Banking deregulation: an assault on America's national sovereignty

by John Hoefle

On Nov. 12, 1999, President Bill Clinton signed the Gramm-Leach-Bliley "Financial Modernization Act" into law, effectively repealing restrictions on banking passed in the mid-1930s and in 1956. The best-known of these restrictions, and the one most hated by the international financial oligarchy, was the Banking Act of 1933, commonly known as the Glass-Steagall Act. This Act was passed under the direction of President Franklin D. Roosevelt, as an explicit measure to limit the power of the international bankers over the U.S. economy. As such, it was a decidedly *political* act, an assertion of national sovereignty, and was widely understood to be so by both the bankers and the U.S. population.

The Gramm-Leach-Bliley Act has nothing to do with bringing an "outmoded" regulatory system into the modern era, and everything to do with the global assault by the British-centered financial oligarchy on nation-states around the world. The repeal of Glass-Steagall is just as much a political act as was its passage. The issue is who runs the country: the financial oligarchy or the elected government.

The bankers' claim that they are unfairly hampered by overly restrictive regulations is more than absurd: It is an outright lie. For proof, one need look no further than the extraordinary level of off-balance-sheet derivatives bets of the big banks. Chase Manhattan Corp., with $31 in derivatives bets for every dollar of assets, is indicative of the extent to which the U.S. commercial banking system has been turned into a speculative casino. Far from being over-regulated, the inmates are running the asylum, and their alleged regulators.

No nation is sovereign, which does not control its own credit. Alexander Hamilton, the first U.S. Treasury Secretary, understood this, and used the credit-generating capacity of the young United States to build the country up to the point that it could enforce its independence from Britain, and become a beacon of hope for the peoples of the world. The financial oligarchy also understood this, and has fought a continuous battle to force the United States into a British-style system, where the economic royalists control government finances. Under the British System, the government does not issue sovereign credit, but rather borrows money through the oligarchy's financial markets.

The distinction is crucial. Under Hamilton's American System, the Federal government issued credits to the productive sector, providing funds to increase those activities which create wealth and provide for the General Welfare; the banks were merely intermediaries between the government and the people. Under the British System, the government borrows money from the oligarchy's financial markets, giving the oligarchs substantial control over government expenditures, and forcing the government to give the oligarchs a cut of every dollar of Federal spending.

To hide the strategic nature of deregulation, the oligarchs and their flunkies attempt to portray the repeal of these essential protections as "technical" in nature, merely a matter of updating old and largely irrelevant laws, to bring the law into the modern era. Naturally, they claim that the laws should be changed not to benefit the banks, but to benefit the public. They're just looking for ways to save money for the "little people," they claim.

Sen. Phil Gramm, the Texas Republican who heads the Senate Banking Committee (and the Gramm in the Gramm-Leach-Bliley Act), pushed this line in an Oct. 22, 1999, press release announcing that the Senate, the House, and the Clinton administration had reached an agreement on the deregulation bill.

"The financial services modernization legislation is the most important banking legislation in 60 years," Gramm asserted. "The people it will benefit most are working families. . . . The hallmark of the bill is that it will make an array of financial services to every American consumer that will provide lower prices and one-stop shopping at financial supermarkets in every city and town in the country."

But Gramm (whose wife, Wendy Gramm, significantly deregulated the derivatives markets during her stint as head of the Commodity Futures Trading Commission) is at heart an oligarch, or rather an oligarch wannabe, who prefers the British System to the American System. In September, Gramm issued a press release complaining about the Clinton administration's attempt to protect the Community Reinvestment Act, which Gramm vociferously opposed. The administration's action, Gramm fumed, "shows how vulnerable a regulatory agency is when part of a politically driven entity like the Treasury Department Regulators exert extensive power as it is. When politics is injected into the regulatory process, as happened in the Comptroller's office, the process becomes abusive. This is vivid evidence of the danger posed

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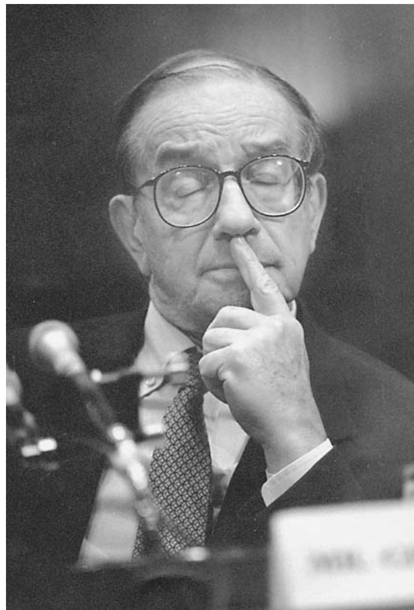
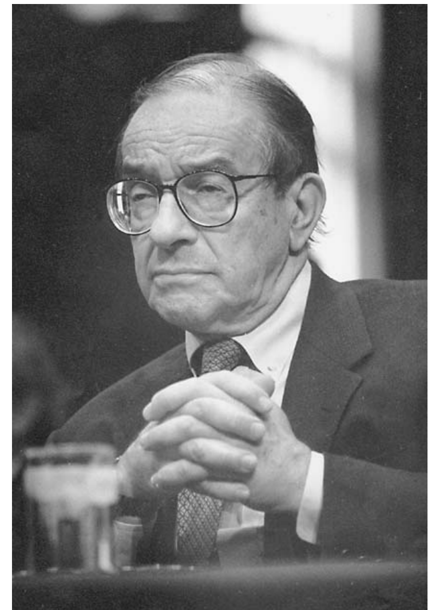



Federal Reserve Chairman Alan Greenspan has presided over the deregulation of the U.S. banking system, helping to create the biggest financial bubble in history. Now, the repeal of the Glass-Steagall Act removes one of the key remaining points of regulation, which had protected depositors from the manipulations of Wall Street.

by the administration's proposal to take regulatory power away from the independent Federal Reserve and give it to the Treasury Department. The proposal is a political power grab that must be defeated."

The trick used by Gramm and other mouthpieces for the oligarchy, is to pretend that the oligarchy does not exist, and blame all problems on government. In such a view, individual freedom is expressed through the "free market," and all attempts by government to regulate the market is an assault on that freedom. Thus, protecting the power of the banks to do whatever they want, is transformed into a battle for the rights of the "little people" against "oppressive government." The battle to increase the ability of the big international banks to loot the population is transformed into a fight for "consumers" to have access to "one-stop financial supermarkets." The "little people" who win such battles, win the right to become human sacrifices.

Past the point of no return

For the past few years, the commercial banks, investment banks, and insurance companies have all heavily lobbied Congress for deregulation, with that lobbying backed by significant campaign contributions. Each year, Congress was prepared to give the financiers what they wanted, but the three sectors could not agree on the precise terms of a bill. That is, they all wanted to make sure that the new law favored them, over the other two. Finally, in the autumn of 1998, with the global financial system in a near meltdown, an agreement was reached and a bill made its way through Congress, only to be blocked by Senate Banking Committee member Phil Gramm. The word in Washington was that then-Senate Banking Committee Chairman Alfonse D'Amato (R-N.Y.) was likely to lose his reelection bid; if so, Gramm would inherit the chairmanship of the committee, a lucrative position with banking reform on the agenda. D'Amato lost, and the rest, as they say, is infamy.

The other obstacle to the passage of the deregulation bill was the insistence of Treasury Secretary Robert Rubin that the new powers to be given to banks be placed inside the banks themselves, instead of in holding-company affiliates. The issue was one of regulation: The Treasury's Office of the Comptroller of the Currency regulated national banks, whereas the Federal Reserve regulates the holding companies. Rubin wanted the government, rather than the Fed, to control the new activities. Rubin stepped down in July of this year, but the Gramm-Leach-Bliley bill concedes some of his demands.

The question remains as to why the banks, securities firms, and insurers finally reached an agreement, after years of infighting. The answer is simple: fear, the fear that their system was spinning out of control.

The problem facing the financiers can best be illustrated by Lyndon LaRouche's Typical Collapse Function (**Figure 1**). The top of the three curves, financial aggregates, represents the hyperbolic growth of financial claims against the economy—stocks, bonds, debt, derivatives, and other forms of paper—which must ultimately be paid. The middle curve represents the monetary aggregates, money created by the central banks to provide the liquidity necessary to keep the pyramid scheme going. The lower curve represents the de-

FIGURE 1
A typical collapse function

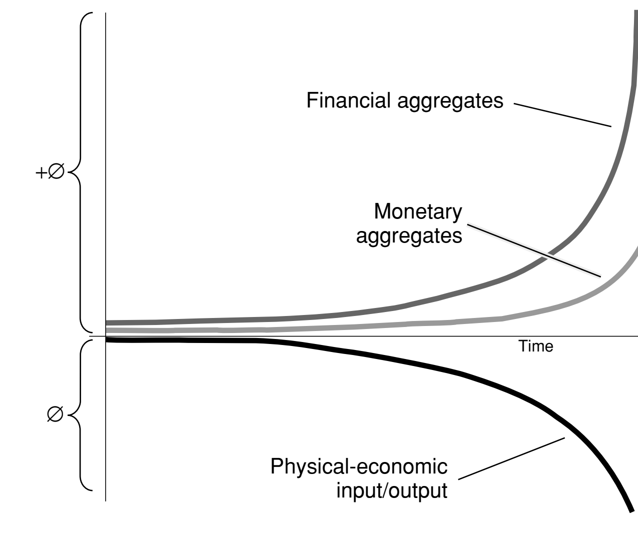
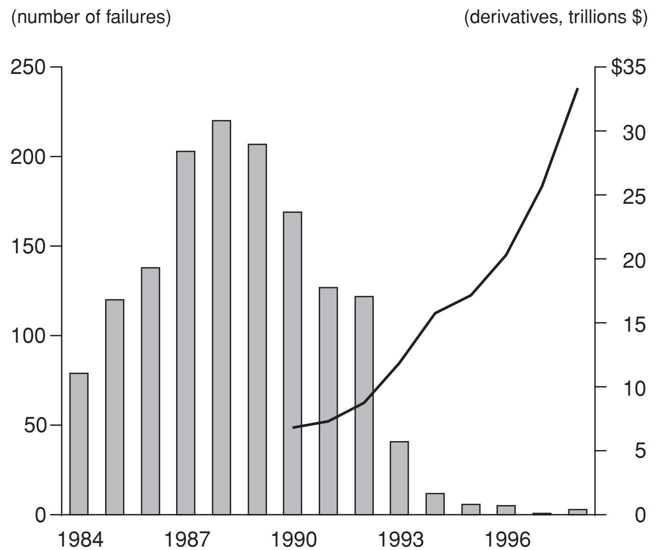


FIGURE 2
Bank failures and derivatives



Source: Federal Deposit Insurance Corp.

cline of the physical economy, as measured by production and consumption of a market basket of necessary goods, calculated not in dollar terms, but in units per capita, per household, or per square kilometer, as appropriate.

These are not three independent curves, but rather represent one function: As the financial aggregates grow, the monetary aggregates increase to provide the liquidity to roll over the rising level of unpayable claims; the money to support this growth is taken out of the productive sector, causing the market basket of physical goods to shrink correspondingly. The relationship is that of a parasite and its host—the parasite grows by feeding off the host, just as the bubble grows by looting the physical economy.

The problem with such a system, is that the faster the bubble grows, the faster it destroys the physical economy upon which it ultimately must turn, for payment of its claims. Eventually it reaches the point where pumping more derivatives into the bubble, fails to prolong the life of the system, and a breakdown begins.

In the late 1980s, the U.S. banking system collapsed with the popping of the real estate and junk bond bubbles. Not only did the S&L sector collapse, but the commercial banks started failing at record rates (**Figure 2**). To counter this, the bankers and the Fed made a fatal mistake: They jumped whole hog into the derivatives market. While the Federal Deposit Insurance Corp. (FDIC) keeps no derivatives figures for years prior to 1990, the graph shows a striking pattern; it was the flight into derivatives, helped by a flood of central bank liquidity and a "see no evil" regulatory policy, which created the illusion that the banking system had recovered.

Derivatives, despite all the hoopla about "risk management," are essentially a vehicle for rolling over the unpayable claims of a bankrupt system, into even larger and more unpayable claims. The use of derivatives has turned the global financial system into a giant casino, which must ultimately collapse.

LaRouche, or bust

That collapse, Lyndon LaRouche observed recently, will take one of three forms: deflationary collapse, in which hundreds of trillions of dollars of paper values simply evaporate in a chain reaction; a hyperinflationary blowout, in which the money suddenly loses its value, as happened in Weimar Germany; or a breakdown of civilization into widespread warfare. Whichever form the collapse takes, the financial system has entered a boundary condition from which it will not, it cannot, recover. As the recent debacle at the World Trade Organization meeting in Seattle, and the moves in Germany and France to resist globalization show, the political power of the oligarchy is beginning to crack. The attempt is being made to hold the financial system together at all costs, to prevent the chaos which will occur when it breaks, but the measures used in the past to hold the system together no longer work. Pumping up the bubble—the aim of deregulation—will only make matters worse, and bring about the very collapse the bankers fear.

The only alternative is the LaRouche proposal, of putting the financial system through a bankruptcy reorganization, then using sovereign credit to rebuild the productive sector. We can build our way out of this mess. It's LaRouche, or chaos.