

# Glass-Steagall or Financial Bust: The End of the System

by Susan Welsh

Sept. 24—The trans-Atlantic banking system is coming to and end, one way or another, as *EIR* has warned. There are basically two options ahead: First is Federal Reserve Chairman Ben Bernanke's hyperinflationary policy, announced Sept. 13, of pouring *unlimited hundreds of billions of dollars, indefinitely*, into the banks deemed Too Big To Fail (TBTF), in what one commentator called "playing their final hand" (Examiner.com, Sept. 13). That way lies disaster. The second option is for Congress to *reinstate the Glass-Steagall law*, an essential first step toward restoring sanity to the banking system.

Authoritative analysts from outside the banks and the government are increasingly stepping forward to demand the sane option. A faction within the British financial establishment started the drumbeat in early July; it was picked up by some U.S. publications, then by former Citibank CEO Sandy Weill. But Congress did not nothing, the Administration adamantly opposes Glass-Steagall, and the whole issue was once again relegated to the back pages of news publications.

Rep. Marcy Kaptur's (D-Ohio) "Return to Prudent Banking Act," HR 1489, which calls for a return to Glass-Steagall's separation of commercial banking and the securities business (speculation), still has only 81 sponsors in the House, out of a total of 435 Representatives, and has not been brought to the floor for debate.

But that may be changing. For one thing, Bernanke's Sept. 13 announcement may have made some people realize just how desperate things are. As we re-



*Rep. Marcy Kaptur, sponsor of HR 1489, a bill to reinstate Glass-Steagall.*

ported last week, former Fed governor Kevin Warsh pointed out that if the Fed really believed the economy were improving, even slowly, "I don't think they would have decided to be nearly as aggressive as this."

While her bill has hitherto generally been blacked out of the establishment press, Kaptur herself was given space in *US News & World Report* on Sept. 17 to describe it and urge support for it. Only as "Wall Street gained political and economic influence," she wrote, were they able to overthrow Glass-Steagall through the Gramm-Leach-Bliley Act in 1999, the enactment of which became "a clear signal that Wall Street was in charge." She concluded, "Congress must act and reinstate Glass-Steagall so the public can be assured that the economy is working for them, not just for Wall Street's CEOs."

## A New Crisis Is Coming

FDIC board member Fed Thomas Hoenig—a strong proponent of Glass-Steagall—briefed the Exchequer Club in Washington on Sept. 19. If big U.S. banks are not forced to sever their investment arms from traditional banking in a modern version of Glass-Steagall, he said, “the behavior and practices leading to this crisis will soon re-emerge, and these highly complex, more vulnerable firms will have an even more devastating effect on the economy.” Hoenig, former chairman of the Kansas City Fed, added that “activities leading to the crisis continue today—and continue to be subsidized—well after the lessons should have been learned.”

The nation cannot effect meaningful fiscal reforms, involving taxing and spending policies, if the public does not trust its government and financial institutions, Hoenig emphasized.

In a speech on Sept. 14, to the American Banker Regulatory Symposium, Hoenig also called for the separation of banking and brokerage.

## ‘Frankenstein Monsters’

Hoenig’s message was echoed in large part in an interview given by Neil Barofsky, the former Special Inspector General for the Troubled Asset Relief (TARP) bank-bailout program. “The real issue is the potential for another financial crisis, because we haven’t fixed the core problems of our financial system,” Barofsky told Hera Research (kitco.com). “We still have banks that are too big to fail.... The big banks are 20-25% bigger now than they were before the crisis. The ‘too big to fail’ banks are also too big to manage effectively. They’ve become Frankenstein monsters.”

When asked what it would take for U.S. lawmakers to finally take on the TBTF banks, Barofsky said: “Some candidates have made reforms like reinstating Glass-Steagall part of their campaigns, but the size and power of the largest banks in terms of lobbying campaign con-



*Thomas Hoenig: Glass-Steagall will restore trust in government.*



*Neil Barofsky: “It may well take another financial crisis before we deal with this.”*

tributions is incredible. It may well take another financial crisis before we deal with this.”

## ‘Top Priority’

Scott Shay, the CEO of Signature Bank, addressed “The Absurdity of Too Big To Fail Banking” in an article for AmericanBanker.com on Sept. 20. “Once the election is decided and Congress gets back to work, fixing the banking system and reinstating Glass-Steagall should be the highest priority,” he wrote.

Shay took apart the basic arguments of the bank lobbyists who claim “that the rise of TBTF banks and the 1999 repeal of Glass-Steagall were actually good for the country.”

Addressing the common argument that the

repeal of Glass-Steagall did not cause the crisis, and that Glass-Steagall would not have stopped it, Shay argued that “the Glass-Steagall repeal was not the sole cause of the financial crisis but certainly a contributor”; long before its “technical” repeal, its provisions had been overturned, with “the permission regulators gave to the banks for the ‘cultural consolidation’ of commercial and investment banking.” It was (and is) Citibank and Bank of America’s investment banking exposure

that needed bailing out, before the mortgage crisis broke.

In challenging the fraud that big banks are better for the economy, Shay says: “Small and medium-sized banks are more effective at making loans to the small and medium-sized companies, which are the primary job creators in the U.S.... [W]hat is good for the big banks is not necessarily good for the economy and the growth of jobs.”

“If policymakers can get the structure of the banking system right, there will be less of a need for the volumes of devilishly complex regulations, which are being created almost weekly.... Once the election is decided and Congress gets back to work, fixing the banking system and reinstating Glass Steagall should be the highest priority.”