US workers paying the price for Wall Street's debacle

Barry Grey 16 May 2008

The Federal Reserve Board, with the full backing of the Bush administration, Congress and both political parties, has carried out a massive and unprecedented intervention to avert an imminent collapse of the US banking system and bolster the major Wall Street finance houses

The Fed's decision in March to underwrite with \$29 billion of its own funds the takeover of investment bank Bear Stearns by JPMorgan Chase, in order to prevent the collapse of Bear Stearns, and its even more extraordinary move to allow major investment banks to avoid a similar fate by borrowing directly from its coffers, was a signal that the US government would marshal whatever resources were necessary to rescue the banking system from the consequences of the speculative binge that had generated billions in salaries and bonuses for the Wall Street elite.

While the government bailout, ultimately to be financed from public funds, has seemingly averted an immediate banking collapse, it has done nothing to address the underlying crisis. Rather, the Fed and the US corporate-financial establishment hope that it has created the conditions for a more orderly "deleveraging" of the financial system, i.e., a liquidation of trillions in vastly inflated and unmarketable assets, in which the social and economic pain is borne overwhelmingly by working class and middle class families.

The Fed's actions have restored a measure of confidence to the financial markets, reflected in a stock market rally that has driven the Dow Jones Industrial Average back toward the 13,000 level. At the same time, the Fed and most financial analysts are acknowledging that the US housing collapse and credit crunch have precipitated an economic slowdown that will likely be protracted.

Addressing a conference of the Federal Reserve Bank of Atlanta on Tuesday, Federal Reserve Board Chairman Ben Bernanke said that financial markets were improving but "remain far from normal." He said the decision in March to allow investment firms to obtain emergency loans from the Fed "seems to have bolstered confidence."

But, he cautioned, the crisis would not be resolved quickly. "Ultimately," he said, "market participants themselves must address the fundamental sources of financial strains through deleveraging, raising new capital and improving risk management, and this process is likely to take some time."

Whatever the technical indices of the slump—not a few experts have taken to denying that the US is in a recession or heading for one—ordinary working people in the United States are suffering a major cut in their living standards. Job losses are mounting, wages are declining, work hours are being reduced and prices for essentials such as food and gasoline are soaring.

In a word, the underlying historical and economic processes that

produced the crisis on Wall Street are making the vast majority of Americans poorer. And we are only at the beginning of this process.

The impact of the economic crisis on the general population was reflected in a *Washington Post*-ABC News poll released Tuesday, which reported that 68 percent of people surveyed said they were concerned about their ability to maintain their standard of living. The biggest factor cited by respondents was the sharp rise in consumer prices.

A separate poll released by ABC showed economic anxiety to be at its highest point on record since 1981.

In the *Post*-ABC poll, the nearly 70 percent who said they were worried about maintaining their lifestyles represented a 17 percent jump since December of last year. The growing anxiety reported by respondents cut across party and income lines, "spreading rapidly among Republicans, people from rural areas and those from middle-and upper-income households," according to the *Post*.

The newspaper said that nearly six in ten people from households with an annual income of \$100,000 or higher said they were worried, up from a third in December. Of those who identified themselves as Republicans, 56 percent expressed concern, up from 32 percent.

Twenty percent cited higher gasoline prices as the single most important economic issue, and about a third pointed more generally to rising prices as the primary cause of their apprehension. Two-thirds called rising gasoline prices a financial hardship, including a third who said higher fuel prices were a severe burden.

There is, of course, a very real basis for these concerns. Just on the question of gasoline, the Energy Department reported that the average cost of gas rose 11 cents in the past week alone, and has gone up 33 cents over the past month on its way to over \$4 a gallon.

According to a report issued Wednesday by the Labor Department, food prices shot up 5.1 percent in April over a year earlier, and 0.9 percent from the previous month. Both of these gains are the biggest since 1990. The spike in food prices was propelled by increases in the price of bread, fruit, coffee and other consumer staples.

Health care costs have risen 4.3 percent in the past 12 months.

Prices for imported goods—a direct reflection of the precipitous decline of the US dollar—rose 1.8 percent in April from March. They have soared 15.4 percent from last year, the biggest year-to-year increase since such records began to be kept in 1982.

Meanwhile, real weekly wages have fallen compared to a year earlier in every month since October.

A major component of the "deleveraging" process is an assault on jobs by means of downsizing, restructuring and corporate bankruptcies. The last three months have seen, according to the Labor Department, a net loss of 180,000 jobs in the US. Aside from

construction and manufacturing, where job cuts continue to escalate, the financial sector is bearing the brunt of the job-cutting.

It is estimated that so far this year 50,000 financial jobs have been slashed. More than 23,000 financial-related US job cuts were announced in April, according to the outplacement firm Challenger, Gray & Christmas. That increased the total to 49,825 in the first four months of this year—nearly as many job cuts as were announced in all of 2007.

This, however, is only the first stage of what promises to be a far larger job-slashing process. Last week, the Swiss bank UBS announced it will lay off 5,500 employees in the US and Britain. Lehman Brothers is expected to announce that it is eliminating 5 percent of its employees, or about 1,425 positions, on top of a previously announced 5 percent cutback in its work force.

By the end of June, Morgan Stanley plans 1,500 more job cuts. This puts total layoffs at Morgan Stanley at about 4,500, or 10 percent.

Citigroup on May 9 announced a plan to shed up to \$500 billion of assets and slash some \$15 billion off its cost base. The bank did not say how many jobs would be eliminated, but the figure will likely be in the tens of thousands. The bank has already announced 13,000 job cuts.

The crushing impact of job losses and price rises continues to undermine retail sales. The Commerce Department reported Tuesday that retail sales fell another 0.2 percent in April from the previous month. This smaller-than-expected drop obscures the dramatic slump in consumer spending in key manufacturing sectors. Auto sales fell 2.8 percent in April, after a 0.5 percent drop in March.

The Federal Reserve issued a report on US manufacturing Thursday which showed that the slump in that critical sector is deepening. Industrial production declined 0.7 percent in April, more than twice the drop forecast by economists.

The financial crisis is taking a growing toll in the form of corporate bankruptcies. Corporate bankruptcy filings rose in the US last month more than 50 percent over the previous year's figure.

In the financial sector itself, losses from failed mortgage-related assets and bad debts continue to mount, reflecting the underlying insolvency of major sections of the financial system. Last week, American International Group, the world's largest insurance firm, announced a record \$7.8 billion loss in the first quarter of 2008. This brought the company's loss to \$13.1 billion over the past two quarters. AIG has written down \$20 billion in credit derivative contracts since December.

The deepening financial crisis of Fannie Mae and Freddie Mac, the two major mortgage companies that are sponsored by the US government, is indicative of the way in which the crisis on Wall Street is being offloaded onto the government. Freddie Mac on Wednesday reported a loss of \$151 million in the first quarter of 2008. The market responded to this lower-than-expected loss by driving the company's stock up by 9 percent.

However, the reported figure was achieved by means of accounting gimmicks that concealed an actual loss of \$2 billion. The previous week, Fannie Mae reported a first quarter loss of \$2.2 billion. Its stock also shot up.

The two companies suffered more than \$9 billion in mortgagerelated losses last year, and are sitting on as much as \$19 billion in additional losses that they have not yet fully acknowledged, analysts say. Their combined cushion of \$83 billion underpins a colossal \$5 trillion in debt and financial commitments—a level of leverage that is unsustainable. But in the aftermath of the bursting of the housing bubble, the government has allowed them to expand their loans while lowering their capital cushions. This is because the two government-backed firms are essentially taking over the mortgage financing business that has been dumped by the banks and investment firms.

As the *New York Time* reported last week, "As Wall Street all but abandons the mortgage business, Fannie Mae and Freddie Mac now overwhelmingly dominate it, handling more than 80 percent of all mortgages bought by investors in the first quarter of this year. That is more than double their market share in 2006."

In a separate article on Thursday, the *Times* explained the reason for the stock market's enthusiasm for the shares of the two companies. "Both these companies are clearly going to be insolvent by the end of the year, but everyone knows that Congress will do anything to keep them afloat, because if Fannie and Freddie go under, the entire global financial system will melt down,' said Christopher Whalen, a founder of Institutional Risk Analytics, an independent research firm. 'These companies' earnings don't matter. Their accounting hardly matters. People buy the stock because they believe the federal government will bail them both out if things get really bad."

No such bailout is in the works for the millions of families that are losing their homes as a result of the mortgage crisis.

Foreclosure filings surged 65 percent in April from April 2007, according to a report issued Wednesday by RealtyTrac. One in every 519 households received a foreclosure filing—the highest such figure since the real estate tracking company began issuing foreclosure reports in January 2005. Nationally, 243,353 homes were facing foreclosure last month. That amounts to 2 percent of all homes.

Foreclosure filings rose in all but eight states. The hardest hit states included Arizona, California, Florida and Nevada. Analysts expect the foreclosure rate to continue to rise, spiking in the third and fourth quarters of this year.



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