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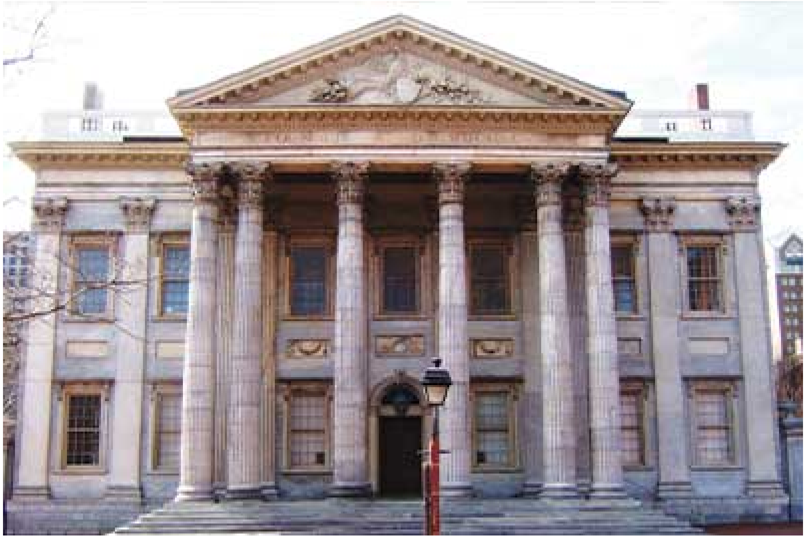
The Federal Reserve Protection Racket

Most Americans have little or no idea what “the Fed” is or does, despite the fact that, ever since its creation in 1913, it has had monopolistic control over the money supply in the country and regulated virtually every type of financial transaction. When Tucker Carlson interviewed former Congressman Ron Paul on his podcast, he recalled how, when Paul was running for the Republican Party nomination and was giving a speech at Michigan State University, hundreds of students began spontaneously chanting “End the Fed!” Carlson said he was taken aback by this since he, as a professional journalist, was paid to know at least something about the Fed but did not. The Michigan State University students obviously did — they had been reading and listening to Paul’s speeches.

The pervasive lack of awareness of the Fed’s activities, as with so much else the government does, is what economists call “rational ignorance.” When it comes to educating ourselves, we spend most of our time and effort on our own education, jobs, family matters, paying the bills — our private lives. We spend very little time and effort learning about what the hundreds of government agencies of all types are doing. This is why the late Rush Limbaugh referred to most Americans as “low-information voters.”

Politicians have always understood this, which is why so many of them are habitual liars and deceivers. Indeed, when Alexander Hamilton made his case for creating a national bank run by politicians in his 1790 *Report on a National Bank*, his political nemesis, Thomas Jefferson, responded by saying that it was intentionally confusing, a subterfuge designed to fool the public into acquiescing to a vast, unconstitutional expansion of governmental powers. Jefferson was right on the money, as usual.



Forerunner: The First Bank of the United States, set up at the urging of Alexander Hamilton, was America's first central bank — although, unlike the modern Federal Reserve, it did not have the power to print money or the authority to purchase government bonds. But it did set the precedent that the federal government should have its finger on the scale of finance by being involved in the banking business. (Public Domain)

Jefferson pointed out that the Constitutional Convention had discussed — and rejected — Hamilton's proposal for a national bank, and that no such thing was included in the delegated powers (assigned by the states to the federal government) in Article I, Section 8 of the Constitution. In what may be the very first significant snub of the constitutional limits on government, George Washington signed legislation creating the first central bank, the Bank of the United States (BUS), in 1791. The BUS was 80-percent privately owned, with the government owning the other 20 percent. It was the first great monopolistic collusion scheme between business and government in America. The BUS promptly did what Jefferson and the Jeffersonians feared: It inflated the currency, causing 72-percent price inflation from 1791 to 1796, and continued to do so for the next 15 years. Consequently, its 20-year charter was not renewed by Congress.

The War of 1812 was used as an excuse to revive the BUS in 1816 as a means of helping to pay for the war debt, and the BUS quickly became known for its "mismanagement, speculation, and fraud," wrote James J. Kilpatrick in *The Sovereign States*. Its monetary expansion created bubbles in the economy, and when they burst — as economic bubbles inevitably do — the result was the first great depression in America, known as the "Panic of 1819." The revived BUS also extended cheap credit to politically favored borrowers, causing great corruption — so much so that President Andrew Jackson claimed that it "impaired the morals of our people, corrupted our statesmen, and threatened our liberty. It bought up members of Congress by the Dozen … subverted the electoral process, and sought to destroy republican institutions." This last claim by Jackson referred to how the BUS had subsidized the campaigns of its favored political candidates.

President Jackson famously vetoed the renewal charter of the Second BUS in 1832, and it eventually went out of business and into the dustbin of history. In his veto message to Congress, Jackson said that the BUS was an example of how "the rich and powerful too often bend the acts of government to their selfish purposes." Such institutions "make the rich richer and the potent more powerful.… The humble members of society … who have neither the time nor the means of securing like favors to themselves, have a right to complain of the injustice of their government."

It would take another eight decades or so before the banking industry's cabal of corruption could get the government to create another central bank that would benefit the cabal at the expense of the rest of the population. That was the Federal Reserve System, or simply "the Fed."

Inherent Corruption

To understand the essential nature of the Fed and central banking in America, it will be helpful to examine it in light of the government/business relationship, often referred to as "crony capitalism." As the name suggests, crony capitalism is not real, free-market capitalism, but a system whereby government coercion is employed to benefit not the public in general, but politically connected businesses — usually *against* the public's interests — by creating some type of monopoly and, subsequently, higher prices.

From the beginning of the Republic to the Civil War, the great economic debates in American politics were mostly about whether or not the United States should adopt elements of the British "mercantilist" system that the American Revolution was fought to secede from. This *British* system was given the name "The American System" by Alexander Hamilton. It was later championed by Henry Clay, and then by Abraham Lincoln, who considered Clay to be his political role model or, as he once put it, his "beau ideal of a statesman."

The system involved what we today call tax-funded corporate welfare for politically connected businesses, tariffs to protect mostly Northern state manufacturers from foreign competition (and to "protect" consumers from lower prices), and a national bank — controlled by politicians even if it was partly privately owned. This was really the Hamiltonian/British system, not an American system, that was championed by Hamilton and his political descendants and opposed by Jefferson and the Jeffersonians for roughly the first 75 years of the American Republic. By the eve of the Civil War, almost none of it had been adopted, as the Jeffersonians had more or less prevailed. Things, however, were about to change.

With the Republican Party holding monopolistic control of the federal government during the war and for decades thereafter, all of the Hamiltonian system was put into place. The average tariff rate went from 15 percent to more than 50 percent, and remained there until the federal income tax was adopted in 1913. The floodgates of corporate welfare were opened with massive subsidies to railroad corporations to build transcontinental railroads. There was no central bank, but the Legal Tender Act of 1862 created the "greenback" dollar and taxed competing currencies out of existence. The National Currency Acts of 1863 and 1864 created a regime, if not an actual central bank, that had regulatory powers over banking. These regulatory powers were steppingstones to a central bank, albeit not the real thing.

The subsidies to the railroad corporations championed by the old general counsel of the Illinois Central Railroad, President Lincoln, led to massive mismanagement and corruption, as the Jeffersonians had always warned would happen. The fraud — known as the Crédit Mobilier scandal — was exposed during the administration of Ulysses Grant. The waste and corruption were so colossal that the politicians and corporations responsible for it learned a lesson: They must find more subversive ways for government to use its powers to create monopolistic profits for its political supporters and campaign financiers than simply writing them checks. So they turned to government regulation as the means of creating monopolies and monopoly profits (presumably in return for veiled kickbacks of all types, including campaign “contributions”).

They could not, of course, tell the public the truth — that their real objective was to disguise corporate welfare to their political benefactors. They needed to bamboozle the people with talk of how government regulation would supposedly be enforced to serve “the public interest.” This was pure Hamiltonianism, for Hamilton himself used “public interest,” “national interest,” and other such rhetoric to describe his quintessentially *special*-interest politics, such as corporate welfare and protectionist tariffs. Such policies would drive up the prices of certain products while enriching politically connected corporations at the expense of their hapless customers forced to pay higher prices for the same or shoddier products.

The very first federal regulatory agency was the Interstate Commerce Commission (ICC), created in 1887 — 26 years before the founding of the Fed. There was a railroad-building boom after the Civil War, and competition among railroad corporations was fierce, causing passenger rates to plummet year after year. The corporations complained bitterly of “cutthroat competition” and attempted to create price-fixing cartels, but they invariably failed because of cheating with secret rebates by members of the cartels, proving once again the old adage that there’s no honor among thieves.

Giving up on attempts at collusion to fix prices, the railroad corporations endorsed government regulation of their own businesses, obviously confident that they, not the vaunted public, would benefit most from the regulation. They were certainly right about that. The first commissioner of the ICC was one Thomas Cooley, a lawyer/lobbyist who, like Lincoln himself, had represented railroad corporations for many years. He lobbied Congress to give the ICC even more regulatory powers. One of the first things he did with those powers was to address the “problem” of long-haul rates being lower than short-haul rates, a sort of quantity discount offered by some railroads. Cooley’s “solution” to this non-problem was to outlaw the lower rates! That was always the policy of the ICC with regard to railroads: Always keep rates higher, never lower. Price fixing did not work when it depended on voluntary agreements among price-fixing conspirators, but it did work when the coercive powers of government could be employed to *make* it work.

When trucks began competing with railroads, trucking-industry lobbyists came to dominate the ICC and created a government-enforced price-fixing scheme for themselves as well. The ICC restricted the number of truckers who could be licensed, reducing the supply and thereby increasing the price of trucking; granted monopoly routes to certain trucking companies; and forced long-haul truckers to return from a trip empty, reducing the supply of trucking services even further and making trucking even more expensive.

The airline industry followed suit in the 1930s with the Civil Aeronautics Board (CAB), which severely restricted competition, directed routes, prohibited price cutting, and essentially made air travel too expensive for working-class Americans until the airline industry was deregulated and the CAB abolished in the late 1970s/early 1980s.

In the late 19th and early 20th centuries, there was vigorous competition in all the public-utility industries, including electric lights, telephone, water supply, natural gas, and others. As with the railroads, there were many attempts at private price fixing, but they all failed. Also as with the railroads, the public-utility industries then turned to government to enforce their monopolistic pricing practices. The technique was to have state or local governments decree that one company should be the monopoly supplier of utility services, and then share the monopolistic loot with state or local governments. One of the very first instances of this was in Maryland, where, in 1890, the Baltimore Gas Light Company contracted to pay the city of Baltimore $10,000 annually and three percent of all dividends declared in return for a government grant of monopoly, as described in *The Gas Light Company of Baltimore* by George T. Brown. City after city followed suit, all the while blaming the monopolies that *they created* on free-market competition by labeling them "natural monopolies." Many other industries, including banking, jumped on the "natural monopoly" bandwagon and lobbied for government-mandated monopolies for themselves.

Hence, the political atmosphere of "progressivism" in which the Fed was founded in 1913 was one of myriad crooked conspiracies whereby businesses and governments colluded and conspired to create government-mandated monopolistic privileges for various businesses and industries. The industries then shared the monopolistic loot with the governments that had granted them their monopoly status and, of course, financially supported the politicians responsible for the whole scam in the first place.

Today there is much talk of the "capture theory of regulation," made famous decades ago by University of Chicago economists and highlighted in Robert F. Kennedy, Jr.'s book *The Real Anthony Fauci*, which discusses how the pharmaceutical corporations have "captured" the public health bureaucracies in Washington, D.C., and elsewhere, especially the Food and Drug Administration and the Centers for Disease Control and Prevention. Historically speaking, however, these bureaucracies were seldom "captured." Their very creation was often lobbied for in the first place by big businesses in various industries, so that there was nothing to "capture." Hiding behind the rhetoric of the "public interest," the regulatory bureaucracies were always intended to serve *special* interests, not the undefinable "public interest." This is true of the Federal Reserve System as much as or more than any industry.

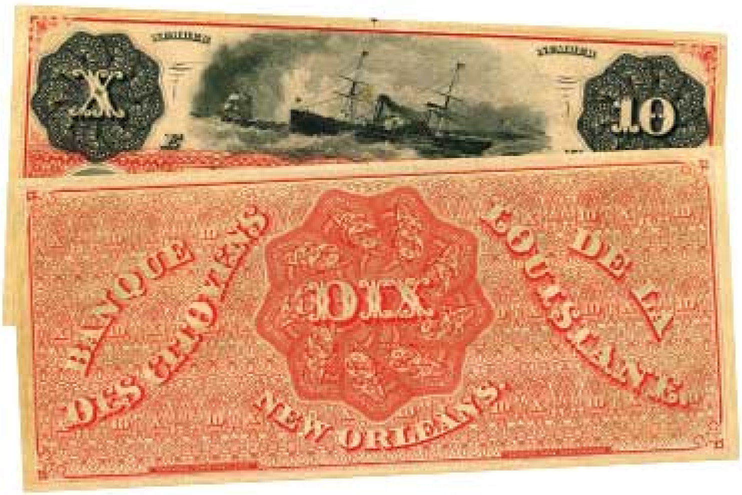
Not-so-immaculate Conception

In a free market, banks make money by charging a higher interest rate for the money they lend than the rate they pay on bank deposits. However, banks have always been tempted to lend far more money than they hold in deposits, or reserves — hence the term "fractional reserve banking."

In the first half of the 19th century, when there were still competing currencies issued by various banks, banks with higher levels of reserves (often in the form of gold and silver) were seen as more trustworthy, and therefore their currencies were more widely used. Banks that lent, say, a hundred times the amount of their reserves experienced the opposite, and often went bankrupt. This is easy to understand: If for some reason such a bank's customers started demanding their deposits back, that bank would quickly run out of money and go out of business. Competition "regulated" the banking system in the same way that it does all industries.

It was Lincoln who ended competition in banking by creating the "greenback" dollar as the monopoly currency while taxing the other currencies out of the market.

Dixie dough: The ten-dollar note, or "dix" (French for "ten"), issued by the Citizens' Bank of Louisiana was considered very sound, and its popularity across the South was the origin of the word "Dixie." (Photo: Public Domain)



For example, in the first part of the 19th century, farmers and merchants from "up river" on the Mississippi would sell their wares and agricultural products in New Orleans and be paid in a currency issued by the Citizens' Bank of Louisiana that was called the "dix," which is French for "ten." They would return home boasting of having a "pocket full of Dixies," and that is how the South became known as "The Land of Dixie." The dix was issued by a bank with a very high percentage of reserves, and was therefore so reliable that it was routinely used in Minnesota and all over the Midwest. It could be exchanged for gold or silver all over the country.

As with the railroads, the public utilities, and other industries during the latter part of the 19th century, corporate executives in the banking industry began to oppose competition. According to them, it was too risky to essentially engage in legalized counterfeiting by lending out hundreds of times the amount of money they had in reserve, risking bank runs and bankruptcy. They and their lobbyists complained bitterly for decades that the money supply was too "inelastic" — meaning that competition among banks restricted their ability to profit from a legalized counterfeiting operation.

They employed a small army of academics and intellectuals to make the case for a banking system that would use the coercive powers of government to allow them to expand their loans far beyond what their reserves would allow for in a competitive system. They wanted what they called a "lender of last resort," a euphemism for government-funded bailouts of their counterfeiting scheme. In other words, they wanted a government-enforced cartel for the banking industry just like the ones in the railroads, public utilities, and other industries. Having failed to cartelize the banking industry privately, they wanted to do what these other industries had done and use the government to be their cartel enforcer. The Mafia-style enforcer (minus all the broken kneecaps) would be the Federal Reserve System.

Economist Murray Rothbard explained the purpose of the Fed in his *History of Money and Banking in the United States* as follows: "The financial elites of this country … were responsible for putting through the Federal Reserve System, as a governmentally created and sanctioned cartel device to enable the nation's banks to inflate the money supply in a coordinated fashion, without suffering quick retribution from depositors or noteholders demanding cash."

In addition, the banking industry recruited myriad academics, especially economists, to dream up theories about why monopoly is better than competition in the banking business. "To achieve the Leviathan state," Rothbard wrote, "interests seeking special privilege, and intellectuals offering scholarship and ideology, must work hand in hand." This is as true today as it was in 1913. Economist Larry White of George Mason University published an article in a peer-reviewed economics journal (*Economic Journal Watch*, August 2005) in which he reported that 74 percent of all academic journal articles published in the field of monetary economics were authored or co-authored by Fed employees or published in Fed journals. Pro-Fed bias is so pervasive that the late Milton Friedman once remarked that if one wanted an academic career as a monetary economist (like Friedman), then it would be a good idea to not criticize the major employer in the field.

Legalized Counterfeiting

The Fed started out by serving as a "lender of last resort" and essentially bailing out unsuccessful bankers. Then, in 1933, a law was passed allowing it to engage in the monetization of government debt by purchasing government bonds. Consequently, the Fed literally counterfeits currency, which it then uses to purchase government bonds. This is the major way it injects billions of dollars into the banking system, creating price inflation and seemingly never-ending boom-and-bust cycles. The big New York investment banks have always been the primary dealers in these government-bond purchases, and have become extraordinarily wealthy and politically influential by doing so. That is why the U.S. treasury secretary is almost always a former CEO of Goldman Sachs or one of the other big New York investment banks. (They were given that name decades ago because they dealt mostly with lending to corporations to create or expand their businesses.)

Rather than encouraging banks to hold on to reserves sufficient to avoid bankruptcy through "bank runs" of depositors demanding their deposits, the Fed allows virtually unlimited lending. It does this through its "reserve ratio," which is the percentage of a bank's reserves that it must hold and not lend out. While this "requirement" has been as high as 10 percent, as of January 2025, the Fed's required reserve requirement was 0.0 percent! The Fed website and sites such as Investopedia explain that the purpose of the reserve ratio is to assure the public that their banks have sufficient reserves so that they don't have to worry about not being able to get their cash on demand. That, of course, is just more pro-Fed propaganda in light of the current reserve "requirement."

The dollar has depreciated tremendously since the Fed's founding in 1913, despite the fact that the Fed is supposed to be an inflation fighter. A typical market basket of consumer goods that cost $108 in 1913 would cost $2,422 today, thanks to decades of Fed-generated price inflation. The highest rates of price inflation in America's history have occurred under the Fed's watch.

The Fed claims that one of its jobs is to "stabilize" the business cycle to avoid dramatic inflationary "booms" and unemployment-increasing "busts." But the academic research of University of California at Berkeley's Professor Christina Romer — President Barack Obama's chief economist — showed that the business cycle was *less stable* after the Fed was created than it was before.

Another key tool of the Fed in its ostensible quest to stabilize the U.S. economy is the manipulation of interest rates. There are essentially two ways to reduce interest rates: If people save more, the supply of loanable funds in the banking system will increase. According to the laws of supply and demand, this will cause a reduction in interest rates, inducing businesses to invest more because lower rates make investment projects or business expansions look more profitable. Or, the Fed can inject money into the banking system by simply counterfeiting it and purchasing government bonds from investment banks, or lowering the reserve ratio from 10 percent to 0.0 percent. In the former case, consumers increase their future purchasing power because they have saved more. In the latter case, they have not. This is what causes the bust — and all the unemployment, bankruptcies, and suffering that come with it. Businesses that have expanded or created new ventures eventually realize that the market for their goods or services is not as big as they thought, and many of them are unable to complete their investment projects.

The creation of boom-and-bust cycles is one thing the Fed has excelled at — along with massively depreciating the dollar — since its inception. The Fed was created in 1913. Its policies led to the Depression of 1920, in which the unemployment rate was higher than in the first year of the next decade's Great Depression, caused by the Fed's monetary inflation in the late 1920s. The Fed's reckless monetary expansions have caused seemingly endless economic crises, including those in 1953, 1957, 1960, 1969, 1973, 1980, 1981, 1990, 2001, 2008, and 2020.

It's not just bankers, Wall Street speculators, the real estate industry, and other related entities that profit from the Fed's inflation and boom-and-bust policies. The State and all of its bureaucratic appendages benefit from the Fed's legalized counterfeiting operation because the people are fooled into thinking they can get something for nothing, whether that "something" is subsidizing foreign wars that have nothing to do with defending America, an ever-expanding welfare state, free hotel rooms, welfare, smartphones, air transportation for illegal aliens, or anything else the government spends money on. As Adam Smith wrote in *The Wealth of Nations*, for example, if governments were constrained to finance their projects with taxes instead of printing money, there would be far fewer wars, and the wars that did exist would be of shorter duration. The same can be said of all other federal government programs. Without the Fed, the federal government would be far closer to focusing on its core constitutional functions instead of the anything-and-everything of today.

To save the American economy from national bankruptcy, the Fed must be abolished by repealing the Federal Reserve Act of 1913, thereby getting the nation's money supply out of the hands of politicians, bureaucrats, and their academic propagandists and special-interest benefactors. Private property, private enterprise, and competition in currency must be restored so that all of America can become a modern-day version of the Land of Dixie, with competitive currencies backed by more than the promises of lifetime-tenured politicians (as most members of Congress are, essentially) and self-serving federal bureaucrats and their academic court historians.