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Column - Sajjad Zohir

Financial rout and future options

US President-elect Barack Obama embraces Iraqi war veteran Tammy Duckworth after the two placed a wreath at The Bronze Soldiers Memorial in honour of Veteran's Day in Chicago on November 11. Photo: AFP

In a recent article (Who are the Architects of Economic Collapse? Will an Obama Administration Reverse the Tide, Global Research, November 9, 2008), Michel Chossudovsky noted that the "bailout" proposed by the US Treasury does not constitute a "solution" to the crisis. On the contrary, he predicts, it will cause further collapse. To quote him: “We are dealing with an absurd circular relationship: to finance the bailout, Washington must borrow from the banks, which are the recipients of the bailout.”

Chossudovsky suggests that the financial crisis is the outcome of a deregulated financial architecture. The Glass-Steagall Act, considered a pillar of president Roosevelt's "New Deal", was put in place in response to the climate of corruption, financial manipulation and "insider trading" that resulted in more than 5,000 bank failures in the years following the 1929 Wall Street crash.

We are informed that the Clinton administration initiated the 1999 Financial Services Modernisation Act (FSMA), which led to the repeal of the Glass-Steagall Act. And this “liberalisation”, coined by many as policies of "greed and irresponsibility", and which President-elect Barack Obama had criticised during his election campaign, is alleged to have paved ways for subsequent mis-governance and the current crisis.

Chossudovsky concludes that Obama provides a "human face" to the status quo, which is drawn from his observations that the very 'engineers of financial disaster' are now being considered for the position of treasury secretary.

He mentions four names, all of whom are alleged to have connections with the financial institutions whose wrongdoings are said to have contributed to the recent crisis. They are Lawrence Summers, professor of economics at Harvard University; served as chief economist, World Bank (19911993). He was treasury secretary under president Clinton in 1999 and played important role in the adoption of the FSMA in November 1999. Summers is currently a consultant of Goldman Sachs, and managing director of DE Shaw Group, a hedge fund. Paul Volker was chairman of the Federal Reserve Board in the l980s under Reagan. He is alleged to have played a central role in implementing the first stage of financial deregulation, which allegedly facilitated bankruptcies, mergers and acquisitions, leading up to the 1987 financial crisis. Timothy Geithner is CEO of the Federal Reserve Bank of New York, which is a powerful private financial institution in America. Jon Corzine, governor of New Jersey, former CEO of Goldman Sachs.

Chossudovsky obviously provided one perspective on happenings in the US and global financial markets. But there are others as well. Some find Chossudovsky's view to be heavily partisan, although see some merits in his identification of the problems with the liberal agenda. Surely, Volker believed that the market could work as long as someone like him kept monetary supply in check.

Unfortunately, he was followed by less prudent people.

An analyst I had an exchange with suggested that the issue cannot be traced to any one cause. He mentioned the following issues that were left out of Chossudovsky's analysis:

1) The Republicans, especially Bush, encouraged American homeownership and national hubris. The idea that someone should have a house over their heads with borrowed fund even if they cannot afford it is absolutely ridiculous.

2) The push towards pooling of pension vehicles and allocations towards IRAs (that fuel the action of any free market miscreants) is a Republican notion.”

I was reminded of the need to look into the irrationality that led to a boom on paper when one looks for 'architects' of a collapse. There, (I quote) “the culprits lie across the chain: a) homeowners who purchased houses she/he could not afford; b) mortgage lender who was paid on commission and sold homes to dead people; c) banks who enticed those mortgage lenders because they knew they could wrap up the mortgages and transfer the risk; d) wall street people who packaged what was worthless and sold it for twice the price; e) "investors" who purchased these securities with no idea what's

underneath, and most importantly, f) the pensioners, insurance purchasers, and people who put money into mutual funds --- who ultimately allowed this pooling of money to be allocated irrationally."

Does that mean that the government policies on both sides made it easier for the different players in this asset bubble to get away with their actions? "Oh yes!" was the answer.

Someone who followed through Obama's speeches suggested that he is too rational to follow his party line of welfare, which was a necessary campaign evil. A friend noted: "People like Summers, Buffett and Volker will be in favour of fiscal restraint. All are historians at heart, and surely they realise that FDR's actions in the 1930s led nowhere. In fact, it worsened the depression, until the war led to an increase in industrial activity."

I was further reminded that "American hubris will never let them admit that Hitler helped them jump out of the depression by exporting war"!

As an onlooker, I had more questions. There have surely been resource transfers across sectors and segments in society through the whole process (rise and fall of prices) -- what kind of implications do these have for the days to come and for policies to dominate? Surely, a large-scale war is historically proven to have 'helped' in getting out of economic recession, but is that conceivable?

The bailouts, the more tempting option for postponing the fall, may make the former option inevitable. Thus, only civil way-out seems to be fiscal restraint, that is, by restructuring the economy (which demands US consumers to live in austerity and for us to rely more on local market) and bearing with recession for some years to come without facing politically instability.

Could the incumbent US president lead that painful road? I am told that "fiscal restraint" is unlikely to be politically acceptable in the US, where "people have a sense of entitlement that is deeply embedded throughout all layers of their society, even amongst the more sensible people". Last person who tried this was Volker, who, as understood by some, was hated at the time.

"What happens along those lines depends on Obama's choice of lieutenants and his ability to stand up to an overly liberal party line" -- thus, the critics of Chossudovsky seem to agree with him on the importance of this choice!

What are we then left with -- a war at a global scale with history repeating itself? Or, have we come of age to innovate less painful ways? On the home front, there is a need to revisit un-scrutinised import of 'intellectual wastes' at policymaking. More importantly, there is an urgent need for restructuring our economy -- greater equity for an enlarged domestic market, helping local industries to switch to that market, and greater caution with the 'bubbles'. The last thing we would want is turning into an instrument of the 'War' that many predict inevitable for recovery in the West!

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