Financial Meltdown: The Financial Edifice of U.S. Imperialism is in Danger of Crumbling

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The events of the last ten days on Wall Street represent a new and more destabilizing phase of the turmoil gripping financial institutions and markets in the U.S. A financial crisis has been unfolding for more than a year. It is now the most serious financial crisis of U.S. capitalism since the Great Depression of the 1930s. And it is by no means contained or under control.

The financial edifice of U.S. imperialism is in danger of crumbling. And the U.S. ruling class is cobbling together desperate measures to prevent wholesale collapse.

This analysis examines the recent eruptions on Wall Street of mid- and late September and the deeper structural causes of the crisis.

I. Wall Street Panics, the Guardians of U.S. Capitalism Scramble

A). A Week of Deepening Financial Crisis

Two of the last two independent investment banks on Wall Street ceased to exist in mid-September. In a matter of hours, Lehman Brothers went bankrupt on September 15, while Merrill Lynch was forced into liquidation and then absorbed by Bank of America. This follows the government-promoted buyout in April of Bear Stearns, another giant investment banking firm that was on the ropes, by JPMorgan Chase.

It was only several weeks earlier that the U.S. government had taken over the two major and failing mortgage-finance giants–Fannie Mae and Freddie Mac. At the time, this takeover was presented as providing an effective firewall against future financial eruptions. But it proved to be no more than the patching up of a pothole during an earthquake. This past week the government had to take over the American International Group (AIG), the giant insurance-financial firm.

AIG had over a trillion dollars in assets. It had earned enormous profits from insuring mortgage-backed investments circulating in the financial system that were held by other banks. But this has turned into a disaster. Here is some of what happened:

Through deceit and aggressive marketing, banks pushed mortgages on people. The Federal Reserve Bank had pumped low-cost funds into the banking system to prop up mortgage loans. These loans were then combined into larger groups of loans by investment banks (like Lehman Brothers) and turned into financial products that were sold on financial markets. All kinds of lending took place with these original loans as collateral. But when housing prices fell, and mortgages could not be paid, much of this collateral became worthless.

AIG was insuring much of this lending against the risk of loss. But as the losses mounted astronomically, AIG could neither cover the costs of backing this debt nor borrow funds on the financial markets to keep itself afloat.

The financial markets had basically lost confidence, and AIG's assets tumbled in value. AIG was in danger of collapse. But if AIG went under, the probability was great that it would have taken down other financial institutions with it. This forced the government's hand.

Normally, so-called bad debt is marketed at distress prices. During the financial storm of mid-September, not only were there no takers for debt but it also proved impossible for the financial markets to establish any kind of value on this debt.

As the pace of the financial crisis grew more frenetic during the week of September 15, the U.S. ruling class was faced with a two-fold danger: additional and cascading losses and bankruptcies in the financial sector; and the possible choking up of lending channels, which could send the economy as a whole into a rapid downward spiral.

On September 19th, the U.S. government announced what will likely turn out to be the largest bail-out operation in U.S. history. Its initial cost is $700 billion, and this is on top of the $200 billion earmarked to shore up Freddie Mac and Fannie Mae and the $85 billion to bail out AIG.

B). International Dimensions

This is a rolling financial and credit crisis. It is amplifying internationally with bursts of instability. In the midst of last week's U.S. market gyrations, the Russian stock market sank and shut down for two days. In other parts of the world, concern spread about whether dollar-based loans in global markets would continue on the scale necessary to sustain daily business operations. In response, the central banks of Germany, Japan, England, Canada, and Switzerland pumped some $185 billion into the financial markets. And investor worry is mounting in East Asia. China, Japan, and South Korea, for instance, count on the U.S. as a major export market.

One of the most significant features of world growth and expansion over the past decade has been the deepening integration of the world capitalist economy. This is happening both on the level of production and trade—like the parts that go into an automobile being manufacturing in different factories around the world. And it is happening at the level of finance—where banks are more globally and tightly interlinked with one another through chains of borrowing and lending and even, as in the case of AIG, insuring the risks of borrowing and lending.

The rescue operation announced by the U.S. government was motivated, on the one hand, by the need to stanch the bleeding of the U.S. financial system; and, on the other, by the need to restore international confidence in the U.S. economy.

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