

# SAN DIEGO WEEKLY Reader

## Free Lunch for Banks

1/13/2010

**By Don Bauder**

Perhaps you are comforted believing that the U.S. government, Federal Reserve, and Wall Street are all working assiduously to provide you with a job. Ha ha ha ha. Not so. The Federal Reserve, our central bank, is loaning money to banks at zero percent, and the banks can gamble with that free money, knowing that if their bets backfire, the government will bail them out. The head of the Federal Reserve, Ben Bernanke, says he will keep doling out free money to Wall Street and other banks as long as unemployment remains high.

And you think Wall Street wants unemployment to go lower? Silly girl/boy! Wall Street is feasting off Main Street's pain. In theory, financial institutions should loan out the money it gets from the Federal Reserve. But it's not happening. Gambling has been so much more profitable — and fun.

Long range, Wall Street needs a prosperous Main Street, says economist Murtaza Baxamusa of San Diego's Center on Policy Initiatives — but, “in a perverse way,” the moneybags would prefer that the employment recovery not come right away. By gambling in currencies, stocks, bonds, and commodities with that free money, the banks are building up their reserves — dangerously depleted because of the popping of that bubble they created. That's the banks' and the Fed's top priority. Not Main Street's.

First, you have to understand that the Federal Reserve is essentially owned by banks. Its mandate is to keep the banking system intact. The Fed's decisions are not ratified by the administration or the Congress, although the government has appointment and oversight power over the central bank, which gives lip service to citizens' well-being. Recently, Bernanke said his only concern was Main Street's economic health, not the banks' health. His nose extended out six feet after making the preposterous assertion. Bernanke works for the banks. He even rubs it in. He is always reassuring Wall Street that inflation is not around the corner. Wages aren't rising, he boasts. Do you find that comforting?

“The Fed is a captive of the large commercial banks as well as Wall Street bankers and, as such, will do what is generally believed to be in those constituencies' best interest,” says Arthur Lipper III of Del Mar, a Wall Street veteran and international financier. “The Fed has become an agent for Wall Street and will keep interest rates low until a significant fall in the U.S. dollar” forces a rate increase. (The dollar has been plunging for years against other currencies.)

“Are Wall Street and the banking system getting rich at the expense of Main Street?” asks E. James Welsh of Carlsbad's Welsh Money Management. “The answer is an unequivocal ‘yes.’”

But he doesn't think the Fed is just sating Wall Street's greed. “The Fed doesn't have a choice in terms of keeping rates near zero,” says Welsh. Despite the propaganda, banks have not regained their health, Welsh says. Similarly, “Housing has not bottomed,” and commercial real

estate is a disaster. The Fed is loaning money at zero because “it is trying to make banks profitable so that they can absorb additional losses that are coming — commercial real estate, credit cards, every form of credit.”

President Obama publicly urges the banks to make loans, but it is empty rhetoric. There is not that much demand for loans anyway. Of course, consumers and businesses can't borrow at zero. Thirty-year fixed mortgage rates are over 5 percent, and the average rate on credit cards went above 16 percent in December.

Main Street is being hit by a triple whammy. Not only do we pay high interest rates while the banks pay zero, but we also get exceedingly low interest on our savings accounts and money market funds. The rates are so low it almost forces us to buy bonds or high-yielding stocks to get income. The Fed is fixated on jacking up the stock market, stating that half of Americans have money in the market directly or indirectly. That's true, but stocks are overwhelmingly concentrated in the hands of the rich, who are effectively getting even more government welfare. So the Fed's policy further exacerbates the huge income and wealth gap between the rich and the rest of us.

Meanwhile, companies strive to keep costs down to make their stocks more attractive. So they are not boosting employment. “Not hiring is one thing,” says Baxamusa. “But the egregious nature by which top executives are giving us the middle finger hurts. Top executives are making 300 times what the average worker makes,” and on Wall Street the ratio is even higher.

The banks are paying back government loans so they can dodge federal rules and pay their chief executives outlandish salaries — a dubious way to gain popularity on Main Street. These same banks are unwilling to dump smelly assets and take losses, rather like the way Japanese “zombie banks” did for so long. Risky mortgage-related paper stays on American banks' books, so woes are pushed into the future. Worse, the banks — whose greed and stupidity led the world to the brink — are fighting attempts to introduce stringent regulation that would prevent or at least slow down another lemming march.

It's bad enough that the big banks and the central bank would like to see unemployment last longer. But there are other reasons why rehiring will be painfully slow: “I do not believe there is any reason for most companies to begin hiring again, as they are operating more efficiently now than before and lots of companies have learned to make do with fewer personnel,” says Lipper. “With the cost of employee benefits rising, there is less incentive for companies' hiring and training people.”

Says Baxamusa, “One of the key problems is the lack of accountability of the financial services industry. In the last decade, the nation was built on a house of straw — essentially Wall Street paying executives to blow up balloons rather than hire workers to produce goods. It was an artificially inflated economy.”

All too true. So if it's futile to put money in a savings account, what do you do? Buy stocks, bonds, commodities? Welsh says all this Fed and government stimulus “has produced a hollow recovery — more challenging than anything we have seen since the 1930s.” Sometime this year, perhaps, the artificially supported economy will run out of gas. The consumer is 70 percent of the U.S. economy. The federal authorities' decision to let unemployment rise while ministering to the banks will backfire. It's possible 2010 will be as bad as 2008, says Welsh. “The cupboard is bare. Social ramifications will be ugly,” he says. He fears deflation. Stocks could crumble again. Because of troubles abroad, the dollar could rise and push gold down.

Lipper, however, says, "I believe inflation is inevitable and that the U.S. dollar will decline." He would avoid most U.S. securities but likes precious metals, Asian currencies, and royalty entitlement contracts, by which a company seeking capital can sell 3 percent of its revenues for 20 years instead of selling its stock. Lipper pioneered the concept.

In any case, Baxamusa, Welsh, and Lipper agree: It will be rough for a while.