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## Volcker Fails to Sell a Bank Strategy

By [LOUIS UCHITELLE](#)

Listen to a top economist in the Obama administration describe [Paul A. Volcker](#), the former [Federal Reserve](#) chairman who endorsed Mr. Obama early in his election campaign and who stood by his side during the [financial crisis](#).

“The guy’s a giant, he’s a genius, he is a great human being,” said [Austan D. Goolsbee](#), counselor to Mr. Obama since their Chicago days. “Whenever he has advice, the administration is very interested.”

Well, not lately. The aging Mr. Volcker (he is 82) has some advice, deeply felt. He has been offering it in speeches and Congressional testimony, and repeating it to those around the president, most of them young enough to be his children.

He wants the nation’s banks to be prohibited from owning and trading risky securities, the very practice that got the biggest ones into deep trouble in 2008. And the administration is saying no, it will not separate commercial banking from investment operations.

“I am not pounding the desk all the time, but I am making my point,” Mr. Volcker said in one of his infrequent on-the-record interviews. “I have talked to some senators who asked me to talk to them, and if people want to talk to me, I talk to them. But I am not going around knocking on doors.”

Still, he does head the president’s Economic Recovery Advisory Board, which makes him the administration’s most prominent outside economic adviser. As Fed chairman from 1979 to 1987, he helped the country weather more than one crisis. And in the campaign last year, he appeared occasionally with Mr. Obama, including a town hall meeting in Florida last fall. His towering presence (he is 6-foot-8) offered reassurance that the candidate’s economic policies, in the midst of a crisis, were trustworthy.

More subtly, Mr. Obama has in Mr. Volcker an adviser perceived as standing apart from Wall Street, and critical of its ways, some administration officials say, while [Timothy F. Geithner](#), the [Treasury](#) secretary, and [Lawrence H. Summers](#), chief of the National Economic Council, are seen, rightly or wrongly, as more sympathetic to the concerns of investment bankers.

For all these reasons, Mr. Volcker's approach to [financial regulation](#) cannot be just brushed off — and Mr. Goolsbee, speaking for the administration, is careful not to do so. “We have discussed these issues with Paul Volcker extensively,” he said.

Mr. Volcker's proposal would roll back the nation's commercial banks to an earlier era, when they were restricted to commercial banking and prohibited from engaging in risky Wall Street activities.

The Obama team, in contrast, would let the giants survive, but would regulate them extensively, so they could not get themselves and the nation into trouble again. While the administration's proposal languishes, giants like [Goldman Sachs](#) have re-engaged in old trading practices, once again earning big profits and planning big bonuses.

Mr. Volcker argues that regulation by itself will not work. Sooner or later, the giants, in pursuit of profits, will get into trouble. The administration should accept this and shield commercial banking from Wall Street's wild ways.

“The banks are there to serve the public,” Mr. Volcker said, “and that is what they should concentrate on. These other activities create conflicts of interest. They create risks, and if you try to control the risks with supervision, that just creates friction and difficulties” and ultimately fails.

The only viable solution, in the Volcker view, is to break up the giants. [JPMorgan Chase](#) would have to give up the trading operations acquired from [Bear Stearns](#). [Bank of America](#) and [Merrill Lynch](#) would go back to being separate companies. Goldman Sachs could no longer be a bank holding company. It's a tall order, and to achieve it Congress would have to enact a modern-day version of the 1933 [Glass-Steagall Act](#), which mandated separation.

Glass-Steagall was watered down over the years and finally revoked in 1999. In the Volcker resurrection, commercial banks would take deposits, manage the nation's payments system, make standard loans and even trade securities for their customers — just not for themselves. The government, in return, would rescue banks that fail.

On the other side of the wall, investment houses would be free to buy and sell securities for their own accounts, borrowing to leverage these trades and thus multiplying the profits, and the risks.

Being separated from banks, the investment houses would no longer have access to federally insured deposits to finance this trading. If one failed, the government would supervise an orderly liquidation. None would be too big to fail — a designation that could arise for a handful of institutions under the administration's proposal.

“People say I'm old-fashioned and banks can no longer be separated from nonbank activity,” Mr. Volcker said, acknowledging criticism that he is nostalgic for an earlier era. “That argument,” he added ruefully, “brought us to where we are today.”

He may not be alone in his proposal, but he is nearly so. Most economists and policy makers argue that a global economy requires that America have big financial institutions to compete against others in Europe and Asia. An administration spokesman says the Obama proposal for reform would result in financial institutions that could fail without damaging the system.

Still, a handful side with Mr. Volcker, among them [Joseph E. Stiglitz](#), a Nobel laureate in economics at Columbia and a former official in the Clinton administration. “We would have a cleaner, safer banking system,” Mr. Stiglitz said, adding that while he endorses Mr. Volcker's proposal, the former Fed chairman is nevertheless embarked on a quixotic journey.

[Alan Greenspan](#), the only other former Fed chairman still living, favored the repeal of Glass-Steagall a decade ago and, unlike Mr. Volcker, would not bring it back now. He declined to be interviewed for this article, but in response to e-mailed questions he cited two recent public statements in which he suggested that the nation's largest financial institutions become smaller, so that [none would be too big to fail](#), requiring a federal rescue.

Taking issue implicitly with the Volcker proposal to split commercial and investment banking, [he has said](#): “No

form of economic organization can fully contain bouts of destructive speculative euphoria.”

For his part, Mr. Volcker is careful to explain that he supports 80 percent of the administration's detailed plan for financial regulation, including much higher capital requirements and “guidelines” on pay. Wall Street compensation, he said in a recent television interview, “has gotten grotesquely large.”

Before the credit crisis, the big institutions earned most of their profits from proprietary trading, and those profits led to giant bonuses. Mr. Volcker argues that splitting commercial and investment banking would put a damper on both pay and risky trading practices.

His disagreement with the Obama people on whether to restore some version of Glass-Steagall appears to have contributed to published reports that his influence in the administration is fading and that he is rarely if ever in the small Washington office assigned to him.

He operates from his own offices in New York, communicating with administration officials and other members of the advisory board mainly by telephone. (He does not use e-mail, although his support staff does.) He travels infrequently to Washington, he says, and when he does, the visits are too short to bother with the office. The advisory board has been asked to study, amid other issues, the tax law on corporate profits earned overseas, hardly a headline concern.

So Mr. Volcker scoffs at the reports that he is losing clout. “I did not have influence to start with,” he said.

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