# Stockmarket crashes are prohibited

Retrieved Wednesday 26th of April 2017 05:19:13 PM

The world's stockmarkets reached an all-time high yesterday. Based on the MSCI All Country World Index, we're above 2007's peak.

Whoop-dee-doo!

It's a bit embarrassing to have only just surpassed the peak from ten years ago. Stockmarkets are supposed to go up in the long run. But how long are you willing to wait for the long run? And if you're a retiree, how many shares have you had to sell at low prices to fund your retirement in the meantime? Not to mention the amount of inflation that's happened.

To get to an all-time high, governments and central banks have had to pump vast amounts of money into financial markets. I wonder if it would've been cheaper to just give that money to the retirees who are using the stockmarket as a retirement plan. (Which is just about everyone because the government pretty much mandates it these days.)

In the first months of 2017, central banks pumped around a trillion US dollars into markets. Imagine what that money could've been used for instead…

Of course, handing out cash to retirees is politically incorrect. Handing cash to financial markets, which then pass some of it on to retirees, is acceptable though.

It's not much help pontificating about alternative realities. You're probably heavily invested into the stockmarket. And governments aren't likely to hand over freshly printed cash to you any time soon. So what's in store for stockmarkets?

Yesterday we looked into how central banks of the world have stopped influencing financial markets and are now downright controlling them. An infinite amount of money can be used to buy any financial asset these days. That used to be an absurd idea. But in the name of rescuing the financial sector, the absurd is allowed.

This begs the question I've been exploring in *Capital %26 Conflict* for some time: are stockmarkets allowed to crash? We have to break it down to answer that question.

**The power of the powers that be**

Central banks have a near infinite budget to buy financial assets. Governments have a near infinite power to suspend market rules, such as the accounting rules they suspended during the financial crisis in order to let investment banks feign solvency.

If governments and central banks consider it desirable to goose the stockmarket, they can do so in the face of just about any obstacle that I can think of.

They can rescue banks, even doing so in secret. Australian banks got help from the US Federal Reserve without anyone realising in 2008. One central bank rescue programme was named after the back-alley entrance into the Federal Reserve because of the unseemly nature of it. In other words, anything goes.

What's happened here is easy to grasp. Governments figured out it'd be rather hard to finance retirements using welfare. The demographic changes are simply too big. Financial markets seemed like a safe bet for governments to pawn off their responsibilities to. After all, the long-term return of stockmarkets is around 7%. (For that to be true, the FTSE 100 would have to be at unimaginable soaring heights today.)

But, as with any government effort, once the markets became politicised they stopped working the way they had. Suddenly stockmarkets were being ploughed with funding from the general population with each paycheque automatically. The numbers of people there to be ripped off grew so fast financial sectors couldn't keep up with more and more harebrained schemes. Even homes became financialised.

But financial markets crash periodically. And when you tie your national retirement policy to something that crashes, you get a nightmare scenario.

The cart is now before the horse. Politics and retirement planning rule the stockmarket instead of just investing in it. This means stockmarket crashes are now prohibited. They've become too important.

**Are there any limits to goosing the market?**

There's only one limit to how far central bankers can go. Central bankers are still accountable to governments in the end. And governments are still politically accountable to voters. If the guardians of the stockmarket are out of favour, voters can choose someone else.

If, for example, central bankers create so much money and buy so many assets that serious inflation breaks out, politics is likely to turn to the issue. It'd be a similar story to Thatcher, Reagan and Friedman all over again.

If a crash starts, voters will demand more action from central bankers and governments.

But central bankers and government economists believe they can tightrope walk between the two possibilities. There won't be a crash and there won't be inflation.

I've taught people to tightrope walk. You fall off eventually.

But the bias is clearly in favour of inflation breaking out. Who would vote for a stockmarket crash?

So if stockmarket crashes are prohibited, why not pump money into stocks? Some say now's the time. But it's never that simple. The "stockmarket crashes are prohibited" thesis has worked since 2009. It's been a long eight years.

More importantly, whenever everyone agrees stocks can only go up, it's time to worry. Bets on a falling US stockmarket are at a ten-year low. It's time to worry.

Just because central bankers can rescue the stockmarket, doesn't mean they will straight away. Most of them are embarrassed about how much of their nation's investments they already own. What's the point of a financial market that the central bank dominates?

So here's the conclusion if you agree with these musings: stay invested in the stockmarket; watch for inflation; and look closely at politics, not just economics. At any sign of a crash, the central bankers will be all that matter.

Until next time,

Nick Hubble
*Capital %26 Conflict*