The EU Is a Dead Man Walking

by Claudio Celani

Dec. 12—The reaction of EU institutions to the Italian constitutional referendum (see *EIR* No. 50) can be described as "Hitler in the bunker." The EU is a dead proposition, after the Brexit, the U.S. elections and the events that have left Angela Merkel as the only survivor—for the time being—of leading EU heads of government in the last weeks. However, the EU Commission, the European Central Bank (ECB), and the German government itself are refusing to surrender, and keep pushing their agenda. It will end like 1945—hopefully including a Nuremberg trial!

As the Italian voters rejected a constitutional change 60 to 40 which would have enslaved the country to the EU dictatorial regime, the EU response was: "It was not about the EU; it was a domestic Italian affair." However, new war plans were drafted and announced against Italy. They moved to plunge Italy into a banking crisis and force it to submit to a Greece-like Troika regime.

Italy does have an urgent banking crisis to solve, but this must be seen on the backdrop of the general crisis of the trans-Atlantic banking system, which is hopelessly bankrupt, and cannot be solved if the issue of commercial banking versus speculative banking is not addressed.

In fact, the Italian banking crisis is mainly due to huge credit losses, whereas the rest of the trans- Atlantic system is burdened by trillions of unpayable financial assets. Additionally, the Italian crisis would be under control if the government were free to use its sovereign power. Instead, it is forbidden by EU laws to bail out a troubled bank unless it first plunders the bank's depositors through so-called "bail-in" regulations. And even after having plundered depositors, Italy is not allowed to recapitalize banks with taxpayers' money, because this would "unbalance" the budget! The only measure offered by the EU to Italy is to take a loan from an EU fund, attached to brutal austerity conditions and to direct EU management of government accounts.

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A greatly inflated symbol of the bankrupt euro, in Frankfurt, with the equally bankrupt Deutsche Bank headquarters in the background.

It is exactly this policy that voters rejected in the Dec. 4 referendum.

In defiance of those voters, two days after the vote, Volker Wieland, a member of the so-called "Economic Wise Men's" advisory board to the German government, gave an interview to the *Handelsblatt* economic daily in which he said that Italy should go to the European Stability Mechanism (ESM), and also get the IMF "involved in the aid program." The ESM is a fund set up by the EU to loan money to financially troubled governments, conditional on brutal austerity measures implemented by a caretaker committee called "the Troika," composed by representatives of the ESM itself, the IMF and the European Central Bank.

The plan, Wieland said, "on one side would represent a 'shield' in case of a debt crisis in Italy, and on the other side, the ESM and IMF together could apply the right pressure to unblock reforms."

How insane the Troika regime is, has been shown in recent years in the case of Greece. Greece was put under the Troika regime in 2011, and since then the national economy has collapsed, unemployment and poverty have skyrocketed, and the country's foreign debt has increased.

EU statistics show that official unemployment in Greece has grown from 12.7% to 24.9%, GDP per capita has plunged from 20,300 to 17,000, poverty-stricken families have increased from 27.7% to 35.7%, and the debt-to-GDP ratio has increased from 146.2% to 176.9%.

Such figures are the result of the EU-imposed target of a 3.5% primary budget surplus for Greece, something impossible to achieve. A primary surplus, or deficit, is the balance of income and expenditures of the government before interest payments. This surplus should then be used, according to the Troika, to pay back foreign debt. Only a few among EU countries have achieved a primary surplus in the last decades, and the strongest country, Germany, reached at best slightly above 2%. Thus, insisting on a 3.5% target for Greece is sheer insanity and an intention of genocide.

This was confirmed at the last meeting of the Eurogroup of Finance Ministers on Dec. 7, where Greece was denied short-term measures for debt reduction because the 3.5% target has not been achieved!

Not that things in Italy have been better; as a matter of fact, Italy has self-imposed an austerity therapy since 2011, when an ECB-led coup installed a technocratic government led by Mario Monti, and Italy signed up to commitments for "reforms" that amount to an "automatic pilot," as ECB head Mario Draghi declared in 2013.

Italy has been an EU champion in consistent primary budget surplus, but this is not enough blood for the EU, and a Troika regime would presumably set the same targets for Italy as for Greece.

The explanation for this genocidal approach is that the Troika bailout programs are in reality schemes for bank bailouts. In fact, most of the €220 billions received by Greece under the ESM program and its predecessor, the European Financial Stability Facility (EFSF) fund, never reached Greece, but were used to pay Greece's international creditors, with German and French banks at the front of the line.

In the case of Italy, it is feared that the failure of a systemic bank such as Monte dei Paschi di Siena (MPS), the most troubled financial institution in Italy, would unleash a systemic collapse. It is also feared that a government refusal to implement a bail-in scheme, would set a precedent which goes against the very foundations of the trans-Atlantic system, which sets the "stability of the system" as the priority over the protection of deposits.

Thus, after the warning by Merkel's advisor Wieland, other orders were issued from the bunker.

On Dec. 7, Moody's rating agency changed the outlook for Italy from "stable" to "negative." Although this is not yet a rating cut, it does have an effect on Italy's financial stability. Rating agencies have regularly determined runs on Italian bonds by lowering their ratings in previous years. This is typical of tactics used to blackmail Italy into accepting mafia-style "protection" by the ECB, in exchange for surrender to austerity programs and technocratic governments.

The next steps were taken by the ECB. First, on Dec. 8, the ECB Governing Board decided to give a clear signal that it intends to continue the life-support measures for the bankrupt system, called Quantitative Easing (QE), indefinitely into the future. The ECB extended QE for six months beyond the planned deadline of March 2017, but said that it could extend it further at will. It then reduced from 80 to 60 billion Euros the amount of assets purchased monthly from banks, which led some commentators to speak of an initial tapering of QE. However, the ECB had already reduced its purchases to 60 billion in the last months, because there are not enough eligible assets on the market. Indeed, the ECB also announced that it has expanded the range of eligible assets, including one-year maturities.

Even the German daily *Der Spiegel* commented that the ECB money will only go to inflate the stock market and the real estate bubble, and warned that all such bubbles in the past, from the Tulip Bubble to the subprime bubble, always ended in a crash.

After having promised an additional half trillion euros for speculators in the next twelve months, the ECB then turned down a request from Monte dei Paschi (MPS) to have an additional 30 days time to find €5bn to recapitalize itself! This dramatically worsened the Italian banking crisis, as it is mathematically impossible that MPS could find the money by the established deadline of Dec. 31. With this move, the ECB intended to put the Italian government, already in the middle of a crisis because of Prime Minister Renzi's resignation, into a corner, and force it accede to a bail-in/Troika combination.

Enter Glass-Steagall

However, a major defection took place in the banking establishment. Jens Weidmann, head of the German central bank (Bundesbank), stated in an interview with Reuters Dec. 12 that in a special circumstance such as

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Banca Monte dei Paschi di Siena in Pisa.

the Italian case, a violation of European bail-in rules could be accepted.

Clearly, Weidmann is worried about the effects of an MPS default on Germany's large zombie bank, Deutsche Bank. His statement, however, puts the issue of depositors' protection up-front. In Italy, Weidmann says, "high-risk financial products were apparently sold to people who were actually looking for more conservative products. If now, for political reasons, you want to protect investors who are considered to need special protection, this could occur for instance in the framework of targeted state transfers."

Weidmann was referring to tens of thousands of MPS customers who were lured into purchasing up to €2 billion of subordinated bonds, and who in case of a bail-in would see all their money wiped out. The Italian government is already considering excluding those customers from a bail-in of MPS, as part of a government recapitalization with taxpayers' money. An executive order has already been drafted, and will be implemented in case the planned "market solution" for MPS fails before the Dec. 31 deadline, as it looks probable that it will.

The issue of depositors' protection is the central issue addressed by the Glass-Steagall Act, which the LaRouche organization is pushing worldwide. In the case of MPS, it is urgent that the government intervene to guarantee deposits, but also credits to the real economy. The rest of the assets side of the bank, instead, must be sorted out, and all assets which cannot be priced must be cancelled. This is a reversal of the approach adopted by EU regulations and by the Dodd-Frank bill in the U.S.A. Such "reforms," in fact, have only focused on the bank-lending side, totally neglecting the derivatives and other fluff on the banks' balance sheets.

These bank assets have prices which are determined by bank "internal models," and do not correspond to reality. Instead of sorting out this mess, EU and U.S. regulations have imposed capital requirements related to so-called risk-weighted assets, which include loans, but leave out derivatives whose risk is not weighted. Thus, those banks which lend more to the real economy are disadvantaged in comparison with banks with an overblown derivative portfolio.

The Italian banking system has been targeted by the ECB because it has accumulated between 200 and 400 billions of Non-Performing Loans (NPL). Most of these loans are credits to large, small, and medium enterprises and farms, and mortgage loans to families. Ever since the Italian economy plunged into a depression in 2008, and has never recovered because of the "primary surplus" regime, those credits have become foul. At least eight major banks are in a troubled situation and need a recapitalization under EU guidelines.

The case of MPS is special because it involves both NPLs and derivatives, i.e. commercial and speculative losses. MPS is reported to have €47bn of NPLs, which the bank has covered with only 20bn special reserves. But the root of MPS' troubles lies in the so-called strategy of "inorganic expansion" in financial trading, which MPS started in 1995, when Glass-Steagall-like regulations were lifted in Italy. This "inorganic expansion" culminated, as an investigating committee of the Tuscany Regional Council has established, with the insane acquisition of Antonveneta Bank from Santander in 2008, which has cost MPS a total of €18 billion. In order to cover such losses on the balance sheet, the MPS management eventually bought derivatives from Deutsche Bank and Nomura which produced more losses.

The acquisition of Antonveneta at three times its market value made no sense from a commercial or financial standpoint, but was a "systemic" operation to bai lout Santander, one of the largest European systemic banks. As evidence of the nature of the operation, which was authorized by the Italian central bank under Mario Draghi, MPS head Giuseppe Mussari was eventually appointed as head of the Italian Banking Association.

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Paolo Gentiloni, Matteo Renzi's replacement as prime minister, announcing the formation of his cabinet, December 12, 2016.

Thus, an urgent intervention into MPS and all other Italian banks must involve a mechanism that: 1. replaces the current, corrupt management, with public officials with both competence and proven integrity; 2. immediately recapitalizes the bank with government money in order to protect depositors and savers, and prevent a run on the bank; 3. creates a committee that sorts out the bank assets, protecting commercial loans but canceling all assets which are not salable. In doing this, the Italian government shall act in full sovereignty, without asking EU institutions or EU member governments.

This will precipitate a crisis in the trans-Atlantic financial system, but a welcome one. Financial measures, however, are not sufficient to turn the situation around. The Italian economy needs an urgent physical recovery, otherwise banks will keep producing losses. Therefore, the second step must be a national recovery program with large-scale infrastructure investments.

Whether the new Italian government led by former Foreign Minister Paolo Gentiloni will take those steps is questionable. Gentiloni is a member of an old aristocratic family with a long tradition in modern politics. The characteristic of this species is that they keep their feet in all shoes, ready to play the winning game. Gentiloni's grandfather, Count of the Holy Roman Empire Vincenzo Ottorino Gentiloni, was a co-founder of the Italian Liberal Party in 1912, and brokered a deal with the Vatican in 1913, to have Catholics vote for the new party. This had two consequences: it paved the way for a government that led Italy into WWI in 1915, shifting from the alliance with Germany and Austria to an alliance with France and Britain; and it sabotaged the process then underway to create a Christian Democratic Party based on anti-oligarchical principles.

Grandson Paolo started his career as a student member of Potere Operaio, a left-wing radical group one step away from terrorism. He then became an environmentalist, and finally a member of the liberal wing of the Democratic Party. As a Foreign Minister he went along with EU and NATO decisions, while at the same time keeping up a dialogue with Russia on Libya and Mediterranean issues.

Gentiloni received a mandate from President Sergio Mattarella to run the government until a new election law is ready, and then go to early elections. This sets a life expectancy of a few months, but events could change it, and even extend it to the natural end of the legislature next year. In the mean time, his cabinet, which won't substantially change from the previous Renzi government, must deal with the banking crisis and other emergencies, such as earthquake reconstruction, as well as fighting with the EU on the budget.

From the government's moves on MPS in the coming days, we will know whether the government has minimally learned the lesson of the Dec. 4 vote.