

Meltdown – A Global Tsunami – Part 2

(Part 1 was post in June 28, 2015 Weekly Offerings)



The failure of Lehman Brothers the largest bankruptcy in US history had sent financial markets into a tailspin. The New York markets had had its biggest one day drop since the 911 attack what markets from Shanghai to Paris falling in lockstep. Russia suspended all trading. In an epidemic of fear the world's major banks stop lending money and accepting collateral from each other. The next morning at precisely 10:15 a.m. President George W Bush of the Oval Office to try and reassure the public. Bush convene an emergency meeting in the White House's Roosevelt Room where Treasury Secretary Hank Paulson told the President that the United States was on the verge of a total financial melt down. He said that, *"if we don't act BOLDLY, we could be in a Depression Deeper than the Great Depression."* Paulson also said, *"This is the Financial Equivalent of War and we're going to need Wartime Powers."*

For the next several days Hank Paulson was the de facto President of the United States. And the man who was supposed to be the free enterpriser in the Bush Administration ended up overseeing the greatest government intervention in the economy since the Great Depression. And all goes back to his key decision to allow Lehman Brothers to fail. Still at a press conference in the White House briefing room Paulson seem almost flippant of the catastrophic bankruptcy, saying that it was not the role of Government to save private businesses.

Except that linen failure has repercussions around the world. Millions and millions of people would lose their life savings. Pension plans were decimated. French Finance Minister Christine Lagarde will play a key role in the crisis. Although she was a close friend of Hank Paulson she publicly called his Lehman decision horrendous, "as all banks suddenly realize, that no one was safe and that any bank could fall."

The immediate impact came in London when Lehman Brothers UK office had to immediately shut down where a lot of trading was done through its subsidiary in London and every Friday it would send all its cash back to New York so on the Monday morning in London there was no cash. The holding company had gone into Chapter 11 and there wasn't a penny to pay the staff. Obviously this was the worst way one could possibly close a bank making the uncertainty on Day One huge and very damaging. This caused Lehman's investors, not just in Europe and Asia but also in the United States and everywhere all of a sudden had no access to their cash and that sets and as a result was forced to start selling down their own assets at fire sale prices as they were getting margin calls producing a vicious cycle.

And none of this was foreseen by the regulators and Wall Street as panic rose in the international financial markets, especially when it began to look like many banks might follow Lehman into the abyss freezing international trade credits.

Immediately after, there was another crisis when American International Group better known as AIG and the world's biggest insurance company look like it was going to collapse when it emerged that the dealings of one obscure executive and the entire world's financial system. His name was **Joseph Cassano** and he was the head of the financial products division at AIG in London. He had moved to London because the kind of trading he did was banned in the United States. Cassano would insure companies against the failure of the business partners, which was a very risky thing to do. But in conference calls with his investors he claimed that it was a no lose proposition... *"It is Hard For Us, without being Flippant, to Ever See a Scenario... that would see us losing One Dollar in any of those Transactions."* Joseph Cassano's bet was that a lot of banks and mortgage companies around the world could never fail all at once. So in September 2008 when many banks around the world began collapsing Cassano's risky Insurance Scheme push AIG to the edge of bankruptcy.

Initially Hank Paulson proclaim that he had no intention of saving AIG as the truth of AIG is desperate financial situation came to a complete shock to the Secretary and all regulatory agencies in the United States. A complete surprise which is an indictment of the country's regulatory system because how could anyone be surprised by something that is so big and so dangerous that if it gets in trouble you have to spend hundreds of billions of taxpayer's dollars to put it out of its misery.

Nobody knew just how big casino AIG was running. The reality was that AIG what such a monstrous creature with tentacles and so many parts of the financial system that if you had let a AIG go down you really would have been risking dragging most of the West's financial system with it. Eventually Paulson bowed to the inevitable saving AIG with \$85 billion of taxpayer's money. Obviously Joseph Cassano was fired by AIG **but he walked away with \$350-million dollars in severance.** SOMETHING IS WRONG WITH THAT!!!

On September 18, 2008 Hank Paulson and U.S. Federal Reserve Chairman Ben Bernanke went to ask congressional leaders for more power and several hundred billions dollars to

staunch the bleeding. Bernanke told the people that if the government did not put up money immediately to bailout the financial system there would be another Great Depression stunning the leadership of both political parties at the meeting.

Although at that time people were focusing on Bear Stearns and Lehman Brothers but the real danger was the possibility of Goldman Sachs, Morgan Stanley, GE and the other major financial institutions falling like dominoes. Paulson realized that he had to pump government money into the financial system to enable banks to resume lending to consumers and to each other. He came up with a plan call **TARP** the "**Troubled Asset Relief Program**", the government would use taxpayer money to buy the banks troubled assets.

Hank Paulson, who was not well liked in Washington showed up with a ten-page plan that was immediately rejected by Congress causing the stock market to fall off a cliff. In the end they Paulson got the money and the powers, but signs of the of a depression began to surface immediately as within several months there were more than one million home foreclosures, with the greatest number in California. Two years later the foreclosure rate was still increasing.

The ugliest part of this saga was the human tragedy of hundreds of thousands of families now living in their vehicles or on the street. We are talking about the elderly, disabled, single mothers with little children, people who lost their jobs and those who have a medical or mental health condition. Although the actions of banks raised the ire of politicians locally, on the state-level and in Washington, little was done to relieve their pain. Worst of all, most of these people had no clue to how to defend themselves legally when their homes were foreclosed and when they were dislodged from their homes which were sold to others.

While at the same time to provide liquidity Hank Paulson gave the major (9) banks \$250 billion. Which Ross Solkin called, "*the biggest welfare check in the U.S. history.*" This bailout of billionaire bankers caused an immediate public outcry to the surprise of Paulson. In congressional hearings Paulson response was, "*it could have been worse.*" As the economic collapse quickly spread to Europe so did the rage against bankers with police fighting pitch battles with demonstrators in London and other cities. Protests in Greece initially began with farmers then quickly spread to civil service workers and students. From the very start European governments stumbled in response as a number of banks began to collapse and European leaders couldn't come up with a plan.

And the only thing that unified the European powers was anger at the United States. When the G7 finance ministers met President Bush at the White House in October 2008 he acknowledged that the United States board the chief responsibility for causing the crisis and promised that the US would change its ways to help clean up the mess. And though an agreement was made at this meeting endorsed by all of the members for Europe the worst was yet to come.

It started in Iceland who in the boom years how to private eyes it's banks and the new owners embarked on a binge of questionable financial practices, with many Icelanders believing that they had created a world beating new banking model. The global financial collapse proved them wrong. In the years leading up to the crash Icelandic banks opened offices in London and launched major ad campaigns deposit their money in high interest Icelandic accounts. In October 2008 almost all of the major Icelandic banks quickly collapse and had to be taken over by the government. The Prime Minister's went on national television to announce that the country was facing bankruptcy and ruin.

The U.K. Government immediately demanded that the Icelandic government guarantee British deposits in Icelandic bank accounts. Already facing bankruptcy Iceland refused. U.K.'s Prime Minister Gordon Brown was furious and froze the assets of Icelandic companies in British banks placing Iceland and Landsbanki on proscribed terrorist organizations. Icelanders couldn't believe it as they were on the same list with North Korea, Syria and the Taliban. As one person pointed out that this was bullying because would have never done that to a bigger country. The only good thing was that this ended illusion in Iceland that it could be a banking powerhouse even though it had no historical experience.

The meltdown triggered an epidemic unemployment around the world and the most astonishing collapse was in China. The inter-connectedness of the world's economics became starkly apparent in late 2008 in China when the country lost tens of millions of jobs as there was a wave of bankruptcies of companies, with some workers not being paid for months. By Christmas 2008 more than 15 million Chinese workers had lost their jobs as thousands of factories had closed suddenly with demonstrations bringing out several cities. Millions of angry workers demonstrating in the street is about the worst nightmare of a communist government in China because the legitimacy of the Communist Party in China depends on economic growth. Fearing another tenement square uprisings the communist government quickly suppress these protest. But by the end of 2008 workers around the world join the global protests brought on by the financial meltdown. In Iceland demonstrators pushed for the overthrow of the government. In France a number of buses were kidnapped and held hostage by their employees. The victims of the crisis were fighting back.

Part 3 (which will be chronicled in next weekend's offerings) centers on the newly unemployed fury... while CEOs have to do making a little less salaries, soup kitchens and tent cities grow across the country. Those who least can afford it paid the price for the Meltdown.
