

Liquidity to Keep the Financial System from Collapsing in a Heap

By [Mike Whitney](#)

Global Research, August 31, 2009

31 August 2009

Region: [USA](#)

Theme: [Global Economy](#)

Ben Bernanke never should have been reappointed as Fed chairman. Obama made a big mistake. The main thing to remember about Bernanke is that, in the two years since the financial crisis began, he's made no effort to force the large banks and financial institutions to write-down their losses. Nor has he pushed for the regulations that are needed to restore confidence in the system. The credit system is still clogged because the banks are buried under \$1.5 trillion in toxic assets and non performing loans which are defaulting at the fastest pace on record. At the same time, Bernanke has failed to push for reform of derivatives trading, off-balance sheet operations, securitization or capital requirements for financial institutions. The good news is that Bernanke has demonstrated great creativity in providing sufficient liquidity to keep the financial system from collapsing in a heap. The bad news is that the core problem is not liquidity at all, but solvency. A good portion of the banking system is underwater. That's why Bernanke's actions have been a complete flop.

The banks can't fix themselves, because-to do so-would drive many of them out of business. If the FDIC doesn't sort them out, they will continue to be a drain on public resources. Lending will continue to contract and GDP will shrink. That's what is happening now, except Obama stimulus has triggered a slight uptick in growth that is being confused for recovery. But there is no recovery. Things are simply getting worse at a slower pace. That's to be expected. Housing prices will not go to zero; they flatten out over time. That doesn't mean things are getting better. They're not; they're getting worse. Personal consumption is in the tank, business investment has never been lower, the rate of bank failures is accelerating, and unemployment is headed higher. So where are the "green shoots"?

The only real cure is political. The notion that the market will fix itself is pure fantasy. We are following the same path as Japan-perennial recession.

Many people believe that the Federal Reserve is the head of a banking cartel. But that's not entirely true. Bernanke is actually an employee of the banking cartel; an apparatchik who carries out the policies that best serve the interests of his constituents. The Central Bank's serial bubblemaking has been a successful means of transferring capital from working people to the investor class and corporate elites. The facts speak for themselves.

A report by University of California, Berkeley economics professor Emmanuel Saez concludes that income inequality in the United States is at an all-time high, surpassing even levels seen during the Great Depression.

The report shows that:

* Income inequality is worse than it has been since at least 1917

* “The top 1 percent incomes captured half of the overall economic growth over the period 1993-2007”

* “In the economic expansion of 2002-2007, the top 1 percent captured two thirds of income growth.”

The Fed disguises its stealth-looting of the middle class with ideological mumbo-jumbo about “supply side” this and “trickle down” that. Ripping off working people has a long history going back 30 years Reagan’s “Voodoo” economics, but the severity of the current recession has pitted market fundamentalism against the sobering reality that the US consumer is not an inexhaustible resource. Debt-fueled consumption has reached its apex and is descending rapidly. This is apparent in all of the recent research and data. Between 2000 and 2007 US households increased their aggregate debt by nearly \$14 trillion. The household debt-to-disposable income ratio rose to 135% and has only recently declined to 128%. For the first time in 60 years, households have begun saving. (although much of what is classified as “saving” is, in reality, just paying down debt) The larger point is, that US consumers are undergoing a generational shift and will not be able to lead the way out of the recession as they have in the past. Nor will they miraculously “bounce back” and provide demand for products made abroad. In fact, the export-driven model (Germany, South Korea, Japan, China) is sure to be challenged in ways that were unimaginable just two years ago. With credit lines being cut, and outstanding credit shrinking by trillions in the past year alone, and unemployment nudging 10 per cent (16 per cent in real terms) the consumer will not be the locomotive driving the global economy. Credit destruction, asset firesales, defaults, and foreclosures will continue for the foreseeable future choking off growth and pushing unemployment higher. Consumption patterns are changing dramatically, although their impact won’t be fully-felt until government stimulus programs run out. That’s when the signs of Depression will become apparent once more.

This is why Bernanke should never have been reappointed as chairman. Bernanke has a good grasp of the issues—underwater banks, overextended consumers, exotic debt-instruments (derivatives), and an out-of-control financial system—but he refuses to do anything about them. The institutional bias of the Fed provides no wiggle-room for structural change. The Fed represents the status quo.

Bernanke’s reappointment isn’t just wrong because he failed to detect the biggest housing bubble of all time, or for supporting the loosey-goosey monetary policies which triggered the current Great Recession, or for shrugging off Congress’s attempts to audit the Fed, or for rejecting Bloomberg News (legal) claims that the Fed should release information about which financial institutions received \$1.5 trillion in Fed loans, or for \$12.8 trillion to keep a corrupt and insolvent system operating while millions of working people lose their homes, their jobs and their prospects for the future. These are bad enough, but, worse still, is the fact that Bernanke’s strategy has no chance of succeeding; it just kicks the can further down the road.

The economy is experiencing system-wide deleveraging and deflation is now visible in every sector of the economy. Exports are down, so is trucking. Railroad freight is off 18 per cent year-over-year. Department stores, building materials, restaurants, furniture sales,

appliances, travel, retail, outdoor equipment, tech; down, down, down, down, down and down. You name it; it's down. Consumer credit is plummeting and personal savings are up. Industrial production is down, PPI down. Capacity utilization has slipped to 68.5 per cent.(another record) There's so much slack in the system, inflation could be low for years. Commercial real estate—a \$3.5 trillion industry—is plunging faster than residential housing. Corporate bond defaults are at record highs, Treasury yields are flat, and the dollar index is teetering at the brink. It's a wasteland.

Bernanke has put himself and the country in the direct path of a debt-liquidation avalanche; a near-endless flow of rising defaults, foreclosures and bankruptcies. His liquidity injections and monetization programs have inflated another speculative bubble in the stock market, but eventually that will run its course and stocks will retest their March lows. The massive debt-purge will continue despite the Fed chief's best efforts. The trend is irreversible.

Debt-reduction can't be put off forever. Markets eventually "correct" and red ink gets mopped up. That's just the way it is. Bernanke is simply trying to prevent the market from clearing. It's futile. And, that's why he shouldn't have been reappointed.

The original source of this article is Global Research
Copyright © [Mike Whitney](#), Global Research, 2009

[Comment on Global Research Articles on our Facebook page](#)

[Become a Member of Global Research](#)

Articles by: [Mike Whitney](#)

Disclaimer: The contents of this article are of sole responsibility of the author(s). The Centre for Research on Globalization will not be responsible for any inaccurate or incorrect statement in this article. The Centre of Research on Globalization grants permission to cross-post Global Research articles on community internet sites as long the source and copyright are acknowledged together with a hyperlink to the original Global Research article. For publication of Global Research articles in print or other forms including commercial internet sites, contact: publications@globalresearch.ca
www.globalresearch.ca contains copyrighted material the use of which has not always been specifically authorized by the copyright owner. We are making such material available to our readers under the provisions of "fair use" in an effort to advance a better understanding of political, economic and social issues. The material on this site is distributed without profit to those who have expressed a prior interest in receiving it for research and educational purposes. If you wish to use copyrighted material for purposes other than "fair use" you must request permission from the copyright owner.

For media inquiries: publications@globalresearch.ca