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Solutions for a New Economy

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QE1, QE2, QE3, QE….

"Unconventional and Last Resort" is becoming commonplace when thinking about Quantitative Easing. One of the functions of the Federal Reserve, the Fed, is to manage the monetary policy of the United States. As such, the Fed manages its policy by influencing the monetary and credit conditions in the economy. The Fed's stated goal is to maximize employment, keep prices stable, and moderate long-term interest rates. Quantitative Easing is usually used as a last resort by central banks to stimulate the economy. As Quantitative Easing becomes more of a commonplace practice, some thought should be given to its effectiveness.

To backup a little, when the economy is faltering, the Fed pursues an expansionary policy by lowering short-term interest rates. As short-term rates approach 0%, Quantitative Easing is another option that the Fed can employ. With Quantitative Easing, the Fed buys financial assets from banks with newly created money. This process has the effect of lowering longer-term interest rates. However, the main goal of QE is to increase the money supply in the economy.

Quantitative Easing is used to stimulate the economy and not to finance government spending. The goal is to encourage banks to lend to businesses and encourage consumption on the part of consumers. In order to provide some perspective on what the Fed has done over the past several years, we need to look at the amount of financial assets on the books of the Fed. The Fed held approximately $700 billion of Treasury Notes before this recessionary period and now holds $2.3 trillion in financial assets.

QE1 was announced in November 2008 and was originally slated to purchase $500 billion in mortgage securities. It was increase to $1.25 trillion in March 2009 and ended in March 2010. QE2 started in November 2010 and focused on purchasing $600 billion in Treasuries. QE2 ended in June of 2011.

The risks of a depression were a real possibility in the last recession, so we could say that QE1 and QE2 did the job. However, Quantitative Easing is a last resort because of the hangover effects.

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This Issue's Trivia Question

Q: What is the oldest Central Bank in existence today?

A: The Riksbank of Sweden, which has been in existence sense 1668.

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Quantitative Easing may cause inflation unless the economy outgrows the increased money supply in a reasonable period of time. This seems to be a big risk on the minds of many investment professionals. With Quantitative Easing, there is no guarantee that banks will lend their increased money pool out to businesses or individuals. Banks may even bypass the US economy and lend to foreign countries as an alternative.

Another unintended consequence is that investors and pensioners earn less on their bond portfolios. This could be considered one of the largest "non-tax" taxes ever paid by investors. Also, we have seen how the US dollar has devalued versus foreign currencies, which is another effect of QE.

To sum it up, too much of anything is not good. What do you think - do we need another round of Quantitative Easing? A QE3 still might be on the horizon.

Absens Haeres Non Erit

Are you engaged in your financial future? Absens haeres non erit is Latin and translates into: an absent person will not be an heir. If you are absent from involvement in your financial future, you might not be an heir to a successful retirement.

SunTrust recently published an article on how to beat the percentages in their Retire Solid publications. They compiled many interesting facts and we have selected several to quote.

A reported 70% of workers say they are behind in planning for retirement. (EBRI)

About 40% of Americans do not track spending against a budget. (Bankrate.com)

Only 42% of workers have completed a retirement needs calculation. (Retirement Confidence Survey)

Nearly 50% of investors rarely or never rebalance their retirement accounts. (FINRA)

An estimated 55% of adults do not have wills or other estate plans in place. (Harris Interactive)

About 41% of adults have no life insurance. (LIMRA)

Is it time to develop a successful personal financial picture?

About 47% of employers check credit reports for select job applicants. (Society for Human Resource Management)

About 35% of parents with dependent children were not saving for college.

These percentages might be a call to action in an area of your financial picture. With a small amount of diligence, it is possible to be an heir to a solid financial future.

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