Structural Greed: The 'Credit Crunch'

John Barker

There have been economic and financial 'crises' ever since I remember. For most people in the world financial crises are anything from an hourly to, possibly a more privileged, monthly experience. But this is not what is being talked of now which is instead a 'major event' in the richer part of the world involving sums of money beyond our ken; billions and trillions. The fetishistic notion of 'economic collapse' then gets floated. What does this mean when there are millions of malnourished people, and when vast numbers of people are continually scrabbling for a living in the 'informal economy'?

Such 'crises' in the richer world are often dramatized as fundamental, even terminal to capitalism by anti-capitalist socialists, and sometimes by excited financial journalists. So far it's been a history of crying wolf which makes a person wary about exaggerating what is happening now in this 'sub-prime/credit crunch' sequence. Most major banks, even those that have had to write-off bad debts often in the billions, have still made profits in the billions. Equally, corporate profits in the US-epicenter have been, in capitalist terms, healthy. And yet this 'crisis' is different to others of the last fifty years, both in reality and in the way it has been presented to the public:

• Its longevity. No sooner was this crisis being put to bed – crosses nailed through hearts, frankness and reassurance offered in the same breath – than up popped another write-off. In April 2008, the Term Auction Facility in the US was increased by $50bn and expanded the kind of assets used as collateral; precisely the kind of assets that precipitated the crisis. The Bank of England followed suit, though insisting the collateral were 'high-quality' assets. Similarly, the size of the write-offs involved seems to get bigger as time goes on.

• The expansion and extension of usury, seen in the sheer scale of credit in an era of securitization, much of it 'non-productive' but all assuming steady cash flows from those who borrow.

• Many of the bones of modern capitalism are now showing, such as the fragility of the valuation of collateral assets and their cash-flow 'assumptions'. How shaky its normally hidden infrastructure becomes when banks are afraid to lend to other banks.

• As a crisis of information in the era of the information technology revolution and with credit ratings agencies coming in for serious criticism it profoundly undermines capitalism's claim to be the only efficient assessor of risk and allocation of resources.

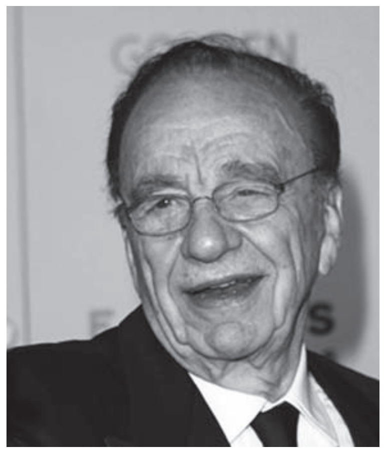
• The ethic of transparency, preached to poorer parts of the world, is now seen to be rooted in a financial universe that is proudly opaque.

• The self-advertised competence of Central Banks and regulators is undermined and in some ways their collusion with financial excesses is revealed. This was shown not just in the seediness of predatory mortgage lending but also in its deceptive packaging.

• More clearly seen is the dependence of so called 'free-market' capitalism on tax gathering nation states and federations. Like the present 'rescues' of banks, the system's dependence on export credit guarantees and state 'defence' spending may yet become news. Shown too is the psycho-political forces at work in the case of the appeals to Sovereign Wealth Funds to ramp up the asset base of banks.

• Most of all, this crisis reveals that the global pot of surplus value – however much it has grown thanks to the development of East Asia and the accompanying pressure on wages elsewhere[1] – is always finite at any given time. This is combined with the added problem of its realisation as the urge to squeeze out more of this same surplus value. As the *Herald Tribune* put it: "In any country or business sector, there is a limit on the number of good investments."[2] Witness the coincident fall in the value of the dollar which is not unfamiliar,[3] but also the global rise in the price of basic food. While the so-called fundamentals of capitalist economies have proved to be elastic, especially when it comes to credit creation, they have been shown up by the real fundamentals of daily subsistence. Needless to say one cannot live without food and its supply cannot be turned on and off by the mouse or the remote-control.

But there is still a job to be done to contest capitalism's explanation of its own present 'crisis' by its elite, wiseguys and lickspittles. They all hope to retain their dignity and go unpunished by virtue of a limited period of purely technocratic 'mea culpa'. This self-explanation is not an exclusive monologue, but those calling for the regulation of 'free-market' capitalism in its own interest have been doing so for a long time, and to no effect.



Left:
Rupert Murdoch, Irwin Stelzer, Josef Ackerman

The Language of 'Sub-Prime'

The most public strategy of in-house explanation of the last several months' 'crisis' has been to isolate 'sub-prime' mortgages as the sole culprit, while at the same time wiseguys like Rupert Murdoch's Irwin Stelzer have emphasized how relatively small the amount involved is, and how even smaller the percentage of 'delinquent payments' – i.e. overdue for more than fifty days. Bank of England figures indicate that bonds backed by 'sub-prime' mortgages is $0.7 trillion. This, as Donald Mackenzie has pointed out, is a lot of money. But it is only 2.5% of all non-government binds and outstanding corporate loans.[4] If this huge amount of money is in fact relatively small, doesn't this then indicate a fragility to the circuits of credit and liquidity?

'Sub-prime' suggests an 'underclass' as promoted by neoliberal conservatives. Josef Ackerman, head of Deutsche Bank referred to 'sub-prime delinquencies'. Others use corporatist allusions; the loans were 'toxic', there was 'gangrene' and danger of 'contagion'. It is the language of disease in what is an otherwise healthy fantasy world where free markets are beneficial to all, similar to the 'rotten apple' line applied in those very rare cases in which police brutality is inescapably proven. But the real blow of these mortgages very clearly lands on those people who have lost their homes; people who have figured rarely in accounts of the credit crunch except for brief TV images of a gothic-looking Detroit and stretches of empty houses in Cleveland. But this obviously has had an impact on banks too. What needs explanation is how this crisis had an impact greater than the relative amount of money involved. We should remember that neither the generic mortgage crisis, nor levels of personal indebtedness, especially in the USA and UK, came out of nowhere. The evidence of its roots can be found some years back.[5]

Jan Hatzius, Chief Economist of Goldman Sachs in the USA, equates what has happened to the dotcom bubble in so far as this crisis is a consequence of the mistaken belief that normal laws had been overcome and, in this case, US house prices could never fall. For the governments of the USA and UK, house prices are politically important because 'house owners' are a key voters. In the UK, the meanness and perversity of a policy of little or no new social housing has helped drive the steady increase in house prices to such an extent that no doubt many bourgeois have felt it to be their right that their properties should go on increasing in value for ever. Blindly they ran into the reality of higher rates of interest as Hatzius's analysis implies. But this does not explain the impact on the wider financial world which is not like the dotcom bubble. This time around, mortgages for the poor at high rates of interest were just one area of riskier lending supported by the prospect of high returns. Of course, in the purview of capitalism, these mortgages were attractive because of the high rates of interest charged. Then they went even higher in the US because Federal Reserve policy at that time intended to counteract inflation. As John Lanchester has pointed out, US interest rates went up "just as many of the sub-prime borrowers were coming off their first two years of fixed-rate mortgages."[6] As a consequence, the money of so many poor people, and their homes with it, simply went down the pan. That wonderful amoral word 'mis-selling' comes to mind here.

These developments are still not explained simply by the picture of eager salesmen followed by eager bankers acting out of greed or the need to perform. The eagerness to squeeze money out of the poor of the developed world tells a larger story. Not so many years ago banks decided they could squeeze no more out of the poor of the lands of 'emerging markets'. In the spectacular case of Argentina they switched attention to that country's middle class. A politico-economic crisis ensured and brought a government that played successful hardball with its creditors and their international financial institution backers. 'Emerging' stock markets have since produced well above average returns for investors, but to match and amplify this the poor of the developed world were brought into play. Here too, however, the competition for even expanded surplus value, created real contradictions. The holding down of real wages in the USA over a long period[7] in the interests of surplus value production made rising housing costs unreasonable, if not impossible, for those same wage earners and it is they who have borne the brunt of 'the crisis' in the developed world.

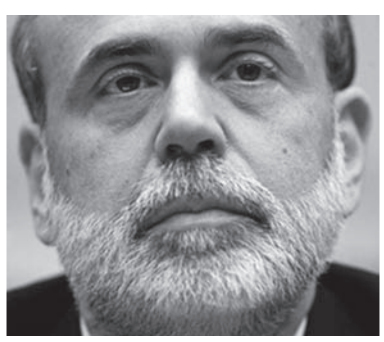
The process of making smart and profitable 'financial instruments' out of mortgages for the poor, mirrors those chains of sub-contracting in globalised capitalist production. With chains of production, the CEO of the multinational can deny knowledge, say, of child labour on another continent. Speculation in mortgages likewise reveals the abstraction of finance and how far apart are the worlds of borrower and banker. Given that Deutsche Bank is said to now be the biggest landlord in Cleveland, USA, the packaging of these mortgages has made that distance even greater.

Bankers Ain't What They Used To Be

When it comes to blaming someone else, the bourgeoisie have no equal. Central banks, regulatory agencies, hedge funds, and credit ratings agencies have all been pinpointed. These prominent damage-limiting self-explanations assume that once-upon-a-time there were bankers who were real, experienced bankers and they would have looked at the realities of where a loan was going and sensibly assessed its risk.[8] Over the last decade and more, as this discourse runs, they have been replaced by mathematical whiz kids empowered by the Scholes-Black equation and the power of computers who created elaborate programmes and new financial instruments designed to get an almost abstract share of the global surplus value pot. It's implied these bright guys were too clever for their own good and are without 'sound judgement'.

If that is the case, however, the degree of havoc caused is only possible because of the greater amount of credit that can be created (liquidity) by contemporary capitalism. Increasing credit increases speculation. The mathematicians may have developed and refined a variety of derivatives, but this only provides the *opportunity*, as the whodunits say. Yet mathematicians did not deregulate banking, nor come up with the idea of 'securitization', nor institute the changes in the capital ratio requirement of banks enshrined in Basel II rules. A lesson drawn from the Wall St. crash of 1929, which had created misery for millions, was that investment and retail banks should be kept separate; that the ordinary depositors should not be financing the risks taken by investment banks (risks on a greater scale given the greater cash base the retail bank could provide). The lesson produced the Glass-Steagall Act which kept them separate. After ferocious lobbying by the banks, the Act was repealed in 1999.

Securitization is the creation of asset-backed securities; debt securities which are backed by a stream of cash flows. In the 1980s, the notorious McKinsey management consultancy empire "was showing its banking clients how securitization had a cost advantage relative to traditional lending. The process has massively increased international liquidity. These are first sold by the borrower to a special purpose vehicle which isolates claims for repayment against the ultimate borrower who can also keep the debt 'off balance sheet".[9] It is also the case that the assets being bought with the borrowed money are themselves collateral. Such deals are 'leveraged'. From the investor's point of view the returns are likely to be greater than on average equities, but assume that the future is tied up, that those cash flows are secure, that, in this instance, mortgages would be paid in orderly fashion by poor people.



Right:
Anthony Bolton, David Einhorn, Ben Bernake, Sally Dewar

The accusation against the first manifestation of mathematician-bankers focused on computer-programmed 'quant' or 'tracker' trading programmes. They were seen to be inflexible and to replicate each other in such a way as to cause exaggerated movements in and out of currencies and investments. It was an internal critique especially prevalent at the time of the South East Asian currency crisis of 1997-8. But they have continued to be part of 'normal practice' because they were normally profitable, though not always. In August 2007 Goldman Sachs announced that its Global Equity Opportunities Fund had lost $1.8bn with such trading, yet this didn't stop it from announcing record profits of $11.6bn 4 months later in December 2007. This hardly gives anyone an image of orderly accumulation!

This time around, in-house analysis has faced serious presentational problem by which widespread faults in risk assessment have to be acknowledged without notions of structural greed or capital's accumulation imperative making an appearance, or even the vicious circle described by Donald Mackenzie between liquidity and 'financial facts'. Loans which share with 'sub-prime' mortgages the promise of high returns were in 'emerging markets' – but also Private Equity buy-outs and highly leveraged Hedge Funds, the material form of what has been called "financial arbitrage capitalism." Back in May 2007, before 'sub-prime' became familiar news vocabulary, one especially shrewd wiseguy – 'star' investment manager Anthony Bolton. Bolton – having sold nearly all his bank and financial stocks – warned that large private equity deals were exposing banks to a default risk; that there had been unchecked lending to support a wave of mergers and acquisitions, and that many of these were "covenant-lite", meaning that if such a company were to go bust the bank would have little ability to reclaim the money lent. This came at a time when in the USA there had been a record leveraged buy-out of the health capitalists HCA for $33bn, and in the UK of Manchester United and Liverpool football clubs, touching certain sporting nerves in civil society. A report by Robert Parkes of HSBC suggested that all but the 20 biggest companies were potentially subject to such buy-outs. He estimated that ready sources of cash and debt gave private equity global purchasing power of $4.5 trillion.

Despite the lack of interest premium in such 'covenant-lite' loans, European and USA banks were falling over themselves to make them, and did not need mathematicians to do it for them. Merrill Lynch, the bank involved in the HCA buy-out, announced that a large part of its profits came from such loans. The lack of premium was dwarfed by their sheer scale and therefore profit to the bank which, like other such banks, wanted its cut from the expanded, yet limited, global pot of surplus value; limited even where it is a matter of "buying and selling claims on future value created in future productive activity," as Peter Gowan puts it.[10] Private equity firms are a case where the assumption is that they will be more efficient in squeezing out surplus value from any given company usually by increasing the intensity of labour of its workforce, or by selling off the most profitable parts of the company, and that the cash flow is guaranteed. A study by Mark O'Hare of the research company Private Equity estimated that in the decade since the mid-1990s the typical European buy-out fund had given 15-20% returns to its investors net of fees, as opposed to a far lower FTSE return. Banks, for their cut, sub-contracted the job of squeezing out the extra surplus-value to these specialists, but with few safeguards.

Anthony Bolton was not alone in speaking out in May 2007. The new chief of the US Federal Reserve, Ben Bernake, gave a warning a little stiffer than that of his predecessor Alan Greenspan who made utterances about 'irrational exuberance.' Bernake said, "I urge banks to closely evaluate the risk that they're taking (…) not only in the context of a highly liquid, benign financial environment, but in one that might conceivably be less liquid and benign'. More specifically, on the 20th of the month the Financial Stability Forum, a typically *ad hoc* set-up of global financial regulators (which "brings together on a regular basis national authorities responsible for financial stability in significant international financial centres, international financial institutions, sector-specific international groupings of regulators and supervisors, and committees of central bank experts") reported to the G8 at its Potsdam meeting that "investment banks are so keen to win business from hedge funds that they are relaxing their risk assessment."

Why should this be the case? At various times, in-house analysis of the crisis has made reference to both the pressures and incentives on and for bankers to make loans. As individuals, the bonuses – often in the millions – come with the loan regardless of how it pans out. This was touched on by London broker Terry Smith: "Now you've got a divorce between the origination of the credit and the person who carries the can for its (the loan's) service."[11] But the bonus system is now built-in by the notion that 'the best and the brightest' must be kept by individual banks at all costs, an elitist manifestation of structural personal greed. This was referred to by the Financial Stability Forum on 10th Feb 2008 in which it cites how the lavish performance pay regimes in London and on Wall St. "encouraged disproportionate risk-taking with insufficient regard to long-term risks."

The pressure on bankers is that the real crime in their competitive world is to miss the boat when new loan opportunities are being taken by other banks. And the pressure to come up with the highest rates of return for investors usually comes from fund managers, themselves under pressure to perform. What has been most revealing is the focus on UBS Bank. They have been portrayed as dowdy virgins, tempted by high returns into an exotic world of credit derivatives which they didn't really understand. But what of the losses made by supposedly streetwise Citigroup and Merrill Lynch which lead to the resignations of the chairmen of both? Simply put, the pot of global surplus value is limited at any given time.

Mervyn King, Chairman of the Bank of England in early 2008, in front of the UK's Treasury Select Committee stated: "One of the problems is the immense pressure on fund managers to achieve above average returns. This is madness when it is not possible for everyone to earn above average returns." Here was an admission that the pot is limited, but then failed to account for structural personal greed by falling back on a familiar ahistorical standby: "But I don't think you can regulate human nature".

"Making Your Investment Work As Hard As You Do."

This has been the slogan of advertisements for the Allianz financial outfit which appeared on the BBC World channel. It highlights the privileged position of the investor class.[12] Up until the recent talk of risk assessment and the lack of it, this privileged class seems to have assumed that its right to a return is inviolate. As shown by Rob Ray in *Mute* (9/8/07), this has been almost institutionalized with PFI. Through the proposed MAI (Multilateral Agreement on Investment) which has been successfully resisted, such privilege was planned to be institutionalised on a global scale with private capital able to sue member states of the WTO. Instead this goal is sometimes achieved with bilateral trade deals between very unequal partners, and backed up with the threat of "investment strikes." Both are aimed at and within nation states.

What has upped the stakes is the investor now expecting a 'higher than average return' *without* risk. The benchmark has been from Private Equity buy-out funds with their 15-20% returns, and on "Emerging Market" funds. With these, the Morningstar investment research firm estimated that in the three years up to and including 2006, "Diversified emerging stock markets funds returned 56%, 24% and 32%, way above the 7% on domestic equities". And returns lower still from the safest, Treasury Bill, assets. Clearly such funds take a more direct share of that surplus value produced in Asia and Latin America, but they have helped create a benchmark.

In a previous 'crisis' which dominated the 1980s and beyond, that of 'Third World" debt, banks with petrodollars to play with but a shortage of investment opportunities in the rich world poured money especially into Latin America. As early as 1976, Chase Manhattan generated 78% of its profits on its international operations. Increased interest rates and restructured debt packages increased the levels of repayment. Even for countries requiring no restructuring, banks increased the interest rate spreads. Over the course of the 1980s the accumulated debt of Latin America grew from $257bn to $452bn despite total *annual* interest payments of $170bn. By 2000 the debt was $750bn. The well-known history is that this form of free-market capitalism then needed the World Bank and a resurrected IMF to keep the show on the road and provide the discipline (with ideology attached) to ensure that higher priority was given to servicing the debt than any objectives like maintaining living standards.

"If You Can't Protect That Which You Own, Then You Don't Own Anything."

This is what Jack Valenti, head of the Motion Picture Association of America, once said. In May 2007, Sally Dewar, capital markets sector leader at the Financial Services Authority, remarked that in the good old days before a decision to lend money by a bank was made, it would go to a credit committee of top bank executives listening to staff giving a pitch about the ability of the client to repay and on what terms. Whereas now, she said, these terms are given less consideration, and instead more importance is attached to how quickly the lender can offload the debt by selling on portions to rival banks. At the same time, this offloading of debt was supposed to make the financial world more resilient to shocks by spreading it around the world. But already by August 2007 the cry went up, "No one knows who owns this stuff." This stuff being CDOs (Collateralised Debt Obligations) and 'credit default swaps', instruments and processes whose workings have been so well documented by Donald Mackenzie.[13] CDOs started as forms of insurance – banks paying others to take the risk on loans or part of loans they had made – but then were taken up as profit-makers in themselves as packages of mixed debt. These too, as sophisticated forms of securitization, were put into special purpose vehicles typically registered offshore. There are different grades of what could be called 'creditworthiness'. Not unusual rates of return are 15-20%, while the highest rated offer returns better than the equivalently rated corporate or government bonds, as the McKinsey Consultancy had predicted. Many are mortgage-backed, of which, as previously shown, 'sub-prime' are a small component. What is difficult, MacKenzie shows, is valuing derivatives like CDOs. It is also an arena for mathematicians and computer power. Naturally enough 'recovery rates' (or the extent to which loans are 'covenant-lite', as Anthony Bolton put it) are a factor in determining 'value', but the most problematic is what is called 'correlation'; the degree to which one loan default might be part of a pattern, a cluster of defaults.

It is at this point that the blame game returns to the mathematician bankers. It's they, as well as the immense computer power used by 'the single-factor Gaussian cupola' (which has become the standard and only mutually intelligible way of CDO valuation), who are at fault. By developing 'credit indices' valuation 'facts' are created but these have proved to be especially volatile. The dynamic created by defaults has, in turn, created increasingly irrational derivatives reminiscent of the 'Persian'/'survive or perish' bet for dodgy cheapo airlines of the future – a great satirical riff in James Kelman's novel *You Have To Be Careful In The Land Of The Free*. The outcome, Mackenzie argues, is not that banks have been hiding their losses, but that the losses are hard to measure credibly. How, he asks, can you value a portfolio of mortgage-backed securities when trading in them has ceased? It has been down to central banks to give them a value which they may not have at all. It is this which gives the lie to the sanguine line that everything is OK, it's not a solvency crisis, but "a fairly typical liquidity crisis." Whatever else, it is not typical.

Out Of The Shadows

Along with Metrolines, credit ratings agency companies (Standard and Poor, Moody's and Fitch) have been dragged out into the bright lights of blame. Auditors seem to have escaped any censure until the Financial Stability Forum meeting in February '08 attacked secretive off-balance accounting. Given the 'form' of the oligopoly of global auditors, this is amazing.[14] Metrolines are presented in the UBS category; foolish virgins who left the safe, dull business of insuring municipal bonds, to insure exotic derivatives, attracted by the returns on offer.[15] More venom has been directed at the ratings agencies, attacks which however, undermine a key component of *ad hoc* capitalist power.

During the 1980s and '90s this oligopoly of private companies (Standard & Poor, Moody's, and Fitch) exerted huge power over 'third world' economies, their country ratings determining what rate of interest they would have to pay on their debt, and in some instances whether they got credit at all. "The ratings agency's appearance as a non-partisan institution devoid of political affiliation, and thus motive, also conceals its disciplinary nature in terms of ideologically reproducing the 'international' standard of corporate governance."[16] As part of an *ad hoc* tyranny, ratings agencies may be more effective, say, than the IMF questioning the creditworthiness of Malaysia when it sensibly introduced currency restrictions during SE Asia's currency crisis. The ideological dimensions of this tyranny were illustrated in an interesting way by a commentator of the sanguine variety: Jeremy Warner of *The Independent* attacked proposals from the British government that would in some way monitor these agencies. He argued that this would mean "governments would become responsible for the ratings, thereby politicizing the whole business of credit." But as we know in so many instances, especially in the Third World, credit is already politicized in this way.

Yet such power is undermined by the present publicity which has arisen because of losses made in the rich world. David Einhorn, CEO of Greenlight Capital hedge fund, and Mackenzie differ in the nature and degree of blame attached to the these agencies for giving too high a rating to many CDOs. But what they agree on is that whereas the agencies were used to rate just corporate and government bonds, much of their business is now with CDOs. Also, that there is a conflict of interests given that the agencies are businesses, and it is the issuers of debt instruments who pay the agencies to rate them.

As presented in *naked Capitalism*, [17] Einhorn argues that it goes further; that CDOs carry the highest fees, and that these fees were correlated with their willingness to look the other way at credit losses. Or rather, that ratings (AAA or AA+ for example) were created equal, whereas "the more complicated the paper – like CDOs – the more risk it was allowed to carry in each ratings category". This is what infuriated Anthony Bolton; the lack of premium on riskier debt and which he warned about months before Standard and Poor downrated some sub-prime-based CDOs. Mackenzie is slightly more sympathetic, given that agreeing on the value of an asset had become more difficult. But says they were/are at fault for rating mortgage-backed securities on the basis of previous experience of default rates and the proceeds of repossession property sales, and did not take into account the bubble in house prices or the appetite for risky debt driven by investor expectations. In reality, the *assumed* cash flows were not there.

All this makes a credit ratings oligopoly, with the power to decide on what terms people can get credit, look amateur as well as greedy in their own way. But they cannot be blamed for this appetite for debt giving higher returns. The 'virgins' of UBS or German landesbanks were not led astray by hired malefactors and incompetents, but the pressure and greed for higher returns.

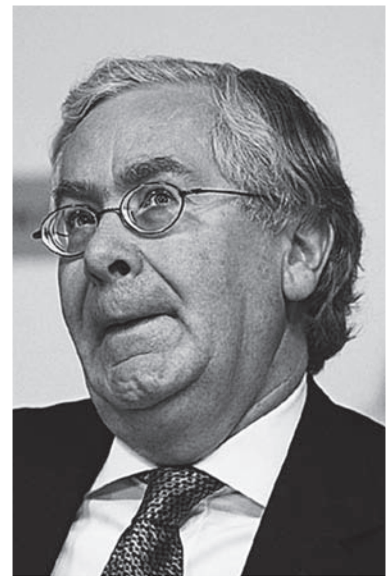
"They got this really nice house... Bought it when the price was right, and I mean: really right. Back the late Seventies you know? Before everything explodes there, prices go right through the roof; then ten or twelve years later, after all the suckers pay them, get in hock past their balls, down the prices come again...And now the banks are goin' under; we're all really inna shit."

George V. Higgins, 'Bomber's Law', 1993

The consequence of this crisis in the value of asset-based securities has had predictable consequences. Not knowing what securities are worth has seen banks not willing to lend to each other and tightening up on loans generally. Equally predictable in the UK, this has focused on mortgage lending, but it also affects what might be called productive loans. Thus the impact of the 'credit crunch' on the real economy.

The great hegemonic strength of capitalism today is its perverse universalism. The financial system must be saved or everyone is affected. In a previous specifically 'debt' crisis, that hit Latin America right through the 1980s, the IMF and BIS (Bank for International Settlements) were brought in to save the banks from potential defaults on their loans. "The decision to ignore the normal workings of the market mechanism and allow the imprudence of the bankers to go unpunished was quite deliberate. The system had to be saved."[18] What happened was an unplanned resort to official recycling, which is what we are seeing now in the present crisis, with injections of liquidity from central banks. Even commentators from the Keynesian tradition who are keen on 'moral hazard' (i.e. that banks and investors should pay for their mistakes), fall back on disease imagery; how the failure of one bank would create a vicious circle of financial mistrust, further failures and a Depression such as began in 1929, and how a financial collapse would end up hurting millions of savers and investors.

The most spectacular rescuing was of Northern Rock in the UK and Bear Sterns in the USA. What stands out in both rescues even though their causes were so different – Northern Rock as a 'victim' of illiquidity – is the determination to at least maintain the fiction of a free market. In the case of New Labour it even at one point meant backing a chancer like Richard Branson until wishful thinking was no longer possible. In the case of Bear Sterns the fiction of the buy-out – on tough terms – was that it was done by the JP Morgan bank at a fire-sale price.[19] In this instance, the Federal Reserve was so keen to see the deal go through that it offered to guarantee the $30bn worth of hard-to-sell mortgage-backed securities,




Above:
Mervyn King, Larry Summers, Alan Greenspan, George Soros

while JP Morgan played tough on voting through the deal by BS shareholders, this while it itself has an unknown exposure to credit default swaps.

These were the unavoidable public spectacles. At the same time there has also been a steady official recycling, that is the provision of credit to capitalist banks by Central Banks. This passes under the rubric of 'liquidity injection' as if this were a neutral process. The Federal Reserve was quickest off the mark. On the 16th August '07 it announced a cut in its discount rate to make it cheaper for banks with cash-flow problems to borrow money; a U-turn from their inflation concerns of just one month earlier. More to the point, they made it possible to borrow cash against assets no one seemed to want to buy (and therefore of undefinable value) with home mortgage and related assets specifically listed as acceptable collateral. The policy of restricting these loans to short periods was also abandoned. The new liquidity would be available as long as needed. The Bank of England was slower off the mark, and has been blamed for this. Starting from a hard 'moral hazard' line, described as 'Victorian', the run on Northern Rock forced it to change. At first banks could borrow from it, but publicly and at stiff rates. In December '07 it joined the Fed, ECB, Swiss and Canadian Central Banks to make a $100bn international 'injection', offering for its part $20bn of 3 month funds at two auctions. This time it accepted a wide range of 'high-quality' collateral, and without the penalty rate it had imposed before. Then this could be done privately and for longer periods. In late April '08, after nine months of 'credit crunch', it was announced that it would be willing to exchange government bonds for mortgage-backed securities; swaps for one year periods which could be extended to 3 years. This facility would run to between $100-200bn. These securities were again described as 'high-quality' but the reality is that these are illiquid in the present climate for the precise reason that who can say what is 'high quality'. With house prices falling, interest rates rising, and the possibility of a sharp economic downturn, an increasing amount of mortgage debt will not produce those cash-flows, and will 'go bad'.

This Bank of England move followed a similar plan announced by the Fed which on May 2nd '08 raised the size of the 'Tem Auction Facility' (another liquidity injection process) and also allowed lower-rated asset-backed debt to be used as collateral, some of which, on the 'free market', would be priced at zero, some of which could be reliant on credit card debt, unsecured loans and auto loans. At the same time, the Fed[20] has been steadily cutting interest rates. This was the policy used consistently by Alan Greenspan to the point where the 'Greenspan put' became part of the financial world's own language, meaning that the Fed would always act to protect the market from losses. The policy under the new chairman, Ben Bernake, was going to be much tougher, just as wise-after-the-eventers were attacking the Greenspan legacy, blaming him for creating one asset bubble after another. In fact, since the 'crisis' began, the same policy has been followed.

The amount of credit, as of March '08, supplied officially to the US banking system far exceeds that coming from Sovereign Wealth Funds to which some banks have turned to 'strengthen' their cash base. For example, in December '07 Merrill Lynch sold $5bn of its equity to the Singaporean government's investment fund Temaesk, and the Abu Dhabi Investment Authority has taken a $7.5 bn stake in Citigroup. These are entirely rational moves by these Funds, given a reluctance both to hold more dollars or to dump them, given that this would set-off a self-defeating spiral in its value. Despite the rationality and the relatively small amounts however, it is these funds which have created psycho-political and ideological anxieties, given that these are the Funds of not-white men from what might be called varieties of 'state capitalism' that had been cast into the dustbin of history by Alan Greenspan in 1998. "Foreign governments may not operate solely in accordance with normal commercial considerations," is the way these anxieties have been expressed. A characteristically ad hoc outfit, The International Corporate Governance Network, met SWF (sovereign wealth fund) representatives in Gothenberg in March, but did not call for a regulatory regime, rather that the SWFs should be transparent in their motivations. This came after the SWFs had rejected Larry Summers' (ex-US Treasury) demand at Davos that they sign up to a code of conduct, transparency and so forth. Capital is capital with a global shared class interest, but these SWFs, having been continually lectured on the subject since 1997, must have enjoyed saying, 'Well, what about transparency in your own banking system then?'

Right: Alexander Lamfalussy, Felix Rohatyn, Peter Sutherland

The Invisible Hand And The Puppeteer

'Adam Smith's invisible hand has a puppeteer – the US Federal Reserve', read a *Herald Tribune* headline after the US government-organised rescue of Bear Stern, the USA's fifth largest investment bank. Calls for regulatory systems and architectures are, rather, the *quid pro quo* for this practical business of rescuing banks. Some of those making such calls are rightly keen to talk of how the free marketers, players and ideologues always complaining of government interference, run to governments for help whenever there is a crisis.[21] What the commentators and players (George Soros and all) demand is that new regulation of the markets be introduced for its own sake, and that of everyone else. Apparently regulations should involve new layers of transparency, accountability and financial monitoring. In the happy world of Will Hutton, it should not be so difficult: "We must have a government that understands the delicate relationship between markets and the state and is ready to act – and a wider business culture that accepts the necessity. Business needs government and has to accept that regulation and intervention are part of the bargain."[22] Well that's all right then, apparently all it takes is a little delicacy and a wider culture and all will be well.

Back in August '07, Gavyn Davies, a pillar of the British power elite, was telling the Bank of England not to play the hardball game it was threatening but that it should "address some regulatory deficiencies once the crisis blows over." In the ever-more comprehensively deregulated world, such calls appear at regular moments of 'crisis'. Real heavyweights like Alexander Lamfalussy and Felix Rohatyn have said such things on and off for 30 years. George Soros, Peter Sutherland, as well as "Third World" governments that had been so currency battered, called for a 'global financial architecture' after the free movement of capital had such a devastating impact on Asian economies in 1997-8. The response from the self-confident Clinton Treasury team was that this was unnecessary and wrong. What mattered were national regulators for transparency and accountability.

Soon after the collapse of the ironically named hedge fund Long Term Capital Management Fund, other regulatory demands were made. But all this talk was merely about calming nerves. The US Treasury obviously hoped the impetus for reform would pass before issues related to offshore banking centres,[23] hedge funds, or even deeper issues like capital market liberalisation, became subject to scrutiny and negotiation. Indeed in 1999, one year after the rescue of LTCM, the Glass Steagall Act was abolished! Soon after all the dire warnings of May 2007, Hank Paulson, the new Treasury Secretary[24] was complaining that regulations introduced after Enron were becoming oppressive and would make New York 'uncompetitive'. It is this same Hank Paulson who planned what *The Guardian* (31/3/08) headlined as the "biggest shakeup of Wall Street watchdogs in 80 years." Although suggesting a merger of some existing regulatory authorities and giving new monitoring powers to the same Federal Reserve, the same 'Club Fed' which missed the mortgage crisis, the proposals would not limit banks' exposure to credit instruments. In fact it sought to limit what regulation was capable of. "I am not suggesting that more regulation is the answer, or even that effective regulation is the answer, or even that more effective regulation can prevent the periods of financial market stress that seem to occur every five to ten years. I am suggesting that we should and can have a structure that is designed for the world we live in."

The Herald Tribune headline[25] was more pertinent: 'Treasury Proposal Gives Wall St. What It Wants'. It noted that a Wall St. lobby group, 'The Committee on Capital Markets', had released a report saying that the "shift of regulatory intensity balance has been lost to the comparative advantage of the US financial market." What also stands out in the Paulson version is his nonchalant insistence that this crisis is just one of those things, a regular period when financial excess is reined in before a new burst of lending and growth will resume on a 'sounder' basis.

In a letter to investment firm ECOFIN in September '07, UK chancellor Alistair Darling specifically warned of the dangers of regulatory overkill. Apart from demands to tackle the role of ratings agencies, the promise has been for more monitoring of a wide range of financial institutions and businesses. In the UK, this to be done by a beefed up Financial Services Authority. It is the banks who pay for the bulk of the FSA's activities, and of course they have lobbied hard to restrict any growth in regulation. It is indeed the regulation by 'principles' only that Paulson wants New York to emulate. The FSA is the same institution which failed to monitor Northern Rock for two years before its share price started to dive in April '07. It brings into question the competence as well as the will of such an agency given that the Northern Rock model of lending long, when 70% of the money with which to make them were from funds raised on the international market, was obviously flawed.[26]

Beyond The Duologue

In-house analysis of the crisis has not been a monologue. There is a clear difference between those calling for regulation and more international managing of the international economy as the price of Central Bank rescues, and those from what I've called the sanguine camp. The 'regulators', also nervous that more and more interest rate cuts may not have the intended effect – as happened in Japan in the 1990s after the fall-out from a property asset bubble collapse – are often enthusiasts for 'moral hazard'. Or, rather, believe that present Central Bank policy is one of postponement and that the next credit crisis will be worse. This idea of 'postponement' figured in critiques of Keynes; that government deficit spending could only postpone capitalist realities for a period, and that in the end debts must be paid. The irony is that the neoliberal model depends on a cocktail of 'Keynesianisms', military, asset, and personal indebtedness, which might also be called privatized Keynesianism. These 'regulators' will, I believe, have little real effective policy impact, even though their concern is for the long-term and general well being of international capitalism.

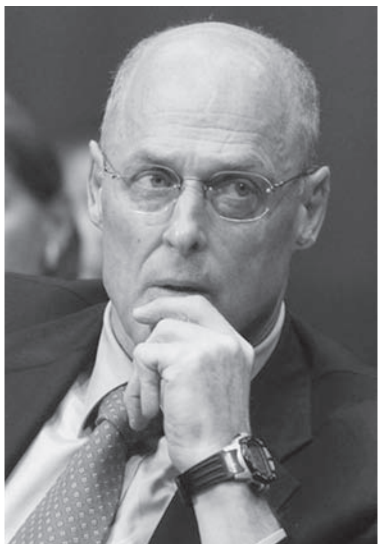
There are many in the sanguine camp but Jeremy Warner of *The Independent* is as representative as any. Talking first in the UK context, he argued that firmer regulation "is a complete waste of time and energy. For the moment bankers have learned their lesson and are already well ahead of the regulators in sorting out the mess they've created. They won't quickly repeat the mistakes they've just made. Whatever the new regulations put in place, markets will inevitably find a way of circumnavigating them. Come the next crisis, it will be a different door altogether through which the horse bolts. Worse still, any new regulatory obligations will help create the next crisis, such is the ingenuity of markets and the law of unintended consequences."[27]

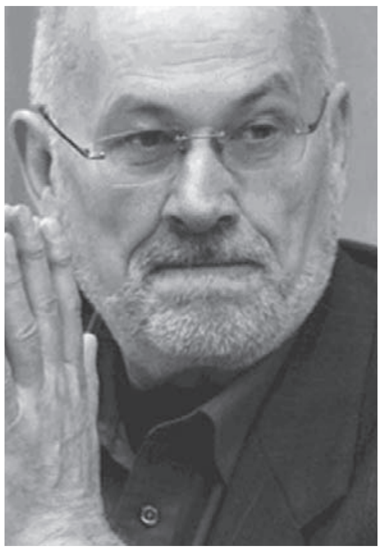
The ideological assumptions here are staggering. Perhaps they should be placed first against Josef Ackermann of Deutsche Bank who confessed: "I no longer believe in the market's self-healing power." But no problem here for the likes of Jeremy Warner: The banks have learned their lesson and are ahead of the game; it's a cyclical business, just one of those things. But there is also a back-up. That the market will out, is backed up by a certain brand of fatalism. Never mind that capital does not want to be regulated, there's no point. Proponents of neoliberalism are very keen on 'inevitability', that everything is cut and dried, no one is responsible and politics are an irrelevance. Internationally Warner argues something similar, that no institution could command in "today's viciously competitive global economy". Vicious? Certainly. But selective when it comes to competitive; competitive for a share of the global pot, but dominated by oligopolies.

If neoliberal capitalism's assumptions are absolute, and its model both global and secure, there is of course truth to Warner's arguments.[28] The British state described by Marx could push capital to act in its long term collective interest, but this no longer seems either possible or desirable from the neoliberal point of view. Regulation and institutional arrangements are anathema except for moments when rescue is needed, because these will inevitably involve negotiations, and negotiations will involve, at however subterranean a level, notions of fairness. The private property nature of capitalism is an absolute given, not to be tampered with by either democratic institutions or notions of justice. Thus, in addition to the prospect of being given short shrift by the Soverign Wealth Funds, it would have been ideologically difficult for the *ad hoc* International Corporate Governance Network to demand regulation in their case.

An often more radical voice has characterized the crisis as showing the evils specifically of financial capital, that this has become 'casino capitalism'. It's certainly true that Wall Street and the City of London have political clout as well as the power to decide who gets credit and who not, and that their demand for higher than average returns (a bigger share of the global pot) has created the present crisis. This too is likely to have a negative impact on economic activity. But if a consequence of this negative impact is a mood of resentment, it would seem all too easy for 'financial' to be made synonymous with 'Jewish' or 'cosmopolitan' capital for example. Easy to imagine how an ultra-leftist turned Nazi like Horst Mahler is already pushing this version of events.[29]

Contemporary capitalism is not just 'financial' capitalism. 'Productive capital' on the front line of squeezing out surplus value is not doing so solely for the benefit of the banks, and besides, also puts a chunk of their realised profit into financial assets. Contemporary capitalism is not going to 'collapse'. It is vulnerable however, shown by its hysterical intolerance of any other economic model, while millions take objection to being squeezed for more surplus value whether through increased intensity of labour, or having the costs of their reproduction increased. To be superceded, or even reformed in any meaningful way, its own version of itself must be challenged; its legitimacy, competence and the self-confidence of structural greed.





Left:
Hank Paulson, Horst Mahler, Alistair Darling

Notes

1. In May 2006, Stephen King, MD of economics at HSBC was commenting on the size of Chinese production and India and its cheap labour, went on to say, it "has made it a lot more difficult for Western workers to demand wage increases in compensation for higher petrol prices or gas bills." And these workers will presumably be none-too-pleased. The smug, patrician tone of that "presumably be non-too-pleased is a real piece of work, but the point is clear a squeeze on real wages can only make the pot of surplus value that much greater.
As to surplus value, I am using this in the broadest sense of economic exploitation. That is the global pot also includes the kind of non-value production, of theft, war looting and the other dirty washing of contemporary capitalism.
2. *IHT* "The Return of Hot Money" 20/5/06
3. During a previous 'credit crisis' , that of 'Third World' debt and its repayment in the 1980s, the dollar also fell
4. Donald MacKenzie "End-of-the-World-Trade": London Review of Books 8/5/08: http://www.lrb.co.uk/v30/n09/mack01_.html
5. See for example, Barker: "The D Word"
6. *London Review of Books*, 3 January 2008, 'Cityphilia', John Lancaster: http://www.lrb.co.uk/v30/n01/lanc01_.html
7. Robert Brenner estimates that for 80% of American workers real wages have stayed at 1979 levels.
8. This hardly explains how it was Derek Wanless former chairman of NatWest was the man in charge of credit controls at Northern Rock at the time of its collapse.
9. Their role in the Enron scandal obviously did not lessen their popularity.
10. 'The Globalization Gamble: The Dollar-Wall Street Regime and its Consequences', Peter Gowan: http://marxsite.com/Gowan_DollarWallstreetRegime.pdf
11. *The Guardian* 15/9/07
12. 'Class' here is admittedly short hand. The privileges of rich and corporate investors are ideologically validated by the existence of pension funds as investors, and therefore of millions of not-rich people, those who, in the slogan, 'work hard'. The question of who loses when investments 'go bad' is also germane. In the case of Enron there is evidence that the biggest losers were pension funds in Republican controlled states. At the same time the fetishistic quality of the slogan is obvious; investments do not 'work'.
13. *ibid*
14. The lectures that South East Asian governments had to endure in 1997-8 on transparency, accounting standards and so on, must have caused grim mirth amongst them given the record say of Coopers & Lybrand, auditors to Robert Maxwell, Polly Peck. In good British style they changed their name by amalgamation. As PriceWaterhouse Cooper they were the auditors for Northern Rock. In fact they earned more from 'advisory' work with it, than from auditing.
15. Though one Metroline, XL Capital, is being sued by Merrill Lynch over 6 'credit default swaps' worth $3 billion.
16. Soederbergh: *Global Financial Architecture*: Zed Books
17. www.nakedcapitalism.com/2007/11/rating-agencies-created-incentives-to.html
18. Soederbergh.
19. JP Morgan has played this role as government –backed leader to both enforce and represent the collective interest of banks before. It was they who took centre stage in the Situations Room of the White House at Christmas 1997 in organizing the 'bail-out' of South Korea.
20. It has been recently dubbed "Club Fed", a piece of wit that has for a long time described Federal prisons as opposed to state ones, on the grounds that such prisons are relatively cushy. This is the Fed in the Greenspan + era..
21. It should be amazing that this free market fiction should still be maintained despite the sheer size of Export Credit Guarantees, and of that R&D and profit that comes through military contracts.
22. The Observer
23. At the height of an earlier round of demands for regulation, Alan Greenspan argued, with a fatalism sometimes used by deregulated capital's apologists, that regulating offshore banking centres would only send such finance 'further underground.' They have proved to be indispensable to deregulated financial capitalism, e.g. the registering of SIVs in the Cayman Islands, and to recycle so much of the dirty money also indispensable to modern capitalism. This is what Loren Gouldner, following Rosa Luxemburg calls 'fictitious capital'. As I noted earlier I have used surplus value in its broadest sense to include such money.
24. Paulson, like Robert Rubin Treasury Secretary under Clinton, was a CEO of Goldman Sachs, the investment bank. 'What's good for General Motors is good for America," is long gone, and one reading might be that it's a case of "What's good for Goldman Sachs." There is some truth in it, but it also indicates the nature of what Wright-Mills called The Power Elite, revolving doors between private capital and government as well as the military. Rubin was drafted in As CEO of Citigroup after the resignation of Charles Prince.
25. 2/4/08
26. This overuse of securitization was used to increase lending to the point where Northern Rock accounted for 20% of British mortgages at the start of 2007.
27. *The Independent* 14/9/07
28. Never mind a lack of authority to regulate, there is not even an "authority on the global scene to come out with a credible estimate of the overall exposure", to 'bad' debt, as Diane Cholyleva of Lombard St Research put it recently.
29. See also the latest from Samuel Huntington, American ultra-nationalist. The cosmopolitan globalizers are the enemies of America and some of them are American: therefore they are in effect, traitors. See his *Who Are We?* Finance capital is rather, a form particularly suited to the Power Elite.