Financiers Are Finally Warning of a Crash

Belated Establishment wailings about a financial blowout are getting louder than the booings of Viceroy Cheney at a Washington ballgame. A selected recent few:

• The mouthpiece of the City of London financiers, the *Financial Times,* lamented April 4 that were "the low interest environment" were to disappear, "the resulting sell-off [on the bond market] would make the recent price falls look like a picnic." Interest rates are on the rise.

• Three days earlier, the director of a large Danish public pension fund, Jeppe Christiansen, wrote a piece in *Berlingske Tidende* headlined "The global balance problems are so great, that the risk of a global financial collapse is much greater than usual."

• When New York Federal Reserve President Timothy Geithner addressed the New York Bankers Association on April 5, he said, in Greenspanspeak, "The more critical role played by hedge funds and other non-bank financial institutions in credit and other markets, has the potential to magnify the impact of distress in those institutions on market dynamics and liquidity if counterparty risks are not managed appropriately." Reuters didn't think it necessary to translate. This is the third time this year that Geithner has made such warnings.

• Vice Chairman of the Institute for International Finance Bill Rhodes was quoted in the *Financial Times* that same day, talking about the prospect of an Ibero-American market crash: "We are in a situation similar to that which existed in the spring of 1997, when threats existed to market stability and a lot of people didn't want to see it."

• A writer for the *Prague Post* noted that "oil price increases have preceded nine of the world's ten recessions since World War II." Oil, now hovering around $70 a barrel, will likely hit $100 by the end of the year, according to several petroleum analysts he cited.

• International Monetary Fund Director Rodrigo de Rato, speaking at Harvard on April 4, warned of growing "global imbalances." Some policymakers, he said, believe global imbalances can either persist indefinitely or dissipate over time. "I find these views optimistic to the point of willful blindness." said. The most visible problem, he said, is the large U.S. current account deficit. Should financial markets force an adjustment, the dollar could be sent sliding, and push up U.S. interest rates. He specifically mentioned a bust in the U.S. housing market as a trigger. To get his full remarks, go to imf.org.

• A report prepared by the Economic and Financial Committee, of the European Union finance ministries and central banks, warns of a systemic disruption of the world's monetary system. The report, which the April 7 *Bloomberg News* reported was "confidential," said that hedge funds can be "a source of systemic risks," and that regulators should "continue to monitor possible threats."

• In a working paper dated April 2006, the Federal Reserve Bank of Atlanta concludes "there is reason to be seriously concerned about potential future social costs associated with the systemic risk emanating from Fannie Mae and Freddie Mac and that this risk largely arises from the institutions' highly-leveraged investment portfolios" of mortgage-related debt. It describes the dimensions of the systemic risks posed by Fannie/Freddie's holdings, "the two largest portfolios of U.S. residential mortgage debt." "These portfolios are highly leveraged, subject to little market discipline, and concentrate the responsibility to manage a large amount of mortgage-related interest-rate risk in only two institutions." What's meant by highly leveraged? In this case, equity less than 4% of assets.

• The April 10 *San Diego Daily Transcript* reported on a Federal Deposit Insurance Corporation (FDIC) forum last month that focussed on "scenarios for the next U.S. recession." It cited three key risks: energy price spikes, a housing slowdown, and mounting housing debt.

• The recent warning of a dollar collapse by the Asian Development Bank continues to get coverage, most recently in an April 10 Internet posting by Reseau Voltaire. The ADB told East Asian nations to somehow prepare for a crash as the U.S. trade deficit grows, and interest rates climb.

• Citibank Vice President Michael Andrews on April 11 backed up former Treasury Secretary Robert Rubin's earlier warning that the United States must correct its economic policies. Speaking at a Washington conference on Thailand, Andrews was asked by *EIR* to comment on the recent speech by Rubin, warning that failed U.S. economic policies were driving the dollar towards a collapse. While the audience tittered, Andrews responded most seriously, saying that, while his friend of 22 years was not speaking for the Bank, Rubin was "sending out a warning shot, that U.S. economic policies must be reformed, to contain the debt, and deal with the imbalances."

• All this was gelled into a literary reference by Gerd Haeusler, head of IMF's International Capital Markets Department. The "dark side" of the housing sector bubble, he said at a Bank of England press conference on April 11, is the risk sharing, visible only when asset prices start to fall, and Mephisto asks for his side of the bargain. "We are talking about a mine field of potential conflicts of interest or worse," it "could discredit a capitalist and market based financial system," and "backfire in an unprecedented way."

"A low level of financial literacy, combined with extensive risk taking, is politically an explosive brew," the IMF official concluded.