Financial Jolts Speed Push for Glass-Steagall

by Paul Gallagher

July 7—The end of June delivered a series of jolts to the trans-Atlantic banking systems. The result was a U.S. House of Representatives Financial Services Committee hearing on June 26, featuring repeated discussions of whether to reinstate Glass-Steagall Act, which one witness called "quite unexpected." Two of the four bank regulators who testified at the hearing told the Committee they favored Congress re-enacting Glass-Steagall.

The U.S. bank regulators told the key House committee that restoring the Glass-Steagall Act would solve the "too-big-to-fail banks" problem, one day after a senior British MP demanded of the Chancellor (Treasury Secretary) that Glass-Steagall be enacted in Britain immediately to stop a bank debt meltdown.

In the June 26 session on "The Federal Reserve and Too-Big-To-Fail Banks," Rep. Michael Capuano (D-Mass.) asked all the witnesses, who are well-known and respected bank regulators, "If you could restore the Glass-Steagall Act now as the solution, would you do it, if you had the power?" Capuano is a co-sponsor of the House bill to do just that, H.R. 129, the Return to Prudent Banking Act, which now has 67 House sponsors and a Senate companion bill, S. 987.

Federal Deposit Insurance Corporation (FDIC) vice chairman Thomas Hoenig answered, "Yes, I would. That's what I am proposing you [Congress] do." Former FDIC chairman Sheila Bair answered the same question, "Yes, absolutely." Dallas Federal Reserve president Richard Fisher said, "I think what we [the Dallas Fed] have proposed is similar." Only Richmond Fed president Jeffrey Lacker implied a negative answer, saying that the Dodd-Frank Act would identify the financial activities that need to be separated from commercial banking.

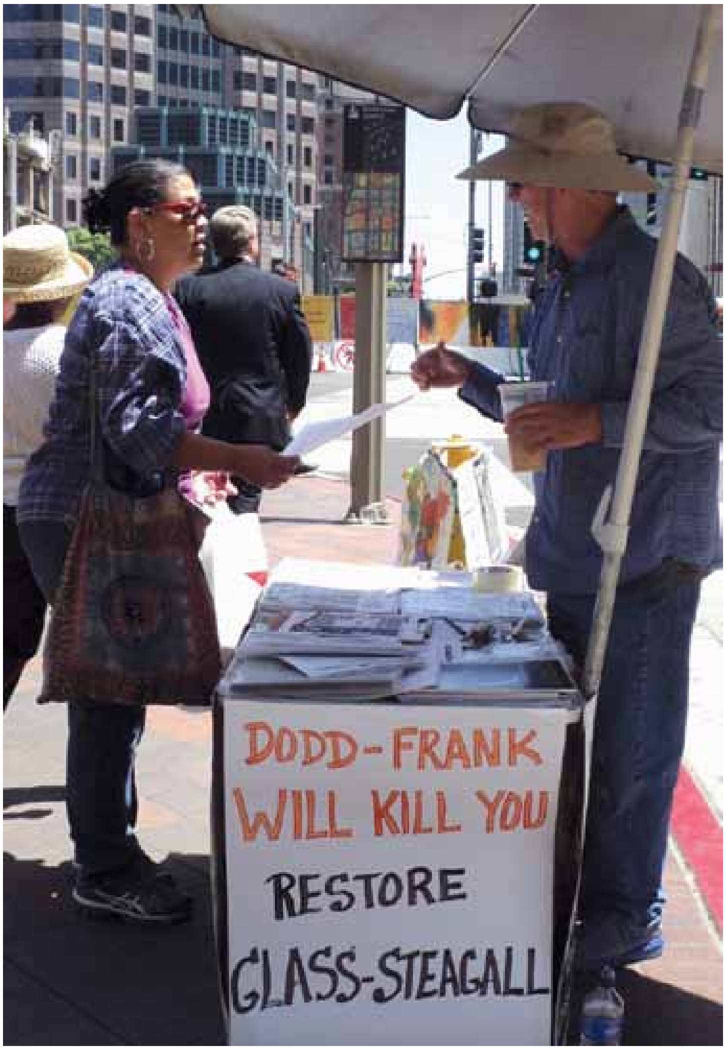
Toward the close of the hearing, Hoenig injected reality into what had been a fanciful discussion of big bank failures. "Title II of Dodd-Frank addresses an idiosyncratic event," Hoenig said, "just a single big financial institution gets in trouble. It's not likely to happen. If you have a systematic meltdown, as we had last time . . . the Congress will be asked for another TARP. . . . Restructure the system now, ahead of time."

On June 25, in the British House of Commons, its senior MP Peter Tapsell, had told Chancellor George Osborne to enact Glass-Steagall legislation in Britain, or face a drastic bank crash.

Deep Austerity Otherwise

That the alternative to reorganizing the banks under Glass-Steagall principles is brutal economic austerity in the short term, was made dramatically clear by events in the second half of June.

First, Federal Reserve chairman Ben Bernanke raised the mere future possibility of printing less money than $85 billion every month for the banks, and the world's bond markets started to crumble. Despite testimonials to unlimited quantitative easing from other Fed



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Without Glass-Steagall, now advocated by a significant number of top U.S. bank regulators, among others, there will be brutal austerity, leading to outright fascist measures. Shown: LaRouchePAC organizing in Los Angeles, May 2013.

governors and central bank heads, by July 5 the U.S. 10-year Treasury interest rate had risen to 2.75% from 1.51% in early May, and mortgage rates in the United States had jumped by a percent and a half. Corporate bond markets fell even faster during that period, and it became difficult to find buyers for investment-grade corporate bonds for periods in late June. Financial bubbles are, once again, potential collapse triggers: in particular, junk bonds, and the financial derivatives known as collateralized loan obligations (CLOs), which played a major role in the 2007-08 bank panic.

U.S. banks dramatically increased their exposure to financial derivatives in the first quarter of 2013—that bubble grew by 72%, to an estimated $231 trillion in nomimal value; and the banks' holdings of CLOs shot up by 24% in the second quarter alone—even as their ordinary commercial and industrial lending stagnated near a record-low portion of their deposit base.

Immediately following Bernanke's press conference, the Bank for International Settlements (BIS) released its annual report on June 28, recommending that the Federal Reserve and the central banks of Europe *stop* printing money—the so-called quantitative easing—now. The bald impossibility of this, from the central banks' standpoint, given the desperate dependence of the large trans-Atlantic banks and securities markets on this money-printing, was shown very quickly by the early July meetings of the Bank of England and European Central Bank. Both kept their interest rates near zero (0.5%), their "liquidity" programs unlimited, and their respective presidents, Mark Carney and Mario Draghi, both broke precedent by issuing "forward guidances" promising to continue this policy "for a very long time" (Carney) or "indefinitely" (Draghi).

But the BIS, from which emerged in 2011 the Cyprus-style "bail-in" policy of stealing depositors' money to keep insolvent banks operating, meant its report dead seriously. "Stop quantitative easing" was obviously a device to get attention; the Bank's real message to governments and the supranational European Commission/IMF bureaucracy, was that bailouts "have bought time" to implement draconian austerity, as in Greece, across the board: Now do it. Specifically, the BIS advised: Break up labor contracts; and eliminate "age-related payments" (pensions, retirement health plans, etc.); privatize government activities.

A special 16-page report on Europe by JPMorgan Chase's research division, which came out one day before the BIS annual report, drove at the same fascist austerity policy. Too many European nations' constitutions, the bank stated, were based on "anti-fascist premises" from the post-World War II period; these stand in the way of the "further process of needed reform." The constitutions of Greece and Portugal were named as obstacles to a policy of fascist economic austerity by Morgan; now, those of Italy and Germany were named as well.

Simultaneously, the Eurozone finance ministers were meeting to finalize a "bank resolution regime" for the continent (the scheme which promises, like the Dodd-Frank Act Title II, to "end all taxpayer bailouts" of insolvent large banks"). What the ministers adopted, after two days of acrimonious negotiations, was the Cyprus model: a guideline of 8% of all the liabilities of a large, insolvent bank will be seized and used to recapitalize the bank—its stockholders' equity, its bondholders' bonds, and its depositors' deposits. The plan gives the bureaucracies the ability to *exempt* from such seizure, any category of bank liability they think will "minimize risk to the securities markets," pointing, of course, to protecting derivatives holdings while seizing deposits and uninsured creditors.

At the finance ministers' meeting, proposals for far more drastic seizures were made, than what was adopted for now. Press leaks made clear that a 2011 report of the Boston Consulting Group had been discussed, which calculated that a 30% seizure of all assets in Europe would be required to wipe out the toxic-debt overhang on the big banks' books, estimated at EU4.5-5 trillion, or about $6 trillion. The 80% wipe-out of a million depositors of the Bankia Group in Spain in May showed just how draconian *this* method of imposing killer austerity can be. And this, with all of Europe exhausted by bank bailouts, already in economic contraction to deep recession, with official unemployment averaging 12%, and youth unemployment 35%.

Glass-Steagall Battle

The financial media recently claim that these demands for fascist austerity are "a matter of contraction in Europe," in contrast to a supposed U.S. "recovery." But U.S. economic "growth" continues to be virtually non-existent, even in GDP statistics. Manufacturing continues to contract and manufacturing employment to fall, even in monthly jobs reports which claim gains. Recent months' reports show the creation of overwhelmingly part-time work in the American economy. During 2013, so far, nearly 80% of the new jobs reported have been part-time; and such jobs now account for 20% of the entire workforce.

In a recent *Wall Street Journal* video interview, Honeywell CEO David Cote was asked, since his company deals with so many industrial sectors in many countries, whether he didn't have a closer view of the real economic situation than Ben Bernanke. Said Cote, "Nothing's happening, as far as we see. I expect less than 2% [GDP] growth in the U.S. in the next two years, zero growth in Europe. I wish I could say it has, but nothing's changed."

The looming fascist austerity clarifies that time is running out to impose a Glass-Steagall bank reorganization, and to pursue a national credit policy to revive real productivity and economic growth. Wall Street, which won't survive such a policy change, knows it as well. Not only fighting the Congressional Glass-Steagall moves with big money and threats, the Wall Street banks have gone down to the state level to battle Glass-Steagall memorials to Congress, which have been introduced in nearly half the states. In Delaware, five major bank lobbyists, led by JPMorgan Chase, registered to stop the state senate from demanding Glass-Steagall. At hearings, they threatened Senators with withdrawing "26,000 jobs" from the state if it did so; the bankers demanded the Governor prevent a vote on the Glass-Steagall memorial.

But Representative Capuano's question to the bank regulators June 26, and their answers, show that the fight for Glass-Steagall can shift unpredictably. The only thing predictable is the alternative; new bank collapses, new bailouts, and fascist austerity.