II. LaRouche's Four Laws

Applying the Principle of Hamilton To Today's Crisis

The following edited interview with EIR*'s Paul Gallagher was conducted on November 21, 2016.*

Jason Ross: I'm very happy to be interviewing today Paul Gallagher, an economics editor of Executive Intelligence Review. Paul wrote the "Frequently asked questions on economics," that we have posted on the LaRouche PAC website. You can find that on larouchepac.com/econ-faqs. This comes up because we have a lot of questions that are coming in about Glass-Steagall, about economics more generally, and took an opportunity to condense and pull them together.

Let me start out by asking Paul the first of these frequently asked questions. You take up something we hear somewhat frequently, where people say, "Well, Glass-Steagall wouldn't have done anything about the financial crisis, because the banks that failed were not combined commercial investment banks anyway, they were just investment banks." What do you say to that?

Paul Gallagher: Yeah, that is the argument that has been adopted from the very top down, including the President, the Treasury Secretary. I think the first thing important to understand is that most people support Glass-Steagall out of a question of justice. Right? That these really, now immense, many, many, part bank giants have, right up to now, continued to use their power to commit so many immoral and, in many cases, illegal banking practices, from fixing interest rates to fixing foreign exchange rates, to fixing the derivative markets—all of them have been found and have admitted to massive mortgage security fraud, and the list goes on and on, and they are still doing this. As the Wells Fargo episode has shown, it's time to break them up, take that power away from them. That's really what many millions of people understand as necessary and done through Glass-Steagall uniquely. . .

There is a more serious question involved here,

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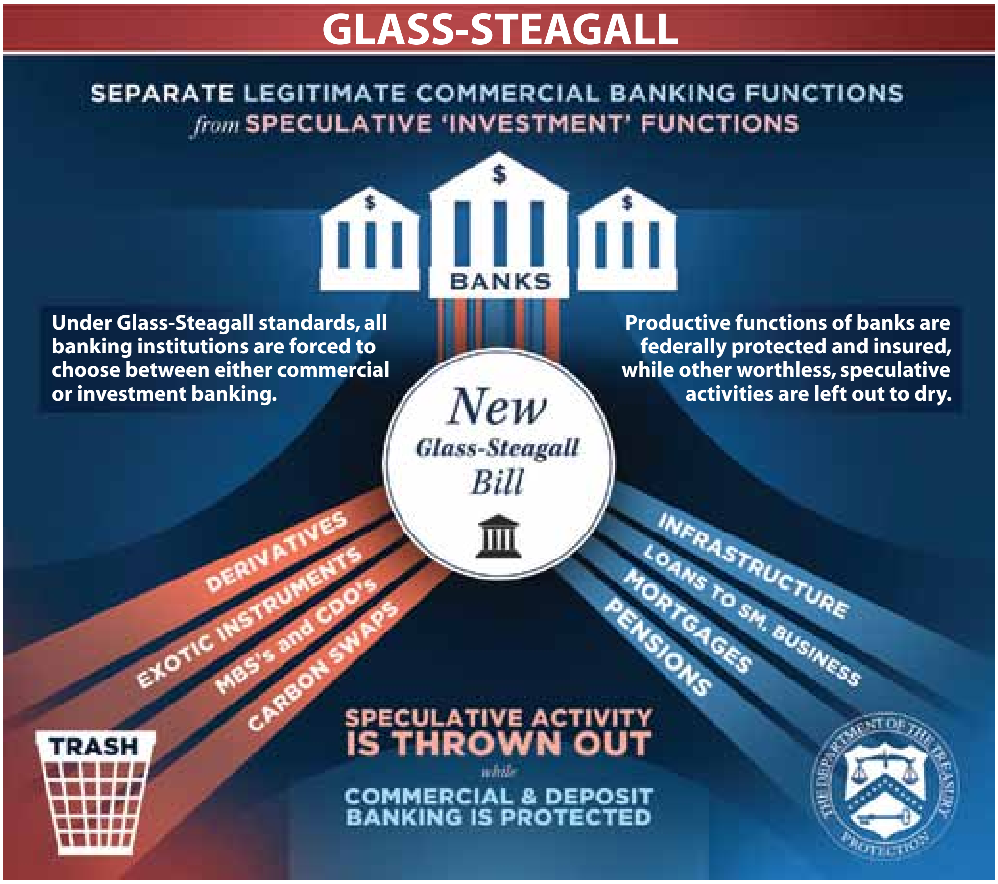
Bank run on Northern Rock, 2007.

which is what did cause the global financial panic, and that really comes down to really only ten years after Glass-Steagall was finally gotten rid of, approximately a third of the huge deposit base of these very big banks, which is in the range of ten trillion dollars, approximately a third of it, within a decade after the end of Glass-Steagall, had migrated over into securities activities, into broker-dealer activities, into hedge fund owning and maintaining hedge funds. All of the commercial banks, the biggest banks got completely out of their lane over into the lane of securities speculation, the whole casino. So they blew, they puffed up that casino by the fact that they had such a huge deposit base, and they were pulling out of their lane into the shoulder over here, and that meant that when one major financial institution failed, no matter what it was, it happened to be Lehman and AIG, but no matter what it was, they were all going to fail. Because the commercial banks which have our deposits have gotten so far out of their lane into the securities casino.



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The major banks are still doing it. They had each, maybe a hundred to two hundred subsidiaries in 1995, the Federal Reserve of New York did a very good study of this. By 2011, each of these giants had three or four thousand subsidiaries, rather than one or two hundred; all these little offshore securities units, special purpose vehicles, derivatives contracts, bets, etc., and that's what the deposits were going into…

We have got to have Glass-Steagall, and we are completely uninterested in preventing investment banks from failing. It might be useful if a number of them and a lot of their individual units were to fail. That is not the concern of restoring Glass-Steagall; it's putting the banks that handle the mass of deposits, the commercial banks, putting them back in their lane, which is providing credit to households, businesses, individuals, revolving credit in the form of auto loans, credit cards, mortgages, this sort of thing, and preventing them from getting out of their lane into unsound banking. That is what the preamble of the original Glass-Steagall Act said.

Financing an Economic Revolution

Jason Ross: On the subject of moving forward, on creating an economic recovery, because a large part of the vote we just saw with the presidential election was a vote in opposition to the destruction and the lack of vision of the Bush and Obama Administrations and the threat of that being continued under Hillary Clinton, in this context, LaRouche has written what he calls Four New Laws to Save the USA Now, which is an appendix in the book Hamilton's Vision, which includes Hamilton's four major economic writings. In that report, Mr. LaRouche says that, given the breakdown crisis we are facing internationally, there are four specific cardinal measures which must be taken. One, Glass-Steagall;

two a system of top down and thoroughly defined national banking, three, the purpose of that credit system is to generate high productivity trends in improvements in employment as through increased energy flux density application in the economy, and fourth, the adoption of a fusion crash program, to reach that next level of economic power seen in the potential of the nucleus through nuclear fusion.

In the context of this, and the idea of saying let's get some growth, let's get some projects going, the *New York Times* published a front page article on November 18th. The article is called, "Trump sized ideas for a new Presidency; build something inspiring." It goes through how Roosevelt built a lot of things, they are still with us today; in contrast the Obama Administration's stimulus program left no program any one can name, nothing is really happening. It says that by investing in things like rail, etc., airports and things like this, that Trump could create an economic recovery.

The New York Times says that, since interest rates are low, the best way to finance a public works program would be for the government to borrow most of the money from investors. Is that the best way to finance a public works program? Since interest rates are low, is it possible for the government to simply borrow money in a standard way to pay for these projects? Would that work?

Gallagher: Now it wouldn't. I have to say I don't really know what they mean by borrowing a trillion dollars from investors. The way in which—the model of what they are indicating might be the Reconstruction Finance Corporation of Franklin Roosevelt, which certainly was successful over a twenty year period of time, which borrowed about fifty billion dollars over that period of time, from the American public. These were not in any way deals for private investors to set up vehicles; rather the Treasury simply borrowed dedicated Treasury Bond issues for the Reconstruction Finance Corporation to engage in all of the New Deal support that it did, and that amounted to fifty billion, perhaps in our current dollars, five hundred billion [dollars].

We need ten times that much investment in new infrastructure. We can get into that a little bit more, in terms of what we really need it to be, and what its character really needs to be, this new infrastructure that is being discussed now, but that amount of borrowing straight out in a short period of time against an atmosphere in which, since election day, the long term interest rates are already rising pretty fast, the Treasury bond ten years interest rate has already gone up from about one and three quarters percent to almost 2.4 percent in almost two weeks. That's a really rapid increase, and that was just at the very idea that an incoming Trump administration was going to spend a lot of money, both on defense, increased military spending and also infrastructure.

I'm not at all convinced that that is what the Times means, to simply borrow a trillion dollars from the public by the Treasury, from the international public, because Treasury securities are sold to countries all over the world, but that would be very difficult to do now without there being very rapid increases in the interest rates, and no one in the Times coverage here gives any suggestion of how it would be paid back, or how the debt service on this borrowing would be handled. Alexander Hamilton's voice is always in your ear, saying that public debt is a public blessing if the means for its extinguishment have been definitely provided, which is certainly not the case here.

That's also not the case with the plan that has been circulated by a California professor and a New York billionaire who may become Trump's new Commerce Secretary; that plan is also quite unworkable. What we have to compare it to is the method of generating credit for increased productivity that Alexander Hamilton pioneered, invented, essentially, because that method was used over and over again—John Quincy Adams with the second National Bank; Abraham Lincoln with the greenback policy in the 1860s; Franklin Roosevelt with the Reconstruction Finance Corporation. This method continued to be successful and accounted for the waves of really new infrastructure over the course of the nineteenth century and the middle part of the twentieth century, which really made this country the pre-eminent industrial and scientific power.

We had productivity increases in the most developed measures of productivity from roughly 1935 to 1965, which have never been equaled since the 1870s. That was under the impact of the New Deal, the credit measures necessary to build up the military for World War II, the actual manufacturing investment strategies which the Roosevelt Administrations carried out in order to mobilize the US economic power, which won World War II, and then the Kennedy Apollo Project centered investments in new infrastructure and in new capital investment in industry. These things produced a wave of very rapid increases in productivity through

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Chinese high speed train leaving Shanghai's Hongqiao Station.

the middle decades of the twentieth century. There hasn't been anything like that since.

Ross: You have also pointed out that even if everything the *New York Times* proposed was financed somehow, it is aiming far far too low. This amount of a trillion dollars—you have pointed out that China is already spending that much money, but the US needs far more than that. What would a real recovery look like? What ought we to be doing in the United States?

Gallagher: We could get into a lot of detail on that, which we don't have time for, in terms of individual industries, but to give one example, or to give several examples and then to zero in on one, we need a new water management and water creation infrastructure for the entire western half of the continent, which everyone knows but tends to look away from in a policy sense. The whole western part of the United States, and Canada, as well, are in constantly advancing drought, verging on desertification, and there is no sign of that drought being alleviated, perhaps for decades into the future. These include the most productive areas of the country, California most notably. Water has to be provided both by a really modern, well designed system of moving it from the places that it is falling in great excess, like Alaska and northwestern Canada, and also creating it by desalination, particularly nuclear desalination all along the coasts in that western half of the continent, and by the more advanced and experimental methods which seem to be working of atmospheric ionization in order to bring atmospheric moisture from the ocean over the land and cause it to fall.

That is one example.

We need a 25-35,000 mile national network of high speed rail. We have no capability now of building that. We need to be building a moon colony, and NASA doing all the preparations as other countries are doing only on the drawing board, but would like to collaborate with us, in order to really go back to the moon in preparation for exploration of the solar system—and also potentially to find materials and fuels which are entirely absent here, like helium 3, which are there on the surface of the moon. We need to generally expand NASA, which, after all, is a transportation infrastructure program, right? It happens to be our transportation to get human beings out into the solar system.

We have to increase the power generation capacities of the United States by a great deal; we have to make big changes in industry. But if you look at just the high speed rail component of it, China, in ten years, has put into operation a national network which is still growing rapidly and which is already 12,000 miles of high speed rail. Japan has also shown the capacity to build it very rapidly. We don't have that capacity at all, not currently. We don't have the capacity either to provide the power to a nationwide system of electrified high speed rail—the transformer systems, the pantograph transmission either to the car, to the engine, if it's high speed rail, to the track if it's maglev rail; we can't produce that. The justification of rails over long distances, with extremely tiny tolerances needed in order to handle trains travelling at really high speeds, we don't have the ability to produce those; we haven't even started on it. Clearly, for some of the absolute necessities that we need, we want to turn and collaborate with the countries, particularly China, which are already doing them, and doing them better than they've been done anywhere else in the world; those are the kind of infrastructure investments.

In this *Times* article, by contrast, the biggest thing they were suggesting was a high speed rail line in California, and another one from Washington DC to Boston.

That’s not the kind of thing that will really revive the US economy or the productivity of the labor force in the US economy.

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Greenback from 1861.

National Banking

Ross: Let me switch to some of the questions we have been getting from our supporters, our organizers, some of the questions that came in on You-tube over the last couple of weeks. A number of people asked about national banking and the Federal Reserve. They said, how can we have both the national bank and the Federal Reserve? What will end up happening with the Federal Reserve? Let me put two questions together and see what you think. Another question that came in was about the question of money, about Lincoln’s greenbacks, debt free money, is this a meaningful concept? Does this have any relevance to what we have to do today? What can you say about national banking, the Federal Reserve and money?

Gallagher: Let’s keep it simple; let’s say what Alexander Hamilton did to create the first national bank and to make it successful, among other things to produce the earliest investments in what was then new infrastructure, particularly canals, ports, roads, and also the experiments in rapid manufacturing technique development which Hamilton was himself in the middle of, particularly Paterson, NJ, Hamilton Township, these were places where new manufacturing techniques were being developed, very skilled artisans from European countries, particularly Scotland, were being imported, literally, by Hamilton’s agency in order to spread the best techniques in European manufacturing into the United states.

How did he do it? He took the debt, there was the famous argument, which he won, whether the United States should honor all the debt of the period of the Articles of Confederation, the Revolutionary War debt, the debt of the new states. He did assume it all; the Treasury did assume it all. The way he did it though, was to have it invested over a period of time into a new Bank of the United States, which took in this debt, much of which was not being paid, but it was debt for which the United States now had responsibility. It took in this debt, made it its capital, and exchanged it for much longer term, what we would call now preferred stock in the new national bank that Hamilton asked Congress to create, and they did create, on the basis of his report.

He then had a bank which was capitalized which also had the support of certain foreign lenders, particularly Dutch banks who organized the five million dollar loan to capitalize this bank; he also made sure that the tax income necessary to guarantee the interest on that debt was passed. They were new taxes, particularly on spirits, on liquor, and there also were new revenues of the post office, and that was the basis on which Hamilton saw already, when he first wrote to Congress about what are we going to do with all this debt, and many people were saying, the important thing is to try to pay the principle, why don’t we just discard the interest, why don’t we just say, we’ll write it down, or we’ll pay very little of it or no one will care about it. Hamilton said the interest is the important part. If you can replace that debt with much longer term principle, and make sure that you actually pay those interest rates, that you provide the means to do that with taxation, then you can expand what was previously merely debt into a much larger amount of investment capital being deployed by that bank, and that is how he did it.

In 1816, after the war with the British, the Quincy Adams administration realized they needed that bank again, it had been allowed to lapse, so they drafted the Second National Bank, exactly the same method and structure. In 1841 the Congress passed a third national bank, after Andrew Jackson had become furious and done away the second one. That was vetoed but very shortly after that Abraham Lincoln found a way to do that in the beginning of the Civil War, which essentially made a new national banking system, rather than simply a national bank, by tying all of the banks in the new Federal system around the country to a new issuance of US debt, which again was over a long period of time, in which these banks had to buy, hold and actually hold at the Treasury, as part of their of their capital in order to be part of the national banking system.

Lincoln created a national banking system, and on that basis printed greenback currency which was tremendously successful in terms of not only what the war required, but all of the other things which followed—the transcontinental railroad, the state college system around the country, the steel industry, all of the things which made us a first power by the end of the century came from Lincoln's banking reforms and greenback policy.

National banking now would simply mean that, in effect, holders of treasury bonds, this is not new debt, but bonds the treasury has already issued in recent years, the holders of those bonds, which of course include some foreign countries that hold a great deal of it, would be offered the opportunity to place those treasury bonds into a new national bank for industry and for manufacturing and infrastructure as its capital. In exchange for that, those bond holders would have the opportunity to get, instead, longer term preferred stock, essentially, in a new national bank, whose purposes included this kind of real frontier infrastructure that we were talking about.

The means of paying the interest, which would have to be higher than the current zero interest rate environment—which has really been a very destructive one for the economy, for the banking system—the means of paying the interest, although the Treasury would be guaranteeing the long term debt of this new national bank, the bank would have to pay it and would have to have the means to pay it, either in a new tax or by the assignment and perhaps increase of a current tax to the bank, as its income. Then the bank of course has to have working capital, has to have funds, not simply stock but funds to initiate, to lend to initiate these projects, and that it could do either by using its stock and discounting it at the Federal Reserve, in other words getting the Federal Reserve to effectively loan the bank money against the stock that it had, or better, if holders of a trillion dollars worth of treasury debt take that opportunity and place it in the new national bank as capital, and in exchange take the long term preferred stock of this bank, then the Treasury, if it's a trillion dollars, the Treasury is then in the position to print a trillion dollars in treasury notes.

That is what a greenback is. That is how the Lincoln policy worked. Those treasury notes would go to that bank and be used as its funds for setting all of this investment in motion. And again, since we need, particularly, the new Silk Road, the investment policy, the development and infrastructure policy of China in particular in building all of this infrastructure along the New Silk Road, since we need to join that, it is an ideal circumstance that a trillion dollars in existing treasury debt is held by China. Another trillion is held by Japan, which is the world's number two infrastructure building power and close behind China, and those two are ideally in a position to invest their holdings of treasuries in this new national bank for manufacturing and infrastructure, and therefore to become not only cooperating builders of what we have to do, but also become cooperating issuers of the credit, and we would be cooperating with them also in issuing credit for infrastructure projects outside the boundaries of the United States, because some of the greatest of these projects, like crossing the Bering Strait and connecting high speed rail in this continent to high speed rail in Asia, obviously requires the cooperation of several countries, and it requires these kinds of things, these kinds of things require the cooperation in credit and funding of several countries as well.

This bank becomes the connection to the Asian Infrastructure Investment Bank, the Silk Road Fund, the BRICS Bank, the other new international credit agencies which have been created by the BRICS, particularly by China, in order to get this kind of really big project done.

Ross: When you brought up the creation or assignment of an existing tax as the way to make good on the bank, on what Hamilton had done with the public credit in assigning a definite income stream which would make the interest payments and make the debt secure, it made me want to ask you about—well the Tennessee Valley Authority paid back its loans by selling electricity and things like this. The administrator of the TVA, David Lilienthal, in a book he wrote about his experience with it, asked, "Did the TVA pay for itself"? Yes, it very directly did that by generating fees and income that way, but, he said, even if that had never happened, just the increased income tax in that region of the nation

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TVA's Ocoee Dam No. 3, on the Ocoee River in Polk County, Tennessee, USA, 1948.

as a result of the TVA, that would be enough to pay for the project as well. What I was wondering about is, does this put this financing, the use of a tax, does this make it possible to finance projects that otherwise people might say on a project-by-project basis, "this won't directly make money and therefore it would be off limits." Does this enable that?

Gallagher: This is why, in the article I just wrote for the *Hamiltonian*, I attacked user fees, because these kinds of great projects do not pay for themselves in a short period of time. The TVA eventually made a profit over an extended period, but that was never its purpose. And the purpose of a new national bank for infrastructure and manufacturing now, is not that that bank should make a profit over any short term or even decade, fifteen year, twenty year period of time. It's that productivity, throughout the economy, throughout the labor force be raised, which obviously will be accompanied with—everyone understands that that will be accompanied by considerably more tax income generally, and that is how the national purposes of the country are met.

I think what Lilienthal actually said in that final report was that the purpose of the TVA was to pursue the national interest of the United States. It happened eventually to make a profit, but that was not its purpose and that's not the purpose of a bank like this; it simply must be put on a sound basis for a relatively long period of time as having the income means to actually keep its debt sound, to pay the interest on its debt, to keep its debt sound. That cannot be based on user fees. If you have such a bank and you say it's going to be paid for by user fees, then immediately its managers will want to do the smallest—the way I put it in the article is, "Kennedy said we do these things because they are hard. We go to the moon, we send a man to the moon, we bring him back in this decade, we do these things not because they are easy, but because they are hard."

These are the major new infrastructure platforms we need to develop with this bank. If you have a bank that depends on user fees, it will do things that are easy. It will build or upgrade an airport here or there, it will put up a rail line only in the most crowded, most used corridor, between Washington and Boston, at best. It's going to build a new bridge that has tolls, and so forth. It's going to try to build a water project that immediately can generate water fees. It is not going to do what Kennedy said, these things that are hard, which actually make America a greater and more productive economy than it was before, because those kinds of things that are hard, as he called them, they don't produce this kind of flow back of revenue to the lending agency which provides the credit for it, or in that case to the Congress, which was funding NASA every year. It changes the economy; it transforms the economy, and the result is it's a bigger, more productive economy and there is more income. So NASA, the Apollo project and associated things, as has been well established, paid back to the economy ten to fifteen dollars to every dollar that was spent on it, but it didn't pay that back to NASA, it was an effect on the economy as a whole.

Hamilton simply said, this is what we are aiming for; he knew absolutely: the goal is productivity. His goal was new manufacturing techniques, advancing the productivity of agriculture as well as the rapidly spreading manufacturing capabilities, and that the bank could make that possible but the bank simply had to assure its investors that it was going to make their investments sound. For that, as he said, the means of extinguishing those debts have to be provided in the bank. And they have nothing whatsoever to do with the projects that will be carried out. A liquor tax had nothing whatsoever to do with the new roads and ports and canals and so forth that were built.

Ross: Right! I think this makes the point that there are objectives, or an opportunity to increase productivity, there are levels of social advancement that are only possible with the national involvement in the economy that way, not with individuals trying to make a profit.

Gallagher: Like the TVA. You can look at poverty maps of the United States, and of course the southeast quadrant of the United States has the worst poverty rates. If you look at a map by county of the United States, you see an area carved out of the southeast where the poverty rates are much lower, and that is the TVA. It's still the case. So it was not only that it transformed water management over that whole area, power production, rural electrification, and all these other things, but also libraries, it also raised up the living standards of the population in that area which were the lowest in the country at that time.

The New Global Paradigm

Ross: Let me just ask as a final question to summarize or wrap up as you see fit on the international question. You had brought up earlier we could not build a high speed rail even if we wanted to. You mentioned some of these other—the New Development Bank, the Silk Road Fund, the Asian Infrastructure Investment Bank—how will the US coordinate with these institutions? How are we going to fit in?

Gallagher: Well, it is fundamentally the policy of China and Russia, but in terms of capabilities both for building and for financing it is overwhelmingly the policy of China which has made what they call a "win-win" whole series of offers to countries all over Latin America, all over Asia, many countries in Africa, and that has become associated with the policy of the BRICS, or more particularly of China, India and Russia. This New Silk Road and the corridors across Eurasia which China has initiated the building of, this constitutes the potential for a global recovery from what has been extremely low growth of the whole world economy in the last decade or so, and most especially the absence of any growth in Europe, the absence of any growth in the United States.

Clearly there has to be collaboration in an effort of putting productivity back into the American economy, or putting the drivers for productivity back in, there has to be cooperation which is being offered now for several years by China in particular—join the Asian Infrastructure Investment Bank. Obama said no, tried to get everyone else out of it, everyone else went into it, but they are going into it, particularly the European countries, with very small contributions to the capitalization. If it is a question of the United States, how will we collaborate in that kind of rebuilding of whole new infrastructure platforms across Eurasia and in this country ourselves? We have no credit institution which is ready to collaborate on that in any way. We have the poor Export-import Bank and nothing else.

We have needed, number one, a complete policy change, getting Obama out of there. We have at least the indications from Trump during the campaign that he had an idea of big investments in infrastructure, an idea of restoring Glass Steagall, so there are indications of a change in attitude toward Russia and China, we'll have to see. But what we absolutely must have in order to make that kind of cooperation is a national credit institution like the ones China has been using in order to drive this development.

Even in recent weeks, three different countries in Ibero-America have upgraded their relations with China on the basis of major investments that its banks are making in those countries' development. They do this because they have major credit institutions, some of them in partnership with other countries, some are Chinese government banks. They have the basis for that credit underlying in the large foreign reserves that they have. We need to start by having such an investment vehicle ourselves, a national investment vehicle in the United States. Then it's very easy, as in the Marshall Plan, to link that vehicle to national credit institutions in many countries, and beginning by linking it to those of China and of the BRICS. Then we can both fund things here, jointly fund third country projects, and combine the joint issuance of credit with joint building because those countries are so far ahead of us, in recent years, in terms of the productivity of the way they have developed their infrastructure so rapidly.

Ross: Great! I think that's a pretty comprehensive view of many of the economic questions we are facing now. Thank you for being on the show today Paul.

Gallagher: Thank you!