Regulators pay homage to Babylon's Whore in London

by Anthony K. Wikrent

The heads of the 103 largest banks in the world gathered in London at the beginning of June, for the annual meeting of the International Monetary Conference (IMC), and to celebrate the tercentenary of the "Old Lady of Threadneedle Street," as the Bank of England is known in the high circles of international banking and finance. The meeting was especially noteworthy for the gaggle of financial regulators from around the world, who, except for some very rare birds from continental Europe, came to prostrate themselves, and assure the bankers that the regulators had no desire to burden or hinder the bankers' derivatives markets with more regulation.

The tone was set by the chairman of the U.S. Federal Reserve, Alan Greenspan, who told the bankers on June 8 that the derivatives markets will have to be increasingly "self-regulated, largely because government regulators cannot do that job." The best line of defense against a bank collapsing because of losses in derivatives, Greenspan said, is that "individual institutions, in their self-interest, become extraordinarily knowledgeable about the counterparties with whom they are dealing."

Tommaso Padoa-Schioppa, a deputy director general of the Bank of Italy who also chairs the Basel Committee of the Bank for International Settlements, told the bankers that the BIS will recommend that banking regulators in various countries use the internal risk-management models developed by the derivatives dealers themselves, as the basis for regulating derivatives. Over the past year, the Basel Committee has been considering whether or not derivatives dealers should be forced to meet capital adequacy requirements. Now, apparently, rather than formulating one standard against which all financial institutions can be measured, the committee is basically telling the bankers that the bankers themselves can set the standards by which it is to be determined whether a bank dealing in derivatives is insolvent or not.

The problem, Padoa-Schioppa explained, is that "we central bankers are still lacking a reliable set of analytical propositions on which to draw in formulating our policy methods in a derivatives-influenced financial environment."

Thus, it is not surprising that the measures advocated in the BIS's annual report—issued just days after the bankers' revelry in London—downplayed the danger of derivatives, focusing instead on a need for "better monitoring." The BIS report asserted that "the ongoing debate about the potential risks posed by derivatives markets has accentuated the need to develop more appropriate measures for the exposures which derivatives actually entail," and concluded, "It would be a mistake to assume that policymaking would be made easier if financial instruments could be limited or capital movements controlled. Global markets are now so highly integrated that suppressing the symptoms of investor preferences in one market would simply lead to their manifestation elsewhere."

The British call the shots

The BIS annual report reflects the significant shift that has occurred under its new general manager, Andrew Crockett, who was a senior official of the Bank of England before moving to the BIS. The previous general manager, Alexandre Lamfalussy, had been quite outspoken about the growing danger of banks' off-balance-sheet derivatives risks. Lamfalussy's appointment to head the new transitional European Monetary Institute, the core of a future European Central Bank under the Maastricht Treaty, was probably engineered in order to silence a voice that no doubt was irritating the international bankers—especially in the City of London, where one-half of the world's $1 trillion a day of foreign exchange trading takes place. London, in fact, trades more dollars or deutschemarks than are traded in the United States or Germany.

The line taken by Greenspan, like the new direction of the BIS under Crockett, slavishly follows the dictates of Threadneedle Street's Old Lady herself. The London *Independent* had reported on May 16: "Washington is preparing to propose new regulations on the burgeoning trade in derivatives, perhaps as early as this week. This is in direct opposition to U.K. authorities, led by the Bank of England, which believe that existing regulatory structures can handle the industry. . . . [The Bank of England] does not want to launch any new structures to deal directly with the derivatives markets. . . . The Bank is skeptical of suggestions that derivatives should only be traded on recognized markets."

That Crockett had the fix in place at the BIS, was indicated by the lead editorial of London's *Financial Times* on May 19. "Anything other than a global approach to regulation will be less than fully effective," it read. "The thrust of supervision [over financial derivatives] should thus continue to be chiefly through the Basel-based Bank for International Settlements."

The next day, Canadian regulators obediently fell into line. "In the absence of evidence of a problem, I don't think it's time for someone to say the sky is falling," proclaimed Richard Gresser, senior policy analyst at Canada's federal Office of the Superintendent of Financial Institutions. "I do not have evidence that would indicate there is a trend developing toward increasing trading losses."

Later that week, Greenspan gave a preview of the propitiation he would offer in London, in testimony before the U.S. House Finance Subcommittee hearings on derivatives on May 26: "There is nothing involved in federal regulation per se which makes it superior to market regulation. . . . Today's markets and firms, especially those firms that deal in derivatives, are heavily regulated by private counterparties who for self-protection insist that dealers maintain adequate capital and liquidity."

But on the continent, the governments of France, Germany, Italy, Spain, and Belgium—shocked by the derivatives-related collapses of Feruzzi, Banesto, Metallgesellshchaft, Crédit Lyonnais, Balsam, and other large companies—were leaning toward the view that controls on derivatives should be tightened. In a speech before the Frankfurt Economic Editors' Club on May 21, Edgar Meister, a director of the German Bundesbank, said that derivatives were increasing the "systemic risks for the financial sector as a whole," and recommended that all derivatives deals be registered at the credit supervisory board, and that all deals involving more than DM 3 million be made subject to minimum reserve requirements.

The response from the nabobs of London can be fairly described as a shriek. "Any form of heavy-handed regulation, when applied to very fluid cross-border business, will make those doing the business say, 'If I can do the business elsewhere . . . then I will,' " warned Anthony Belchambers, executive director of the London-based Futures and Options Association, the day after Bunsdesbank director Meister's comments.

Rolf Willi, secretary general of the International Exchange Association (ACI), the international organization of 51 national foreign exchange clubs—which just happened to be gathering in London the same time as the IMC—told reporters on June 3, "We are concerned that one day we will be over-regulated." ACI President David Clark was even more emphatic: "The worst thing that could happen . . . is that someone comes along and regulates the derivatives market." And just in case anyone missed the point, Her Majesty's Minister for Trade and Industry, Michael Heseltine, observed, "In contrast to some other marketplaces, the regulatory system in the U.K. has allowed these new products to be developed. . . . We in the U.K. do not impose a mass of burdensome procedural regulations on markets."

To drive the point home, a song was specially composed and performed by a choral group for the IMC's festivities, which went as follows: "Glory be to the deutschemark, and to the yen, but mostly to the holy pound. As it was in the beginning, before all this talk of a single European currency, is now, and ever shall be, Amen."

The collapse has begun

The bankers will soon have their comeuppance, however. Speaking at a conference of the Inter-Action Council in Dresden on June 7, former West German Chancellor Helmut Schmidt warned of an imminent major financial crisis, most likely "triggered by a collapse in the offshore banks," creating a danger in 1994-95 similar to the danger created by the collapse of the Vienna Kreditanstalt Bank in 1929, which initiated an international banking panic that opened the way to World War II.

Actually the collapse has already begun, in a form American System economist Lyndon LaRouche describes as "the great mudslide." The most recent event in the process occurred in Venezuela, at 2:00 a.m. on June 14, when the government put the eight largest banks into receivership—after having used 70% of the national budget to try to keep them afloat since this spring.

Ah, rich irony! One of the major social events at the IMC meeting was a private performance of Walton's "Belshazzar's Feast, the biblical story of the king of Babylon, who throws a feast during which the words "*Mene, Mene, Tekel, Upharsin*" mysteriously appear on the wall. When his wisemen cannot not decipher the words, Belshazzar summons Daniel, who tells the king that the words foretell the fall of Babylon, as punishment for the king's lifting himself up against the Lord of heaven, and praising the gods of gold and silver. How fitting that the last grand orgy of the masters of money was held in London, feting the slavish Babylonian/Venetian whore of Threadneedle Street!