Senators say Greenspan is running out of bullets

by Chris White

On July 21, Federal Reserve Chairman Alan Greenspan presented his semi-annual "Humphrey-Hawkins" evaluation of the state of the U.S. economy to the Senate Banking Committee. The report is named for legislation which tied unemployment rates to national security as a prime concern of national policy.

The hearings were not the typically cozy, mutual stroking sessions which usually take place between the legislators and the Fed's chief bureaucrat. This time the gloves were off. Greenspan was treated with a rudeness not usually seen in such appearances. His opening testimony was interrupted by Michigan's Senator Riegle. The substance of his remarks was demolished by Paul Sarbanes (D-Md.), quoting from Greenspan's testimonies of the last year and more. But Sarbanes had not even been present when Greenspan delivered his prepared remarks. All in all it was quite a humiliating day for the jazz clarinetist and sometime companion of NBC's battle-scarred journalist Andrea Mitchell, who was elevated way out of his league to end up as head of the Federal Reserve.

Greenspan was hauled over the coals in a number of different ways, and President Bush and the Brady Treasury Department were dragged along in his wake. Chief among them were his record over the last year and half. Senators James Sasser (D-Tenn.) and Alfonse D'Amato (R-N.Y.) griped: "You're always after the fact. You're always trailing economic developments." And committee chairman Donald Riegle (D-Mich.): "Why is there any more reason for us to think you're right this time, when we look at the record and see that you've said essentially the very same thing in past months, and it has turned out not to be right?" Greenspan had basically taken the tack of arguing that everything is more or less on the right track, and if we only persevere, all will eventually turn out okay.

Particular emphasis was placed on the failure of Greenspan's 23 successive reductions in interest rates to get the economy moving again, and on the collapse of employment, unforeseen by him in his earlier testimonies. Earlier in the year he had told the Senate that if the official unemployment rate were to go above 7%, he would have to conclude that there was not only no recovery, but a recession. Now, with the narrowest of the government's measures showing 7.8%, and a new round of job eliminations in the works, he is still looking forward to eventual recovery.

Bailing out the banks

Charges also flew thick and heavy, that his interest rate reduction policy has only been intended to bail out banks. This time around, Greenspan was accused of "conflict of interest" in his dual capacity as manager of the nation's money supply and regulator of some of the biggest banks. Senator Sasser accused him of organizing a taxpayer bailout for the commercial banks. "We're reducing rates, and the banks are using the reduced rates to cut the return they give to savers. They in their turn take the funds and invest them in government securities, and we now find that the banks, in my view, are getting wealth from their ill-advised leveraged buyout policies. In effect, the taxpayers are bailing out the banks for their problem loans of the 1980s, and the CD holders are helping to pay the freight of it."

Greenspan's testimony, as well as his next day's report to the House Banking Committee, was organized around precisely this idea. He calls it "rebuilding balance sheets." It now turns out, from the mouth of the Fed chairman himself, that lower interest rates have not been intended to bring about an economic recovery, but rather to prevent an uncontrolled meltdown of the financial system. That's no surprise to *EIR* readers. Greenspan put it this way: "The successive monetary easings have served to counter these contractionary forces, fending off the classic bust phase that seemed invariably to follow speculative booms in pre-World War II economic history. Lower interest rates have lessened repayment burdens through the refinancing and repricing of outstanding debt. And, together with higher stock prices, have facilitated the restructuring of balance sheets."

Blacker than Black Monday

Greenspan's testimony was presented just one day after his 23rd reduction in interest rates brought the world financial system to the brink of the precipice for the first time since the Black Monday global stock market meltdown in October 1987.

The dollar was in free-fall, nearing its post-World War II low against Germany's deutschemark. Stock markets plunged, down 7% in Italy and Sweden, 4% in Japan, 3% in Germany and France, and 2% in Britain. Panic intervention from central banks in Europe and North America attempted to stem the tide.

Some said it was the combination of the Democratic presidential nomination of Bill Clinton, and the campaign pullout of non-candidate Ross Perot, which did it. Others said it was the decision by Germany's central bank, the Bundesbank, to increase interest rates which set everything off.

What has finally begun to hit is the reality that the United States is bankrupt—financially, economically, and politically. As the publication of June's 7.8% unemployment report supposedly confirmed, Greenspan's lowered rates again failed to give the economy a kick and stimulate recovery. After 23 times, such stories wear a bit thin, even for the most credulous. As Senator Riegle bitterly remarked: "I don't think you see the risk in terms of all the damage that is happening to the economy. You don't seem to be able to see that. You can see the future risk, the inflation risk, but the damage in terms of all the unemployment, all the business failures, loss of confidence, and the massive job eliminations: Look at that, and you have a very benign reaction to it."

The new round of financial collapse is the not-so-delayed reaction to the obscenity which unfolded in Munich, Germany on July 7 in the name of the summit of the Group of Seven countries. There, it became apparent that the policymaking structures of the western world have broken down. There isn't a recovery, and there won't be one, without a fundamental shift in policy-orientation. Yet, here was the supposed leadership of the world, acting out roles which could have been assigned to any of the unfortunates who have adopted names like Alexander, Julius Caesar, or Bonaparte, in psychiatric wards around the world.

There was Bush and company, fresh from the recognition that there would be no "recovery" to bail them out till November, insisting that "character" and "family values" would be hot election issues, not the economy. France's François Mitterrand, his country gridlocked by transport strikes, facing a social explosion. Italy, set perhaps to become the first industrialized nation to default on its state debt. John Major's Britain, where unemployment is over 10% and rising, and bankruptcies and foreclosures are at rates not seen since the 1930s.

That's why the worldwide panic of July 20, and the central banks' intervention, mark a turning point. The world financial system and economy is running out of control, and nobody is minding the store. Back to the fore of the agenda has come the crisis which too many people had been prepared to believe was under control: the depression bankruptcy of the United States.

The July 20 events were more than just a backdrop. They gave Senators Sasser and Riegle the opportunity for one final twist of the knife as Greenspan concluded his testimony. As Sasser put it: "I think you're running out of bullets over there at the Fed . . . because the Germans are not cooperating with you. You're running out of options." Riegle supported him in this way: "We're wedged into a corner here where decisions in foreign countries, like for example, Germany, are becoming very difficult for us to deal with because of the implications for us and how weak our economy is. . . . If in fact you're out to the end limits of what you can do—and that's the cold hard fact of the matter—then I think we have to begin a discussion about what other tools are available in other directions."

Both senators emphasized what will no doubt become obvious very shortly. The Bundesbank's decision to increase its discount rate has eliminated Greenspan's ability to lower interest rates any further, for example, at the end of September, in time to give another kick to Bush's reelection campaign. They point out that if Greenspan cannot lower interest rates, and if he is to act on his double-talking opposition to a free-fall in the dollar, then U.S. interest rates are going to have to start to go back up again. Or standing policy will have to be changed.

Meanwhile, it seems that Germany's central bank will raise interest rates again at its next council meeting in August. Again the events on July 20 showed that Greenspan and company are lagging after events. If his interest rate reduction option is removed, then all his claims about "fending off the classic bust phase" will be proven to be hot air.

Sasser, Sarbanes, and Riegle are, of course, Democrats. Their name for a different policy is "fiscal stimulus," featuring "make-work" programs fixing up roads and bridges and the like. The next day, they opened up their committee to hear the view of Clinton's economic advisers such as Lester Thurow, and of Peter Petersen of the Council on Foreign Relations.

They've got the symptoms down pat, but as for solutions, that's a different matter. Now is the time to take up Lyndon LaRouche's legislative draft and federalize the Federal Reserve, to make credit available for job creation in basic economic infrastructure, industry, and agriculture. That's the way out of the abyss Greenspan and company have pushed us into.