GLASS-STEAGALL

The Other Wall That Fell In Europe in 1989

by Claudio Celani

July 20—In 1989, along with the Berlin Wall, another wall was torn down: the wall separating traditional banks from investment banks. But, whereas the former ended an era of oppression for many peoples, the latter started another era of oppression.

In 1933, for the first time in the United States, President Roosevelt introduced the separation between banks of deposit and credit, and banks involved in financial trading. By so doing, he successfully protected depositors' savings, and permitted an unprecedented expansion of productive credit, thereby fostering the economic recovery of the United States. The U.S. model, called the Glass-Steagall Act, named after the two senators who had drafted it, was quickly imitated in many nations around the world, and facilitated the reconstruction and economic boom of western Europe after the war.

Joyous celebration of the fall of the Wall at the Brandenburg Gate in Berlin in 1989.

Under the bank separation system, no major financial crisis broke out. Failures of individual banks occurred in many nations, without ever jeopardizing the savings and credit system itself.

The abolition of bank separation in Europe preceded the official repeal of the Glass-Steagall Act in 1999 in the United States.

On Dec. 15, 1989, a little more than one month after the fall of the Berlin Wall, the European Commission issued Directive CE 646/89, which established that from then on, credit institutions could do all sorts of activities, including trading the entire spectrum of high-risk derivatives.[1] That directive bound all member countries of the European Union to abolish their national regulations differentiating between the different types of banks—of which some regulations resembled the Glass-Steagall Act that established two categories of banks, while others separated banks according to short-term versus long-term borrowing and lending, and others simply separated savings banks as a special category.

The introduction of CE 649/89 occurred in the framework of the tumultuous events that followed the fall of the Berlin Wall and the strategic decision to accelerate the so-called "integration" process in Europe. The process of ceding sovereignty to the supranational institutions of the European Community had gone on for decades. The plan for the transition to a complete surrender of sovereignty to a European Union, with a Monetary Union, had been discussed for some time—but it had been kept on the back-burner by justified national interests of European nations. The events of November 1989 accelerated that process: French President François Mitterrand, in agreement with British Prime Minister Margaret

1. CE 646/89 is very explicit on what kind of activities "credit institutions" are allowed to perform. The annex lists them all: 1. Acceptance of deposits and other repayable funds from the public. 2. Lending. 3. Financial leasing. 4. Money transmission services. 5. Issuing and administering means of payment (e.g. credit cards, travellers' checks and bankers' drafts). 6. Guarantees and commitments. 7. Trading for its own account or for the accounts of customers in: (a) money market instruments (checks, bills, CDs, etc.); (b) foreign exchange; (c) financial futures and options; (d) exchange and interest rate instruments; and (e) transferrable securities. 8. Participation in share issues and the provision of services related to such issues. 9. Advice to undertakings on capital structure, industrial strategy and related questions, and advice and services relating to mergers and the purchase of undertakings. 10. Money brokerage. 11. Portfolio management and advice. 12. Safekeeping and administration of securities. 13. Credit reference services.

Thatcher, seized the opportunity as a geopolitical means of depriving a unified Germany of its sovereignty, and at the same time avert any pro-agro-industrial and pro-labor reconstruction of the economies of the post-communist countries.

Mitterrand had already reversed France's traditional Gaullist policy, which had opposed excessive transfers of sovereignty to European institutions. He had forced his own party to adopt the so-called "Europe 1992" plan, which was aimed at creating a Single European Market to eliminate trade barriers between European Commission (EC) countries by 1992. The EC is the executive of the European Union. When the Delors Commission (Jacques Delors headed the European Commission for three terms, including the period through 1989) pushed for a Monetary Union, Mitterrand backed it.

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From left to right: French President François Mitterrand, UK Prime Minister Margaret Thatcher, and German Chancellor Helmut Kohl.

Mitterrand, a typical representative of French Social-Imperialism, followed geopolitical designs aimed at ensuring a French sphere of influence in an area stretching from continental Europe to North Africa and the Middle East. In this geopolitical design, however, France would play the junior partner to Britain, which had built the City of London as the real center of global financial power. Thus, the euro was promoted and backed by London and Paris as a geopolitical tool for controlling Germany and enforcing neoliberal policies to the advantage of financial markets dominated by London.

Germany had to be persuaded, by whatever means, to accept the euro/neoliberal blueprint for Europe. Deutsche Bank chairman Alfred Herrhausen, the most influential figure in corporate Germany, had a different idea. He had publicly proposed an anti-free-market dirigist economic development approach for the economies of East Germany and Poland, emphasizing the productive sector. Herrhausen's policy was consistent with the more ambitious proposal of Lyndon LaRouche for a European Productive Triangle.[2] Herrhausen was assassinated on Nov. 30, 1989, physically eliminating the threat of his vision.

Two days earlier, Chancellor Helmut Kohl had presented his Ten-Point Program for the reunification of Germany: Points one, two and three of his proposal involved economic aid to East Germany for reconstruction and cooperation.

The day after Herrhausen's assassination, Mitterrand telephoned Kohl, telling him that he expected him to approve Mitterand's proposal for an Inter-Governmental Conference (IGC) on the Monetary Union at the coming European Council meeting in Strasbourg, Dec. 8-9. Kohl accepted on condition that the IGC would take place after his re-election.

The final communiqué of that European Council meeting did indeed draw a road map for establishing the European Monetary Union, starting from the coming Inter-Governmental Conference.[3] The first action of the European Commission was to issue CE 646/89, with the intention of tearing down the wall separating commercial banks from investment banks, thereby opening up national banking sectors to takeover by London-centered financial speculation. CE 646/89 was eventually incorporated into numerous other directives, and ultimately into the European Treaties in 2007.

The elimination of banking separation meant that only one type of banking model was admitted, the universal bank, under whose roof, both traditional deposit and lending activity takes place, as well as high-risk speculative activity. Investment banks that issue asset-backed securities could now rely on the protection offered by the commercial side of the bank, and on the entire savings of bank depositors as potential collateral for the expansion of the financial bubble. Suddenly, local savings banks would have to participate in derivatives trading on the global financial market. Banks started to merge and expand their balance sheets, grow-

2. See http://www.larouchepub.com/eiw/public/1990/eirv17n31-19900803/eirv17n31-19900803_031-the_economic_geography_of_europe.pdf

3. See http://www.europarl.europa.eu/summits/strasbourg/st_en.pdf

ing larger and larger. Inevitably, the bubble burst in 2008, threatening the collapse of the entire system.

At that point, monetary authorities and governments used the blackmail of deposits being at risk, to implement the biggest bailout in history. Remember, that in the midst of that financial panic, German Chancellor Merkel and her Finance Minister, Peer Steinbrück, went on prime-time television to declare to the nation that "all savings and deposits are 100% guaranteed." But instead of doing the most reasonable thing, i.e. reintroducing banking separation and guaranteeing *only* deposits and savings, the German and most other EU governments also guaranteed that speculators would be bailed out.

Deutsche Bank Chairman Alfred Herrhausen.

It has been calculated that direct government bailouts of banks in the EU cost 800 billion euros. Germany alone paid 238 billion to bail out its banks; Spain 52 billion, Ireland 42 billion, Greece 40 billion, Netherlands 36 billion, Austria 28 billion, Portugal 19 billion and Belgium 19 billion. This massive bailout, financed with newly-issued government debt, only postponed the problem, and created another. Suddenly, the sovereign debt market in Europe was flooded with a giant supply, met by a relatively small demand. This forced countries including Italy, Greece, Portugal, and Spain, to offer higher yields to compete with German bonds. A European debt crisis developed which threatened to destroy the euro system itself. The first stage of the crisis was dealt with through so-called "bailout packages," carrying murderous austerity conditions. Greece's national economy was destroyed under this therapy.

In the longer term, to save the euro, the European Central Bank (ECB) started an unprecedented monetary expansion, buying sovereign bonds from the banks, and issuing special lines of zero-interest loans. Eventually, the ECB started buying corporate bonds and derivatives as well. Thus, its balance sheet was blown up to uncontrolled dimensions. At the end of 2016, the ECB balance sheet amounted to 3,661,439 million euros (3.6 trillion). The Eurosystem is *de facto* bankrupt.

All this would not have happened, if CE 646/89 had never been introduced.

And yet, all the measures taken since 2008—from government bailouts to central bank monetary expansion—have failed to solve the problem. The overall debt has increased, while the real economy has stopped growing because of the austerity policy being implemented in the EU. The next explosion of the system is around the corner, even though monetary authorities have created the illusion that the system is "safer" through fake reforms such as stress tests and higher capital buffers.

In a further ceding of national sovereignty, banking supervision has been transferred from national central banks to the European Banking Authority (EBA), which is under the ECB. The EBA has conducted stress tests to simulate the effects of a crises on major EU banks. Banks that failed the test were ordered to increase their capital ratios.

However, the EBA has failed in assessing the real risk of megabanks' balance sheets, by allowing the banks to use their own internal models to assess the value of their financial assets. The most outrageous example is that of the so-called "Level 3" assets—toxic derivatives that have no market, and whose value is equal to zero. Yet the EBA has permitted the banks to declare an arbitrary value for those derivatives, turning losses into assets!

In April, the Italian Banking Association published figures for Level 3 assets in the EU, which show that the *highest ratio of Level 3 assets to capital* belongs to German banks, with 35.5%. Next come British banks, with 25.4%, and French banks with 20.5%. Italian banks, which are being vilified by the EU because of their losses on commercial loans, have "only" 15%.

In the case of Deutsche Bank, Level 3 assets amounted to 54.8% of tangible net worth!

While closing its eyes to toxic assets, the EBA is tightening the screws on commercial banks which are increasingly burdened by losses on their commercial loans because of the economic crisis. This has become acute in Italy; the Italian economy has suffered a severe recession due to the draconian budget cuts and tax increases imposed by the EU. It is calculated that Italian banks have about 400 billion euros in non-performing loans (NPLs).

The absurdity is that under EU law, it is impossible to recover an NPL. In former times, if a customer defaulted on a loan, the bank would try to negotiate measures with the customer to alleviate his economic condition, allowing him to pay back the loan in the near future. EU law prevents this, obliging banks to write off the asset and end any financial assistance to the customer—thus ensuring that the loan will never be repaid.

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Italian Senator Oskar Peterlini

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Former Italian Finance Minister Giulio Tremonti

EIRNS/Julienne Lemaître

Italian Member of European Parliament Marco Zanni

It is not difficult to see where all this leads: to the elimination of commercial banks as such!

The EU is not hiding the fact that this is its goal. Banks loaded with NPLs are told that they must change their "industrial model."

Whatever commercial banks survive this triage, will be finished by the next "reform": the Capital Market Union (CMU). Announced in 2016, the CMU is intended to replace bank loans with capital markets. In other words, firms will be told that if they need money to finance investments or trade deals, they must issue bonds on the market. In order to do so, they must turn to an investment bank, which will place those bonds. This ensures that smaller enterprises will be cut off from credit. In fact, only larger companies can afford both the minimal size of a bond issuance (5 million euros), and the fees charged by investment banks.

Reintroducing Glass-Steagall

In recent years, the call for reintroducing a bank-separation system has grown in Europe, especially among euro-critical and anti-establishment political forces. The campaign for Glass-Steagall has been especially strong in Italy, where many remember the 1936 Banking Act that had worked so well until it was formally abolished in 1995 by the Amato-Draghi reforms.

The cancellation of bank separation was the main cause for the crisis of Monte dei Paschi di Siena (MPS) bank, the third largest Italian bank and the oldest active bank in the world. Originally a commercial bank, MPS expanded into investment banking and into acquisitions, culminating in the leveraged purchase of Banca Antonveneta in 2008. In order to cover the losses from that purchase on its balance sheet, MPS then bought derivative contracts with Deutsche Bank and Nomura, which increased the losses. Eventually, the government had to step in and *de facto* nationalize the bank in June 2017.

The banking crisis and the first implementation of the bail-in procedures have produced popular outrage and support for the reintroduction of banking separation. The first draft bill was filed by Sen. Oskar Peterlini in the Italian Senate in 2012. That bill was drafted together with Movisol.org, the LaRouche organization in Italy. In the following years, parliamentarians from almost all parties filed similar draft bills, both in the Chamber of Deputies and the Senate. Among them were prominent figures such as former Treasury Minister Giulio Tremonti. Finally, on March 16, 2017, the Finance Committee of the Chamber of Deputies began discussion of the eleven draft bills which had been filed, and decided to have hearings on the matter. That discussion has not yet been resumed, however.

In the European Parliament, the Italians Marco Zanni (Independent Party) and Marco Valli (M5S Party) began a fight for Glass-Steagall in the Economic and Monetary Committee. That fight was not successful, but it managed to prevent the two larger factions, the liberals and the social democrats, from uniting on an anti-Glass-Steagall platform.

But it is clear that a healthy banking system and issuance of credit to the economy can be re-established only under national law, repudiating and cancelling EU regulations. Step by step, the EU has built a system of financial feudalism which is destroying the real economy and impoverishing the population. It is necessary to reverse this process before the system collapses chaotically with devastating effects. European nations now have the unique historic opportunity to join the "One Belt, One Road" policy of economic growth initiated by China. In order to do that, they must re-establish national systems of credit.