The Genesis of Today's Economic Crisis, And How To Solve It

by Paul Gallagher

Jan. 29—Lyndon LaRouche has a pretty powerful record in forecasting, going back a very long way, to the early 1960s; the forecasts he's made over that period of time have been few in number, and very fundamental in character. They haven't been recommendations to buy gold, or buy this stock, or something like that. They have been decade-long forward looks at what different fundamental economic and financial policies on the part of nations, would produce.

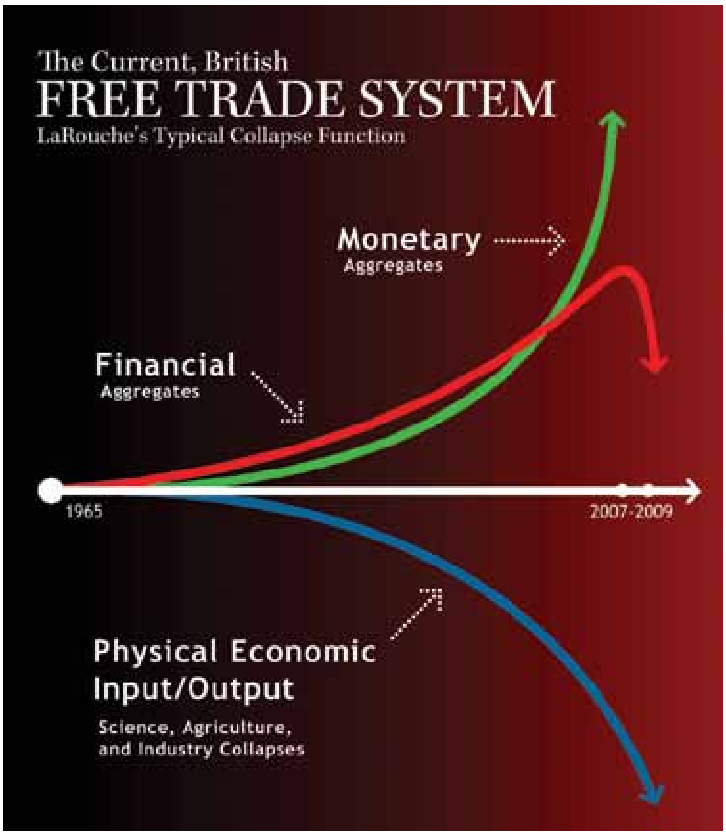
Very early, in the early 1960s, he forecast that by the end of that decade, the Bretton Woods System, under the continuation of the then-present policies by the trans-Atlantic banks in particular, would break up, and the dollar and the other currencies would be broken from gold. That happened in 1971, and caused a shockwave around LaRouche in the economics profession and otherwise, internationally, because he had forecast the series of the events leading to that a decade before.

He did this again, in the middle 1990s, in what he called his Ninth Forecast, in a kind of gesture to Beethoven's Ninth Symphony, and that forecast, also over a decade's period of time, proved to be absolutely correct. He foresaw that, under a continuation of the policies of the international banks in the new environment following the fall of the Soviet Union, and the unleashing, or unbridling, of the wildest speculations of these banks in the environment of the looting of Eastern Europe, Russia, and so forth, the growth of debt was even being exceeded: As wildly as the debt was growing, it was being exceeded by the printing of money (**Figure 1**). And he said, this is going to lead, within a certain period of years, to a thorough crash.

In a webcast in the Summer of 2007, he said it is coming down now, and it was, in fact, as everybody knows now, coming down just at that time, when it was still being denied by the chief of the Federal Reserve, and the heads of the central banks, and so forth. And it came down.

So, LaRouche is saying now that Wall Street is in a crisis—and by Wall Street, he means, and we always mean, the trans-Atlantic system of banks, centered actually in London, not in Wall Street, of which those are the two primary centers in the world, which provide the policy direction and the insanity direction for all of the rest of them. So when he says that the whole Wall Street

FIGURE 1



system of banks is now facing a bankruptcy crisis, he means that trans-Atlantic system.

We know, for example, that half of all the money that the Federal Reserve printed—the trillions and trillions that it printed and gave to the banks in the aftermath of the Crash of 2007-08—went to European banks; it went through their U.S. branches, but well over $2 trillion went into the creation of reserves for European banks. So, when he says that, that's what he means.

Wall Street-London Owns the Central Banks

The central banks themselves are completely creatures of the London and Wall Street banks—they are in no way government institutions, and in critical periods, not even influenced significantly by governments—they're creations entirely of the Wall Street and London banks. They are the ones who are creating this crash, and have been working hard to create this crash over the last six years.

I would say to people, in thinking about this: Forget TARP [the Troubled Asset Relief Program]. TARP was a few marbles thrown into a can. Compared to what the Federal Reserve, the Bank of Japan, the Bank of England, the European Central Bank have done since, in the printing of approximately $16 trillion worth of currency reserves for the banks—what was done in TARP was not only tiny, it was even relatively sensible, by comparison.

What is the objective of this policy of printing? The objective was that the banks, in particular in Europe, but almost equally so in the United States, have become completely loaded with debt securities which were becoming increasingly impossible to collect. That is, increasingly toxic debt securities, and securities based on debt, and derivatives bets based on those securities based on those debts—they have become increasingly unpayable, and that has continued to be the case ever since the crash in 2007-08.

Why haven't those banks taken those losses and gone out of business—the investment side of them, anyway? Because the Fed has continuously been printing money, in order for the banks to plunge into new speculations. They would be loaned the money at effectively zero interest, by the Fed and the other central banks; and they, the major banks, would find new high-yield (what they call high-yield, means high interest rate) investments to make, with the many, many trillions in essentially free money they would receive. And those superprofits which they would be able to make in those high-yield areas, would eventually, over time, allow them to ease their way out of these massive piles of unpayable debt which they had on their books, and which they were calling assets.

We had a discussion just today with one of the leading economists in Europe, both in terms of his capabilities and also the positions he's held, and he said that he thought that the dismantling of Wall Street and the elimination of investment banking were going to happen one way or another, because the banking system is now veering toward a much bigger crisis than 2008. He said it was inevitable, that no one was moving to stop it, that you cannot get out of quantitative easing—which all these banks are now in, and have been in—which is designed to protect the present system of banks. If the low interest rates stop, he said, the debts then can't be serviced. If you continue quantitative easing, you reach a tipping point eventually, where significant inflation, and even hyperinflation, is likely. And he concluded: Japan has now nearly reached that point, of a hyperinflationary explosion.

We've Seen This Movie Before

Or take what the *Financial Times* wrote in a op-ed two days ago, talking about the oil debt crisis, which has suddenly hit the banks, both in Europe and the United States, because of the plunge of oil prices. This is a quote: "Last decade the investors learned a nasty lesson about contagion. When the price of mortgage bonds and related derivatives plunged in the Summer of 2007, it initially seemed to be an isolated problem. Ben Bernanke, then the Federal Reserve governor, declared that losses on subprime mortgages would be limited to $25 billion. But in the event, the panic spread to infect the whole financial system. Losses were 100 times higher.

"Could the same thing happen again, as a result of plunging oil prices? Timothy Lane, deputy governor of the Bank of Canada, told an energy conference in Wisconsin [Jan. 26] that it could, and that central bankers are alert to the possibility that financial linkages could transmit stress from oil markets to the financial system.

"Meanwhile, big investors are pondering those parallels with subprime."

The *Financial Times* then quotes one of these big investors, a manager of the Bank of America, who compared the trajectory of the Brent crude oil price falling, to the 2007 ABX index of subprime mortgage derivatives falling. He found that the patterns were almost identical. And he said, and they quote him: "As mortgage analysts, our concern with the disorderly downside scenario [to oil prices] perhaps is heightened by our experience with the subprime crisis. We feel that we may have seen this movie before."

Now, the central banks have created this. This is just a few very well-informed economists, like the one we spoke to today, who understand, and take the overall view of it: that this has not been created by this or that bank, JPMorgan Chase or Citibank; it has been created by those banks, through their instruments—the Federal Reserve, the European Central Bank, the Bank of England. This has created even wilder high-yield, higher-interest speculation bubbles, and they have printed the money for the banks to go into these bubbles, and loaned it to them for free in the volumes of many, many trillions of printed dollars.

EIRNS/Stuart Lewis

LaRouche demonstrates his Triple Curve at a conference in January 1998.

This is what has brought us to the oil-debt crisis that ironically is going to bring these guys down now—although it's not the only thing that's currently doing it.

The Looting of Greece

The case of Greece is very important, because it illustrates exactly how this works.

There is a column in the London *Daily Telegraph* today by that venerable British intelligence agent and financial columnist Ambrose Evans-Pritchard, calling Greece the "nuclear device" of debt. And basically, in spite of that explosive title, he says, what the new government of Greece is demanding is completely justified, because it wasn't Greece that wanted all this money to be loaned to it, in the second half of the first decade of this century. Rather it was the European major banks which insisted on plowing into Greece after it was pulled into the European Union, and lending it money, far, far beyond what the productivity of the Greek economy could repay. And including lending it to some of the most corrupt possible agencies and institutions, and corporate networks.

Then, in 2010, after those banks crashed, they discovered that Greece couldn't pay any of this debt. And what they then did, was to get the European-wide institutions like the European Stability Fund, and also the IMF, and the European Central Bank itself—they got those institutions, essentially institutions based on taking money from the European countries, to lend another huge volume of cash to Greece—except they were not lending it to Greece. Greece didn't want it, but it had to take it. And it had to take it as debt, and then pass it on to the major European and London banks which had previously loaned it all that money.

So, in effect, those loans, including Wall Street-backed loans to Greece, were loaned for the London, European, and Wall Street banks, by European governments and international institutions, and the Greek government wound up with the bill for all that, in a mound of debt which never, in a million years, could be paid. Because as a price for getting that second wave of liquidity, which left the country as fast as it came in, Greece was given an austerity program which completely crushed the economy over the last five years, to the point where, as Evans-Pritchard said, this debt is now completely unsustainable; no one should fool themselves it can ever be paid under these circumstances.

'Extend and Pretend'

There is an open letter to the German people from the new Greek prime minister, Alexis Tsipras, which says exactly the same thing, and much more. It says that the sane people in Greek political parties in 2010 didn't want all this money to be loaned to Greece, because they knew where it was really going. And both of them—Pritchard and the prime minister of Greece—used the same term to describe this: "extend and pretend."

It's a very well-known term in the financial sector. When you have loans on your books which can't be paid, you make new loans to the borrowers, and pretend that they paid the old loans with those new loans, even though they haven't in fact paid you anything. Or you simply extend the terms, but impose some condition on them, which makes them even *less* able to pay, but meanwhile, you satisfy yourself that you've extended the term of the loan.

This is exactly what the central banks and the IMF and central European monetary institutions, did in the Greek case. And it illustrates what they've done in respect to the international banks in all of these cases. And in the broad case of the printing of this $16 trillion, which has actually been made available to the banks by these central banks.

That is what LaRouche says has brought us to a crash, has brought Wall Street to a crash, at this point.

I won't go through in detail how this extend-and-pretend operation in U.S. banking, in the big Wall Street banks, focused itself on the so-called shale oil patch, because that is the bubble they chose to build. They built it through high-yield loans. The loans to that sector are on the order of, and have always been, 6 to 10% in interest; they're now considerably higher than that, because they're now in crisis. They have made a tremendous amount of money for banks, which under Glass-Steagall, couldn't even be going into these commodity areas. And they also created a bubble of debt on the order of $650 billion, which is absolutely going bad now, and it's part of a bigger bubble of two and a half trillion, which is being exploded by that energy high-yield bubble within it.

They did that because they were enabled to do it by the Federal Reserve. And they did it with the Obama Administration leading the charge, and saying: Our recovery, our new superiority of the United States against Europe, our decoupling, our breakaway economic recovery, it all comes down to our being the new Saudi Arabia of the world, because we have these two technologies for recovering oil, inefficiently, expensively, and that's what we're going to do.

There's a famous meeting that Obama had in a backyard in Virginia, where he said: We, the United States, don't need any of these exotic things like fusion energy, because our inventors have come up with new technologies in the oil sector, which will make us the leader of the world in this regard.

So, it was Obama policy all the time. It was Wall Street policy. The bubble's been built up. This is by no means not the only bubble bringing the banks down, but in terms of Wall Street per se, it is.

LaRouche's Solution

So, LaRouche said, what we've got to do is make two things clear:

First of all, these banks have to be crushed, in effect; broken up, made to go bankrupt, except for the commercial bank parts of them which can be insured and protected. The other parts of them have got to be let go. They will go bankrupt. This has to be done right away. Wall Street has to be put out of any situation in which it can continue to manage the economic affairs of the country, as it has been doing.

We've seen this really obscenely lately in the way the banks, led by Citi and JPMorgan, intervened immediately into the Congress, rolled over the Congress, and got the few little regulations of Dodd-Frank which were annoying them, and annoying their derivatives operations, got them repealed, got them out of the way, as the very first items of business in this supposedly jobs-oriented Congress, which is coming in. The very first few weeks they had their noses put to the grindstone, and Wall Street told them, repeal these regulations. And they did it.

Break that power. Get them completely out of any management of the U.S. economy. Break them up. That means start the process of the bankruptcy reorganization by re-enacting the Glass-Steagall Act, but don't wait for that breakup to be completed. As LaRouche made clear, we have to, at the same time, create a kind of a buffer of credit, of new credit, from a Federal institution—either a new institution, or a renovated existing institution—to create a buffer of credit for states, cities, businesses, agencies, ultimately for households—but only indirectly.

We need the kind of credit that can put people back into relatively highly skilled, well-paid employment in the kinds of investments that increase the productivity of the economy, because they introduce new technologies through new economic infrastructure, and therefore they make that productivity increase.

That Federal credit buffer—there are immediate ways to provide it, and these things *have* to be done.

For example, Congress should create a Reconstruction Finance Corporation immediately, while initiating the measures to break these Wall Street banks up. A Reconstruction Finance Corporation can get initial government capital, and issue RFC bonds to the public, to commercial banks, and use that credit to support national and state projects, the same way the RFC worked from 1934 to the late 1950s, when it was finally wound up.

Obviously, as LaRouche said, the United States must incur a certain amount of additional debt in order to create this buffer of credit, to make up for the inevitable collapse of Wall Street, which we're going to accelerate. But that debt is measured. It must specifically be taken solely for the purposes of this kind of productive employment, and re-employment, and increase in the productivity of the economy, investments in the development of the real economy.

Aid the states with a national high-speed rail network. Give credit support to state and municipal bond issues for new economic infrastructure. Provide Western drought measures, from large-scale water diversion, to a large network of nuclear desalination and power plants. Restore and replace the ancient national network of locks and dams, water for navigation, water management, and flood and storm protection. Restore the worst cutbacks in medical care, in fire-fighting, in sanitation, in water purification, and build them anew. And crucially, restore the nation's historic levels of investment in projects of the National Aeronautics and Space Administration. Get the United States back into the Solar System, in a leading way.

Join the BRICS!

And even more crucially, use the new Federal credit institutions to join the Asian Infrastructure Investment Bank, and the many other new international development banks under the BRICS nations, keynoted around China. And by doing so, increase the buffer of new credit which you're putting into the U.S. economy itself.

Besides the RFC, Congress should create a new national bank, and it should do that, again, by an initial capitalization, in the way that every national bank plan, and actual national bank in American history, was created: by initial capitalization of perhaps 10-20% of the capital of the bank by the government, and the Treasury issuing new debt to that bank, and then otherwise, by the trading in of existing debt, by the holders of that debt—it could be you, and I, and all of us, and many commercial banks, and foreign countries' wealth funds and so forth—trading in a relatively small portion of that publicly held debt of the United States, in exchange for debt of this new National Bank.

Obviously, with higher interest rates, and with a long and in most cases, much longer term, which is exactly how the banks of Hamilton and the Second National Bank of Biddle were initially capitalized.

There is $13 trillion of publicly held Treasury debt out there. If even $500 billion of the debt that's held by the public is invested—is actually traded in for capital in this new National Bank—then the Treasury can issue an equivalent amount of Treasury notes, can issue them directly to that bank, and that bank then has $500 billion in working capital, for investment in infrastructure, and purchase of municipal and state bonds. This is the use of the credit buffer in the way that I was describing earlier.

That's what has to be done, and has to be done quickly, at the same time as the fundamental measures to break up the Wall Street banks are put underway. The point is: If you create this buffer, if you make these investments, if you redirect the U.S. economy toward productivity in that way, you are taking the power to manage the economy away from Wall Street, at the same time that you're starting the process of breaking them up.

And LaRouche stessed the urgency of this, because the financial warfare in which these banks are engaging, in their desperation, has gone beyond trying to control Congress. That's been easy for them, in recent periods. It has been going to the point of trying to bring down nations, and there's no better example than the intense financial warfare, by the banks and by Obama, aimed at bringing down the Putin government in Russia, and plunging that country into chaos, with the immediate consequence tied up with that, of the likelihood of a thermonuclear war.

That's what's involved in this bankruptcy, and we have to put it to an end very quickly.