SENATE HEARING MAKES CLEAR

It's Either Glass-Steagall Or a New Crash Very Soon

Special to EIR

Jan. 13—A panel of five economists questioned by Sen. Elizabeth Warren (D-Mass.) at a Jan. 8 Senate Banking Committee hearing, was unanimous in declaring that neither the Volcker Rule nor the entire Dodd-Frank Act has removed the "too-big-to-fail" danger of the Wall Street banks which brought down the economy in 2007-08. Warren responded to the panel's judgments by stating that it is time for Congress to take additional action; she is one of the prime sponsors of Senate legislation to restore a "21st Century Glass-Steagall Act" (S. 1282) and break up these Wall Street banks.

The hearing, of Sen. Sherrod Brown's (D-Ohio) Subcommittee on Financial Institutions and Consumer Protection, was called to receive a new report by the Government Accountability Office (GAO) on how much the big banks were bailed out in the crash (in the trillions), whether they are still subsidized (yes), and whether the Dodd-Frank Act had ended the threat of a new crash and colossal bailout. GAO economist Lawrence L. Evans summarized his conclusion, "Dodd-Frank aims to restrict future government support, but implementation is incomplete and effectiveness remains uncertain."

The GAO's criticism was directed at Title II of the Dodd-Frank Act, the so-called orderly liquidation, or, more acurately, "bank bail-in" scheme. Well-known economists Luigi Zingales of the University of Chicago, Simon Johnson of MIT, Alan Meltzer of Harvard, and Harvey Rosenblum formerly of the Dallas Federal Reserve Bank and now at Southern Methodist University, all debunked Title II in the course of testimony and questioning. What was clear was that Dodd-Frank measures would not prevent massive new bailouts, nor a market crash.

Warren Poses the Question

But Warren brought the hearing to a point by asking all the witnesses, first, "Will the Volcker Rule [another section of Dodd-Frank—ed.], if vigorously enforced, end 'too big to fail'?" All answered "No," with Rosenblum adding, "Hell, no." Warren then asked whether all the regulations of Dodd-Frank, if completed and vigorously enforced, would end the too-big-to-fail (TBTF) danger. Again all responded "No," with Meltzer and Rosenblum emphasizing that only action by the legislature, not relying on myriad rules and on regulators, could solve the urgent problem.

Johnson explicitly told Warren that, barring any "credible" plan for shutting down bankrupt banks, which he did not see in the cards, "the Federal Reserve and other authorities should take remedial actions, including much higher capital requirements, including breaking up the banks as you proposed, along the new Glass-Steagall lines."

Having teed the ball up, Warren then drove it down the fairway, saying that Treasury Secretary Jack Lew had agreed, at a mid-2013 Banking Committee hearing, that if TBTF Wall Street banks were not reined in by the start of 2014, a different attack would be needed. She concluded that it is now time for Congress to act again. The reference to her Glass-Steagall restoration legislation was implicit, and is the obvious next subject for a hearing in Senator Brown's subcommittee.

A YouTube video of Warren's exchange with the witnesses and concluding remarks, spread rapidly.

Lew Does the Opposite

Treasury Secretary Lew, of course, has no intention of taking action against the huge, predatory Wall Street banks. He, his boss President Obama, and the European Union banking authorities are instead desperately trying to shore up the bankrupt trans-Atlantic banking institutions, by extending the Quantitative Easing (QE) process and protecting the banks from any regulatory measures which would expose their fundamental insolvency.

While the Senate hearing was taking place, Lew was traveling to the capitals of France, Germany, and Portugal to deliver the message which the bankers want to hear: New measures of bailout should be put into effect immediately. In particular, Lew urged every minister he met with to get Mario Draghi's European Central Bank to start large-scale QE—Fed style—buying the toxic assets off the books of the Euro-banksters, e.g., Deutsche Bank, HSBC, etc.

Then, the "global regulators," including the Federal Reserve and European Central Bank, going along on every point with the biggest trans-Atlantic banks, agreed on Jan. 5 that the bank's minuscule capital ratios should not be touched, leaving them at 3% (or about 35:1) indefinitely. *This leverage ratio destroyed Lehman, Bear Stearns, and would have collapsed all the others without TARP, FDIC, and Fed bailouts.* It was left untouched after what the *Financial Times* called "ferocious resistance" by the banksters to proposals to raise the ratio to 6% (or 16:1), or to 8%, (or about 12:1 leverage).

Moreover, the regulators, meeting at the Bank for International Settlements (BIS) in Basel, agreed to change the definition of bank assets *back to one which includes almost none of the so-called "systemically important financial institutions'" derivatives exposure*, or other off-balance-sheet structured investments.

The decision at the BIS was hailed by ECB head Draghi.

The biggest British and Eurozone banks have no ability to raise capital because of their toxic condition, except from government bailouts, or by confiscating assets from creditors and depositors. They also do not want to be forced to get any less big, the other way to raise their capital ratios. The only thing the Eurozone big banks will now have to do, is to drop the "risk-weighting" which makes even their tiny capital ratios fraudulent—and they may have to make that change as early as ... 2018. "The big banks can now exhale," wrote the German financial daily *Handelsblatt*.

They could, that is, if they were alive and breathing, not the zombies they are. Combined with the leaked reports that the EU's Single Resolution Mechanism treaty and EU bank union head Michel Barnier will *not* regulate any breakup or even ring-fencing of banks, the picture is clear: The Eurozone banks are too fragile to be touched in any way while they "stumble toward the next crash," to quote former U.K. Prime Minister Gordon Brown in the *New York Times* Dec. 16.

Where's Glass-Steagall?

The weapon with which to prevent a disastrous crash lies in the hands of the Congress, with two matching bills in each House. So far this session, no Congressman has stepped forward to push them through.

On the state level, the situation has begun to move. On Jan. 8, State Senator Richard Black, a Republican from Virginia, introduced S.J. 22, a resolution urging Congress to pass the Glass-Steagall Act. This is the first memorial to be submitted in 2014.

Then, speaking Jan. 9 before the Economic Forecast Luncheon of the Wisconsin Bankers Association, Kansas City Federal Reserve president Esther George issued a clear call for Glass-Steagall, as the most effective means to eliminate the too-big-to-fail banks, restore sanity to the U.S. banking system, and especially to provide desperately needed relief to community banks, which are not being aided by the incredibly complex Dodd-Frank monstrosity.

George is a key ally of former Kansas City Fed chairman and Glass-Steagall proponent Thomas Hoenig, as well as an opponent of Quantitative Easing and the low-interest-rate policy that has wreaked havoc in the economy, and she is now the only member of the Fed to openly advocate Glass-Steagall.

As for Wall Street, however, the bankers are well aware that there could be an immediate surge for the Glass-Steagall they so greatly fear, at any point. This fear was writ large in a Jan. 9 "Top Story" published in the *American Banker*, which dealt with Glass-Steagall and Hoenig's arguments at length—only to claim that the bill's popularity was due to it being an eponym, i.e., bearing the names of its sponsors! That's called whistling past the graveyard.