a yearly statement from their mutual fund or stock manager showing paper gains of 25-30%, as had been the case in the last year or two, would "feel" wealthier and risk going into credit card or other debt to buy a new house, a car, or other consumer goods. This so-called "wealth effect," or consumer spending binge, backed up by the illusion of stock market wealth, was said to be the main prop to fuel robust U.S. GDP increases of 4-5% per year since 1995.

The Plunge Protection Team

Little wonder then, that just on that day, Nov. 13, when the U.S. election uncertainty threatened a dollar crisis, on top of a meltdown of the stock markets, the Federal Reserve and its aptly named "Plunge Protection Team" stepped in—for at least the fourth time in two months—to save the day. The Fed intervened discreetly with an injection of liquid funds, cash, into the banking system, in the form of $3.01 billion in 28-day repurchase agreements, or repos. Then, some minutes later, it again injected $2.71 billion in overnight funds into the banks. That sudden, nearly $6 billion injection of liquidity by the Fed, was enough to stop a full-scale Nasdaq meltdown, but not enough to push it above the psychologically important 3,000 level.

Planning such inflationary, printing-press interventions is the task of the so-called Plunge Protection Team, consisting of a small group which, in addition to Federal Reserve Chairman Alan Greenspan, and Treasury Secretary Lawrence Summers, includes select Wall Street stock brokerages such as Goldman Sachs, or trusted banks such as J.P. Morgan or Citigroup, where former Treasury Secretary Robert Rubin is vice chairman.

So, with no resolution of the U.S. election crisis, and an economy severely weakening, the Plunge Protection Team went into full gear on Nov. 14. First the Fed injected another $2 billion early in the day. Then, minutes later, as if in response to a cue, Goldman Sachs' market prophetess, Abby Joseph Cohen, was brought out to tell the world press that the stock market was undervalued, and should rise by "at least 15% by year-end."

Since the October 1987 stock market crash, Cohen has been used to "predict" a rebound every time the markets are threatened with meltdown. Wall Street insiders know that when she predicts a rally, Goldman Sachs and other major players have been told to buy that day, so a rush of speculative buying usually ensues. In addition, the process is leveraged via derivatives, or stock futures contracts on the Nasdaq or Dow Jones Industrials index. In the short term, relatively small amounts placed into derivatives can help push the entire stock market sharply higher, adding credibility to this "suckers' game." On Nov. 14, it was no different, and within minutes of the combined Fed and Goldman Sachs intervention, the Nasdaq was soaring, ending the day well above 3,100 for a rise of 5.7% on the day.

According to market sources, had the Fed and the Plunge Protection Team not stepped in, today we would be in a full-blown systemic financial crisis which would soon spill over into a dollar collapse, threatening the fabric of the global system, as Lyndon LaRouche repeatedly has warned. The problem is that such intervention by the Fed only holds the dam for a matter of a few days or hours in the present hyper-fragile situation. Soon, a stock market loss equal to the U.S. GDP of some $9 trillion will be on the horizon. At that point, no plunge protection will be possible, because the panic will simply be too great.