Federal Financial Analytics, Inc.

MEMORANDUM

TO: Federal Financial Analytics Clients

FROM: Karen Petrou

DATE: February 5, 2021

At the outset of the French Revolution, the Duchess of Devonshire rode into Paris with her aristocratic pals for a glamor-filled shopping spree. Initially flummoxed by all the people on the streets, the party continued until, turning into one of the boulevards, the fury of the mob came fully upon them. So it often is – many of us living in the "good place" the Fed called the U.S. economy were stunned when the mob turned upon the stock market last week. Indeed, at the very same time, FRB Chairman Powell said he thought financial stability-risks were back to a comfortable, "moderate" range. But, Ray Dalio and others who astutely follow the money – not their own models – forecast exactly this type of what I'll call anarchic capitalism. To be sure, GameStop isn't the Bastille – instead, it's like one of the small insurrections ahead of 1789. With ultra-low rates and free trading urging on the mob, far bigger bastions may tumble.

Some high-risk targets immediately come to mind. What, for example, becomes of a big bank the next time there's an easy-to-understand consumer-protection scandal? These on their own cost companies dearly in terms of market capitalization, but not as dearly as might come to pass if day traders are hell-bent on vengeance.

It's not hard also to envision a group of anarchic capitalists targeting a sector that, like Big Oil, is feeling some pain and engaging in business activities that draw significant amounts of public ire. Why wait for strict climate-change rules if you and your allies can drive a firm's stock price down so far that it implodes? Even if your "trading rave" can't push a solvent firm into bankruptcy, you can certainly make its life more than miserable. With GameStop, the goal was to drive up the stock price in part to punish hedge funds, but it could just as easily have been to drive down the price of a stock to punish a company and its investors and, along the way, still make more than a buck or two.

Congress, Treasury, and the SEC are of course now well aware of the power of anarchic capitalists and are looking feverishly for ways to restrain them. A raft of remedies ranging from the regulatory changes we outlined last week to a financial transaction tax are on the table. Some of these would control aspects of anarchic capitalism and enhance market stability along the way. None, though, will quell anarchic capitalism because ending order-flow payments, increasing hedge-fund transparency, or achieving faster trading speeds can't solve the real problem.

Anarchic capitalism isn't a mob that can be quashed by rules any more than Capitol Hill's insurrectionists were deterred when the cops told them to go home. This is not just about making money; it's about striking back after a decade in which Fed policy made the stock market the only

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way anyone in the U.S. could get ahead. As we showed earlier this week, making a living is no way to ensure a living return – only investing in the market can do that now that savings rates are infinitesimal and the Fed has spread a safety net beneath the stock market.

Anarchists of the early 20th century made a mess, but they had a point. Industrial capitalism then spawned both a Gilded Age and profound economic injustice. Anarchic capitalists of our own era made a mess of the market, but they too have a point. Our financialized economy has spawned another Golden Age with economic inequality unrivalled since the Roaring 20's. Stock-market rules may make equity markets a bit more orderly, but only the Fed can make the financial system more equitable.