

One Year Into the Meltdown

The More Things Change, the More They Stay the Same

By Robert Weissman

One year ago, Lehman Brothers declared bankruptcy, bringing to a head the growing chaos on Wall Street.

In the days and weeks that followed Lehman's Sept. 15, 2008, collapse, credit markets would freeze, the stock market plunged, the government took a controlling interest in AIG, Wachovia and Merrill Lynch merged themselves out of existence, the Congress approved a plan to spend \$700 billion to bail out Wall Street, the Federal Reserve innovated an array of programs involving trillions of dollars worth of support for Wall Street and the credit markets, and the national economy — and much of the global economy — declined precipitously.

As the crisis unfolded, it quickly became commonplace to suggest that nothing would ever be the same, on Wall Street or in the national economy. The Wall Street goliaths had been humbled — and many had gone out of business, via merger or bankruptcy. Deregulation went out of style and even former Federal Reserve Chair Alan Greenspan indicated that the conceptual underpinnings of his deregulatory approach had proven flawed.

One year later, it is clear that the conventional wisdom emerging as the crisis developed was wrong.

Some things have changed dramatically — notably in the real economy — but Wall Street's political power remains intact. No new rules are in place to prevent a recurrence of the crisis. Major questions remain about whether any such rules commensurate with the scale of the crisis — with the important exception of a new consumer financial protection agency — will be seriously considered.

The financial crisis has had a devastating impact on regular people — and the situation continues to worsen, even as the economy enters what may be a potential recovery.

Overall economic growth fell by more than 5% (on an annual basis) in the fourth quarter of 2008 and by more than 6% in the first quarter of 2009.

Thanks to this economic crash, the official unemployment rate is racing to 10%, with many believing it will persist at or near double digits through the end of 2010. The actual

unemployment rate — taking into account underemployment and discouraged workers — has topped an astounding 16%. A staggering one in six workers is out of work or underemployed.

The poverty rate has worsened dramatically, just based on the available data for 2008 alone. The official poverty rate in 2008 was 13.2%, up from 12.5% in 2007. There were 39.8 million people in poverty in 2008, 2.5 million people more than the previous year. The 2008 poverty rate — and things have surely gotten worse — was the highest since 1997.

The mortgage crisis continues to worsen. More than 1.5 million foreclosures were filed through the first seven months of this year. By mid-2009, roughly a third of outstanding mortgage borrowers were underwater — meaning they owed more than the value of their home — and the number is growing. Mortgage modifications — almost none of which touch principal — do not come close to keeping pace. Goldman Sachs projects there will be 13 million foreclosures between the end of 2008 and 2014.

The causes of the financial crash continue unabated and in some cases have worsened.

Out-of-control compensation packages, linked to short-term profit performance, drove top Wall Street and big bank executives and traders to take reckless risks. For them, it was a game of heads we win, tails you lose: If their firms registered short-term profits, they received outrageous bonus packages; if there was a longer-term fallout, that would hurt shareholders, but they would have already pocketed their bonuses. Wall Street bonuses are already on track to match or exceed the glutinous pace of 2007.

Banks and other financial institutions deemed “too big to fail” engaged in wild speculation, secure in the knowledge that they would ultimately be backstopped by federal support. These behemoths helped generate the crisis as well by leveraging their political power to peel back the regulatory restraints on Wall Street. Now, thanks to a series of shotgun mergers, the banks are bigger than ever, and there is a greater combination of commercial banking and investment bank operations in single corporate entities.

The proliferation of exotic financial instruments led to massive leveraging and complicated interconnections among top firms that no one could track. The unraveling of these ties led to the downfall of AIG, among other things. While financial derivatives are justified as helping economic players hedge against risk, it turns out they are primarily speculative tools used overwhelmingly by a small number of players. This concentration of massive speculative betting continues, with five banks owning more than four-fifths of the notional value of all outstanding derivatives in the United States. The notional value of these banks’ derivatives exceeded \$190 trillion in the first quarter of 2009.

Wall Street’s go-go years earlier this decade were fueled by a housing bubble and deceptive lending practices. Consumer rip-offs continue apace — and appear to be central to the banks’

business model. Overdraft fees alone will bring in more than \$38 billion in revenue to the banks in 2009.

Meanwhile, the public is paying massively for rescuing Wall Street from itself. The Special Inspector General set up to oversee the bailout estimates that government agencies, including the Federal Reserve, will ultimately put out more than \$23 trillion in various programs and supports related to the financial crisis. This total is almost three times what was spent on World War II, in adjusted dollars.

Most of these trillions will return to the Federal Reserve or the Treasury, but that hardly mitigates the scale of the public investment and risk committed to save Wall Street. And the Treasury Department is certain to lose tens of billions — quite likely hundreds of billions — in the deal.

The deregulation that led to the financial crisis, the bank-friendly immediate response to the crisis and the failure to impose meaningful restraints on Wall Street after the crisis can all be traced to Wall Street's political power. Wall Street spent more than \$5 billion on federal campaign contributions and lobbying from 1998 to 2008, and its fervent spending continues. The financial sector has spent more than \$200 million on lobbying in 2009 alone.

In spring of this year, the banks defeated a proposal, which had been expected to pass, to authorize "cramdowns" of mortgages in bankruptcy. This modest measure would have permitted bankruptcy judges to adjust mortgage principal in bankruptcy, to help people stay in their homes. It would have had relatively limited application and likely would have helped the banks, which are hurt by foreclosures in an environment where they cannot sell houses from which they have evicted borrowers. But cramdown violates the banks' ideological commitment to preventing adjustments of principal. They mobilized to defeat it, leading a frustrated Senate Majority Whip Richard Durbin to say the banks "own the place" — meaning the Congress.

And now, the Financial Services Roundtable has openly announced its intention to "kill" the most important reform measures urged by the Obama administration: creation of a consumer financial protection agency.

Perhaps one of the most telling statistics is the number of stand-alone pieces of financial reform legislation passed, one year after the collapse of Lehman Brothers: zero.

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Multinational Monitor (www.multinationalmonitor.org) and contributing writer to The Progressive Populist since 1998, on Sept. 8 was named president of Public Citizen (www.citizen.org), a national, non-profit consumer advocacy organization founded in 1971 to represent consumer interests in Congress, the executive branch and the courts. He takes over from Joan Claybrook, who served as president for 27 years and will remain on the group's board.

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