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Greenspan and Volcker Play Public For Suckers

by John Hoefle

With talk of recovery coming out of one side of the U.S. Federal Reserve's mouth, and discussions of the possibility of emergency market interventions coming out of the other side, the disparity between the propaganda and reality is growing by the day. While the suckers are bombarded with false statements and fake statistics designed to induce the hope that all is well, financial corporations are rushing to plug holes in their balance sheets, and both current Fed Chairman Alan Greenspan and his predecessor, Paul Volcker, are struggling to keep the seismic shocks hitting the global financial system from bringing the entire house of cards down.

If anything is clear in the post-Enron period, it is that the financial speculators cannot be trusted to police their own behavior, and that the Federal government must abandon the policy of deregulation—a policy which has blown up in their faces—and return to a sane regulatory policy which keeps the speculators' addiction to cheating and corner-cutting in check. Enron's wild hiding of losses and debt should be enough to convince any sentient being that relying on crooks to police themselves is a prescription for disaster. But, as is often the case, what is obvious to most, is not obvious to the Fed's Dr. Greenspin, who continues to insist that regulation—not fast and loose, book-cooking corruption—is the real danger.

'Trust Us,' He Pleads

In a March 26, speech at the Stern School of Business at New York University, the Chairman of the Bubble did allow that "our most recent experiences with the bankruptcy of Enron and, preceding that, several lesser such incidents, suggest that the governance of our corporations has strayed from our perceptions of how it is supposed to work." Despite the fact that you could drive a truckload of weasels through that sentence, it does at least seem to admit that there is the possibility of an appearance of a potential problem. Still, Greenspan suggests, the marketplace is the best regulator, relying on corporate officers, backed by shareholder pressure when needed, to keep companies in line. The one thing we don't want, he said, is more regulation.

"We have to be careful, however, not to look to a significant expansion of regulation as the solution to our current problems, especially as price-earnings ratios increasingly reflect the market's perception of the quality of accounting," Greenspan said. "Regulation has, over the years, proven only partially successful in dissuading individuals from playing with the rules of accounting."

It's perfectly normal to want to scream when reading such a sentence, with its deadpan call for the inmates to be allowed to run the asylum. The part about the price-earnings ratios is especially cute, since in these days of falling corporate income, a rising P/E ratio is often an indication that profits are falling faster than the stock price.

What Greenspan is actually saying, is that in times of crisis—and we're in the big one—it is important to keep all options open, including the ability to cook the books as needed to maintain the perception of solvency. The rule of the day is: See no bankruptcy, hear no bankruptcy, speak no bankruptcy.

That same point is being made by the Fed's Queen Mother, Paul Volcker, who is attempting to ride to the rescue of Arthur Andersen, the accounting firm which seems to specialize in being hoodwinked by its clients.

Andersen was indicted by the Federal government for obstruction of justice, after the company engaged in widespread shredding of Enron-related documents in several of its offices around the world. Hit with a criminal indictment, Andersen's customers began defecting in droves. In response, Volcker forced out Andersen Chief Executive Joseph Berardino and proposed to the Department of Justice that he would appoint a new board to run the firm, if the Feds would drop the indictment.

Volcker is an old hand at this. He joined the Fed in 1979 to implement the New York Council on Foreign Relations' "controlled disintegration" deindustrialization policy; his role is not so much to protect Andersen, as to make sure that any investigation into Andersen's activities doesn't expose the larger scam of which Andersen was a part. Volcker knows where the bodies are buried, because he helped dig the graves.

Both Volcker and Greenspan have the same job, that of keeping the U.S. government out of the hair of the international financier oligarchy, while the oligarchy tries to manage the collapse of its financial system by pushing the losses onto the public.

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TABLE 1

Changes at J.P. Morgan Chase & Co. and Its Lead Banks During Fourth Quarter 2001

($ Billions)

	Assets	Derivatives
Third Quarter		
Chase Manhattan Bank	435	17,996
Morgan Guaranty Trust	228	12,597
Two banks combined	663	30,593
Fourth Quarter		
JP Morgan Chase Bank	538	23,533
Change	–125	–7,061
Holding Company		
Third Quarter	799	24,148
Fourth Quarter	694	23,904
Change	–106	–244

Sources: Office of the Comptroller of the Currency, *EIR.*

TABLE 2

Assets and Derivatives at Top U.S. Derivatives Bank Holding Companies

($ Billions)

Rank	Bank Holding Company	Assets	Derivatives
1	J.P. Morgan Chase & Co.	694	23,904
2	Bank Of America Corp.	622	9,399
3	Citigroup Inc.	1,051	9,191
4	Wachovia Corp.	330	2,088
5	Wells Fargo & Co.	308	843
6	Bank One Corp.	269	798
7	Bank Of New York Co.	81	379
8	HSBC North America	110	353
9	FleetBoston Financial	204	312
10	Countrywide Credit Ind.	37	279

Source: Office of the Comptroller of the Currency.

Melting Down

The evidence is growing that what Greenspan and Volcker are so desperate to cover up, is a major derivatives disaster which occurred in mid-2001, and remains unsettled. Such events are never publicly announced, but the responses to them are often visible.

The most dramatic example that something went seriously awry can be found on the books of J.P. Morgan Chase & Co., which bears the deadly distinction of being the world's top derivatives bank. The bank is actually a combination of three top derivative banks: Chemical Bank bought Chase Manhattan in 1996, changing its name to Chase; then bought J.P. Morgan & Co., in a deal which closed at the end of 2000. During the fourth quarter of 2001, the bank holding company merged its two lead banks, Chase Manhattan Bank and Morgan Guaranty Trust, into a new bank, J.P. Morgan Chase Bank. It appears that this merger was used to hide significant problems.

At the end of the third quarter, Chase Manhattan Bank and Morgan Guaranty Trust had combined assets of $663 billion, and $30.6 trillion in derivatives (**Table 1**). Three months later, the newly formed J.P. Morgan Chase Bank had $538 billion in assets and $23.5 trillion in derivatives, a decline of $125 billion in assets and $7.1 trillion in derivatives. In terms of assets, that's the equivalent of losing a Top Ten bank (number nine, National City Corp., had $106 billion in assets at the end of 2001), while the drop in derivatives is more than the total assets of the U.S. banking system ($6.6 trillion at year's end). It is also the equivalent of losing the fourth-largest derivatives bank holding company in the nation (**Table 2**).

These staggering changes went largely unmentioned. J.P. Morgan Chase & Co.'s explanation of its asset decline, in a press release announcing its fourth-quarter results, blamed "the majority of the reduction" in the assets of the holding company on "the resolution of the industry-wide clearing and settlement problems experienced in September." That statement raises more questions than it answers, since the existence of such post-Sept. 11 problems was roundly denied at the time.

Then we have the giant Citigroup, which sold 21% of its Travelers Property Casualty unit in an initial public offering on March 21, raising $4 billion. Citigroup said it was spinning off Travelers (it will distribute the remaining 79% to shareholders later this year) to concentrate on faster-growing businesses, but that explanation also raises questions. After all, when Travelers bought Citicorp in 1997, it cited the supposed synergy from the combination of commercial banking, investment banking, and insurance. So, either the synergy didn't work out, or the bank needs the money for reasons it prefers not to disclose. Our guess is that both are true, since most big bank mergers are actually bailouts in disguise.

Morgan Stanley also got into the act, borrowing $7.3 billion through bond sales on March 27, the largest bond sale ever conducted by a securities firm.

Another company which may be in trouble is General Electric, which borrowed $11 billion through bond sales in March, and is reportedly considering selling its Employers Re unit, the world's fourth-largest reinsurance company. GE is both a major industrial company and a financial company, getting half its income from its industrial operations and half from its financial operations and its NBC

broadcasting unit.

On the industrial side, GE is likely being hit hard by the overall decline in manufacturing in the United States, as well as a significant decline in its power systems unit, due to the drying up of orders for natural gas turbines for the electricity market. In the post-Enron period, many of the energy pirates have dramatically scaled back their plans for new natural gas electricity-generating plants. Power Systems accounted for one-third of GE's non-financial operating profit in 2001, pulling in $5.2 billion, compared to $2.8 billion in 2000.

GE has also been in the news due to its involvement with Enron, having been partners in some of Enron's off-balance-sheet deals and its New Power Company retail power company. Given that GE has been widely praised for its financial machinations in recent years, including off-balance-sheet activities, serious questions exist about what might be lurking on and off the company's books.

One person raising questions about GE is Bill Gross, the head of Pacific Investment Management Co. (PIMCO), the world's largest bond fund. In his March newsletter, Gross called GE "a conglomerate financed by a money machine—its subsidiary GE Capital . . . using near hedge-fund leverage." "Without benefit of this leverage afforded them by [Wall] Street," Gross wrote, "their operations to me resemble more closely the failed conglomerates of yesteryear such as Gulf + Western and LTV. PIMCO will own no GE commercial paper in the foreseeable future."

Unsustainable

Despite all the behind-closed-doors maneuvering of Greenspan, Volcker, and company, their system is collapsing. While the physical economy goes under, the level of debt, derivatives, and other financial aggregates continues to soar. The derivatives holdings of U.S. commercial banks increased by $11 trillion in 2001, up 27% over 2000, while credit-market debt rose by $2 trillion, or 7%. This combination of rising claims and physical decline, defines a process which is clearly unsustainable.

The suspicion is growing that many of the headlines we see today, are actually reflections of a big derivatives blowout last year, involving J.P. Morgan Chase and Citigroup. The presence of these banks, as well as Arthur Andersen, at a number of high-profile disasters over the last few months, also suggests the possibility that, contrary to the impression given in the press of a series of random bankruptcies, a particular network is being rolled up, as part of a larger derivatives workout process.

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