EIR Economics

World Makes a Narrow Escape from a 'Black Friday'

by Lothar Komp

The fuse was lit on Friday, Sept. 22, on the worldwide powder-keg of stock-market bubbles, financial gambles, and unpaid debt titles. A systemic financial catastrophe threatened, which would hardly have remained limited to a pure stock-market crash. The entire edifice of global short-term liabilities was on the brink of collapse, such as it was in the Fall of 1998. But, in contrast to the situation in September 1998, when the Long Term Capital Management hedge fund disintegrated with its $100 billion of debt and more than $1 trillion of financial derivatives, far larger volumes of paper values will disappear in the Fall of 2000, the consequence of a systemic catastrophe. Between October 1999 and March 2000, after all, there occurred the largest orgy of credit expansion and stock-purchasing panic of all times.

It can not be precisely foreseen at this point in time how many corpses have already accumulated in the cellars of large banks and funds. But the stench is already intense. The most visible sign of the desperation of governments and central banks is the joint intervention on Sept. 22. Out of the blue, U.S. Treasury Secretary Larry Summers and Federal Reserve Chairman Alan Greenspan were willing to join in an intervention into exchange markets, launched by the European Central Bank, to support the euro, the single European currency, together with the central banks of Canada, Japan, and Great Britain. Up to that point, Summers and Greenspan had done everything to push the euro down with respect to the dollar, because that was the only way to assure the urgently needed flow of foreign capital into the deficit-plagued U.S. economy. Likewise, on Sept. 22, U.S. President Bill Clinton announced the release of some 30 million barrels of crude oil from the U.S. Strategic Petroleum Reserve, in hopes of lowering the price of oil. The U.S. Treasury Secretary had scoffed at the very idea of such a decision as a "crude political blunder" just days previously.

High-Tech Stocks Fall

On the surface, the surprising change of sentiment on the part of members of the Clinton government had to do with the fear of a "Black Friday" on the stock markets. In addition to the weeks-long sell-off mood on worldwide stock markets, triggered primarily by the collapse of the euro and the explosion of oil prices, a devastating hurricane threatened to wipe out technology stocks on Sept. 22, led by the Nasdaq. On Thursday evening, after the markets had closed, the flagship of the U.S. computer sector, Intel, announced that it expected a drop of profits for the third quarter, which sent the processor producer's stocks plunging 20% within a brief time of electronic trading. Intel's stock slid down 22% in official trading when markets reopened, which wiped out $95 billion—the largest daily loss of a single firm ever recorded—of the firm's stock capital. On that day, 307 million Intel shares changed hands, also a record.

The Intel shock naturally threatened to spill over to the rest of the technology stocks. On Thursday evening, U.S. computer firms, including Compaq, Dell, and Texas Instruments, rushed to assure the public that they are really in fine health and investors should not allow themselves to be stampeded into a general panic because of Intel's problems. That provided little relief. On Friday morning (European Central Time), Japanese and South Korean technology titles were being bashed collectively. The New Market in Frankfurt opened with heavy losses. When Wall Street opened for busi-

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ness, all the dams were about to burst.

On Sept. 25, the Monday following the melee, the German financial daily *Frankfurter Allgemeine Zeitung* wrote: "Whatever the detailed reasons for Friday's intervention in favor of the euro may have been, the delicate situation which had built up following the warning by Intel on Thursday after markets closed, and which began to unravel early on Friday in the Asian-Pacific area, belonged to a causal chain, according to the view of these strategists. A stock-market crash of unforeseeable dimensions, with severe dislocations also on international exchange markets, could very well have occurred out of this situation. At that moment, everything came together, which had to force the central banks to act."

But that is still not the whole truth. Well-informed financial experts in Europe emphasize that, in the hours and days before the combined euro intervention of the Group of Seven (G-7) nations, rumors were circulating on the financial markets, that a large American investment fund, which had invested primarily in technology stocks, was on the rocks. Had Nasdaq taken another severe plunge on Sept. 22, this fund would have gone under completely. But it is possible that has already happened, and the fact has simply not been made public, in view of the tense mood at this time.

Morgan Bailed Out

Moreover, experts point to strange circumstances surrounding the takeover of the U.S. investment bank J.P. Morgan by Chase Manhattan. J.P. Morgan is one of the largest players on the worldwide derivatives markets. At the end of August, financial journals released the spectacular report that Deutsche Bank was going to buy up J.P. Morgan, and thus become the world's largest bank. Soon after these reports circulated, the silence of the graveyard greeted this mega-marriage. And a few days later, the news was that it was not Deutsche Bank, but Chase Manhattan, that would buy up J.P. Morgan, and the deal was supposedly already worked out in the finest details. A financial newsletter, *Golden Sextant,* which is closely associated with Gold Anti-Trust Action Committee (GATA), which is battling against the manipulation of gold prices, reported on Sept. 19, that, as a consequence of failed derivatives gambles, J.P. Morgan was hard hit, and the takeover by Chase was nothing but a "bailout."

According to *Golden Sextant,* this was also the reason why the chief of the derivatives department of J.P. Morgan, Peter Hancock, resigned on Sept. 8, and it was the reason why the Chase takeover deal was packaged at such record speed. Such rescues, disguised to the public as takeovers, are nothing unusual, and Swiss financial sources say that this was the decisive reason for the merger of Union Bank of Switzerland and Swiss Banking Corp. two years ago.

The newsletter refers in this connection to the surprising and contradictory series of articles in the *Frankfurter Allgemeine Zeitung* at the end of August and beginning of September, which dealt with the manipulation of the gold markets and with accusations by GATA in particular. On Aug. 25, the *Frankfurter Allegemeine Zeitung* carried an article entitled "The Gold Market Is Being Manipulated by Financial Institutions," which explained in detail how the price of gold had been artificially depressed for years, by means of futures sales of four times more gold than is produced in any given year, and these future contracts represented a "ticking time-bomb" for the participating banks and funds.

In this article, written in Frankfurt, according to the newsletter, the German central bank, the Bundesbank, had delivered a deliberate broadside attack against the plans, which still existed then, for a merger of Deutsche Bank and J.P. Morgan. Both Deutsche Bank and J.P. Morgan are massively exposed in gold derivatives contracts. Had there been a merger, then troubles at the largest banking group in the world would have fallen within the jurisdiction of the Bundesbank, and that would have represented a problem "which the Bundesbank obviously did not want to have."

On Sept. 5 and 7, the *Frankfurter Allegemeine Zeitung* published two articles, this time written in London, both of which vented their rage at the representation given in the article on Aug. 25.

Another indication of the corpses in the cellars of the large banks, is the fact that not only the chief of the derivatives department of J.P. Morgan had to step down, but this was followed in mid-September by the sudden and premature resignation, of Rolf E. Breuer, the chairman of Deutsche Bank.

More Stock Market Losses

All of these developments are occurring in an environment pervaded by the extremely nervous stock markets, in which even the heavy-weights among the technology stocks are suffering severe losses. Relative to their record heights, the stock valuations of the three largest technology titles in the United States have recently practically evaporated: Microsoft has fallen from $616 billion to $333 billion, Cisco from $555 billion to $424 billion, and Intel from $503 billion to $322 billion. T-Aktie in Germany fell from 105 euro in March to less than 38 euro at some points, which is a loss of a hefty 64%.

Currency markets are also playing insane, so that extreme swings even among the five leading currencies are a daily occurrence. Stocks, currencies, and other financial titles form the basis, in turn, for the highly speculative derivatives contracts between the largest banks and the funds, to a total volume which corresponds to hundreds of trillions of dollars. There is also the gigantic debt of international corporations, especially in the financial and telecommunications sectors. The growth of worldwide indebtedness is so large, that it is only possible to describe it as a credit explosion that has run out of control. According to the most recent data of the Thomson Financial Data Service, the new debt of the largest debtors in the world is growing at an annual rate of 140%. The next financial corpse dumped into the cellar could well be one too many.