Wall Street:
Still Out of Control

A Presentation by Robert Weissman

To Public Citizen Members

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Outline

I. Causes of the Crisis

II. The Current State of Affairs

III. What Can Be Done

I. Causes

Context: The financial crash was the culmination of unhealthy economic trends

- Housing bubble
- Rising inequality
- Too big, out-of-control financial sector

Deregulation --> Financial Recklessness

1. Repeal of Glass-Steagall
2. Deregulation of financial derivatives
3. Decline of antitrust enforcement
4. Repeal of the “net capital rule”
5. No enforcement of predatory lending rules

Repeal of Glass-Steagall

- Depression-era law that mandated separation of commercial banking and investment banking
- Eroded starting in 1970s, repealed in 1999
- Key players: Citigroup and its executives
- Result: Commercial banks took more risks, investment banks borrowed more to take bigger risks

Corporate Civil Disobedience: Citi and Travelers Merge Despite Prohibition

Photograph courtesy of National Archives and Record Administration, 306-PS-68-1130

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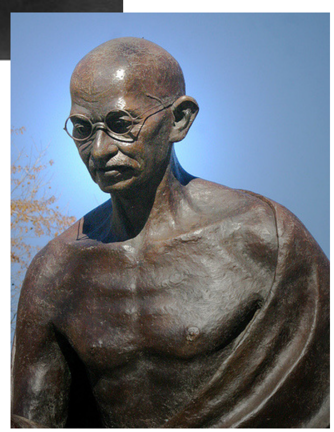


citibank

citi Citi never sleeps

Robert Rubin, formerly of Goldman, later of Citigroup, on “financial modernization” -- while still at Treasury

Deregulation of Financial Derivatives - I

- Derivatives are not new, but exotic financial instruments started proliferating in the 1990s
- Commodity Futures Trading Commission under Clinton took modest steps to regulate; Rubin-Summers-Greenspan blocked effort
- Sen. Phil Gramm has law passed in 2000 that prohibits regulation of financial derivatives

Sen. Phil Gramm - now with UBS

Deregulation of Financial Derivatives - II

- Explosion of financial derivatives follows
- The result is much bigger risks and entanglement of institutions
- Regulatory vacuum means, for e.g., that AIG did not set aside appropriate capital in case it had to pay out on derivative trades
- Many serve no social purpose whatsoever

That Didn’t Work So Well

Decline of Antitrust

- Reagan = End of robust antitrust enforcement
- In the United States, about 11,500 bank mergers took place from 1980 through 2005, an average of about 440 mergers per year.
- Larger banks: lower capital ratios (more risk), more investments in derivatives, less responsive to local needs
- “Too big to fail” institutions feel free to take excessive risks; unfair advantage because able to access cash more cheaply

Repeal of “Net Capital Rule”

- Securities and Exchange Commission had established leverage ratios for investment banks -- 12:1
- Repealed in 2004, at urging of Hank Paulson of Goldman Sachs and other big investment banks
- Result: Much higher leverage -- use of borrowed money -- by investment banks

Formerly of Goldman,
subsequently Treasury Secretary,
Henry Paulson

No Predatory Lending Enforcement

- Consumer groups beg for regulation and enforcement in 2000-2001, and earlier
- 2003-2007: 3 enforcement actions by Federal Reserve
- Preemption of state efforts

$5 Billion

… $5 billion is the amount the financial services industry spent on lobbying and campaign contributions from 1998 – 2008.

II. The Current State of Affairs

Since the Crash, the Industry Has Not Changed (or has gotten worse)

Kate Thomas/SEIU

Financial sector is now much more concentrated

- JP Morgan Chase gobbles Bear Stearns; Wells Fargo takes over Wachovia, Bank of America buys Merrill Lynch
- JP Morgan Chase, Bank of America, Wells Fargo
  - share of mortgages: 25.9% in 2007, 41.8 in 2009
  - share of deposits: 21% in 2007, 33.9% in 2009
- Big banks pay <u>much</u> less to access capital -- because markets view them as too big to fail

Consumer Ripoffs Continue Unabated

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

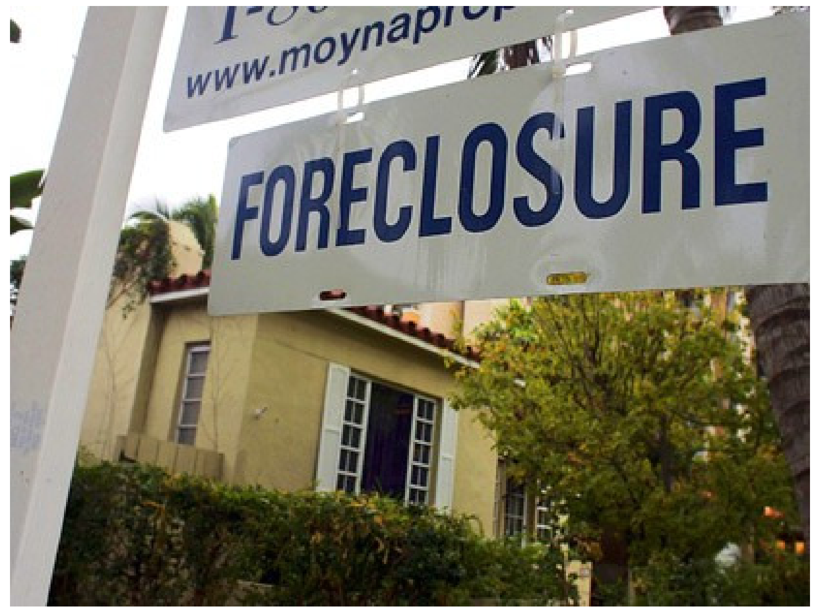
Bonus Compensation is Again Out of Control

- Tally expected of $150 billion for Wall Street compensation
- Modest changes, but this continues to reward short-term risk taking
- Siphoning out taxpayer money

Mike Licht, CC2.0,
http://www.flickr.com/photos/notionscapital

Meanwhile, Foreclosure Crisis Unabated

- 31,000 permanent modifications through November 2009
- Goldman Sachs predicts 13 million foreclosures through 2013
- Ongoing refusal to adjust principal



Politics as Usual

- Washington quakes in Fall 2008
- But Wall Street soon resumes its usual role
  - 940 former federal employees as federal lobbyists in 2009
  - $85 million in campaign contributions
  - Strategy: frame what is acceptable, then chip away
- Regulatory reforms are, by and large, very disappointing

III. What Can Be Done

6 Reforms That Can Work - I

1. **Consumer Financial Protection Agency**
   - Passed House, under threat in Senate
   - Power to issue rules to protect consumers, inspect institutions
2. **Break Up the Banks/**
   Reimpose Glass-Steagall
   - Method: Order to divest assets in excess of a certain size
   - House bill does NOT do this or anything close
   - Populist appeal
   - Sens. Cantwell and McCain propose new G-S

6 Reforms That Can Work - II

3. Control Derivatives

- House version very disappointing
- Ideal: socially useless instruments prohibited
- Minimum: Everything must be traded on open exchange, like stocks

4. Speculation Tax

- Small tax on financial transactions - like sales tax
- Can raise $150 billion/year
- Bills by Rep. DeFazio and Sen. Harkin
- Interest growing

6 Reforms That Can Work - III

5. Windfall Bonus Tax

- Huge bonuses being paid only because of government intervention
- UK has adopted
- Rep. Kucinich bill, momentum

6. Ensure global trade rules do not preclude national regulation

4 Things You Can Do

1. Sign our Petition to Sen. Dodd on the Consumer Financial Protection Agency

   www.Citizen.org/doddpetition

2. Get ready for next week's initiative on the windfall bonus tax
3. Ask 10 friends to sign these petitions
4. Let us know that you would like to be a grassroots leader for financial reform
   – Contact: action@citizen.org