Record corporate bailout reveals the bankruptcy of American capitalism

Barry Grey
10 September 2008

The US government takeover of the mortgage finance giants Fannie Mae and Freddie Mac has dealt a shattering blow to the ideology of market capitalism, which has been used for decades to justify a relentless assault on the working class and a vast transfer of wealth to the American ruling elite.

The endless invocations of the virtues of private enterprise, individual entrepreneurship and self-reliance, used to demonize socialism and defend a system that exploits the vast majority for the benefit of a financial elite, have been exposed as frauds. When it comes to big capital, losses are socialized. Only profits remain private.

The same forces who year after year have inveighed against “big government” in order to justify the removal of all legal impediments to the accumulation of corporate profits and private fortunes, and carry out the destruction of social safeguards for the working class, have engineered a massive expansion of government power to safeguard the interests of the financial elite.

The bailout has as well exposed the real relations of political power and influence behind the façade of American democracy. The largest government bailout of private companies in world history—whose ultimate cost to taxpayers is likely to reach hundreds of billions—was sanctioned in advance by the Democratic Congress and given instant approval by the leadership of both parties and both of their presidential candidates.

There have been no investigations into the greatest financial scandal in world history. Neither party has any interest in bringing to light the swindling and skullduggery of the Wall Street moguls, because they are both bound hand and foot to those responsible for the financial debacle.

What has been revealed is the existence in the United States, behind the increasingly tattered veneer of democratic institutions, of a plutocracy—the political rule of the rich. When it comes to the basic interests of the financial aristocracy, both parties and all of the official institutions of society snap to attention and do the bidding of their Wall Street masters.

The bailout of the two mortgage giants—which account for 80 percent of new home mortgages in the US—is a demonstration of the historic failure of American capitalism and the profit system on a global scale. It was precipitated by the deepest economic crisis since the Depression of the 1930s, whose epicenter is the United States. The Bush administration moved to take over Fannie Mae and Freddie Mac under conditions of a rapid erosion of international confidence in the solvency of not only these two companies, but of the United States government itself.

Over the past several months, global investors, including central banks and government investment funds, primarily in Asia and Russia, have been dumping their vast holdings in mortgage-backed securities issued by the US government-sponsored firms. Fannie Mae and Freddie Mac have a combined liability of $5.3 trillion in mortgage-backed securities which they own or guarantee. The run on their assets has not only intensified the crisis of the two companies, which are massively leveraged and have suffered billions of dollars in losses as a result of the collapse of the US housing market, it has thrown into question the status of all US government debt, including US Treasury bonds.

The US, by far the world’s largest debtor nation, with a current account deficit of nearly $800 billion, is sustained by the inflow of hundreds of billions of dollars from abroad. It currently imports $1 trillion in foreign capital every year, or over $4 billion every working day.

But the assumption by the US government of the debts of the two mortgage companies, while averting an immediate financial meltdown, only compounds the crisis of American capitalism. As Martin Wolf, the financial correspondent of the *Financial Times* wrote on Tuesday, “As a result, US housing finance has been brought under direct government control and, in the process, the gross liabilities of the US government, properly measured, have increased by $5,400 billion, a sum equal to the entire publicly held debt and 40 percent of gross domestic product.”

At a stroke, US sovereign debt has doubled and is now roughly equal to America’s gross domestic product. On July 14, one day after US Treasury Secretary Henry Paulson called for legislation to give him unilateral and unlimited powers to use public funds to rescue Fannie Mae and Freddie Mac, the *Wall Street Journal* editorialized on the implications of a government bailout of the two companies. It wrote: “But with financial woes mounting, some investors are betting they may profit from weighing the unthinkable question: Could the US government default?”

This immense increase in US government indebtedness can only further undermine international confidence in the credit-worthiness of US Treasury bonds, resulting in a further decline in the dollar and a sharp increase in the interest paid by the US to borrow from its international creditors.

The claims made by the Bush administration, echoed by the US media, that the bailout of the two mortgage finance companies will consume at most $200 billion in public funds—itself a massive amount that eclipses previous corporate bailouts, including the $160 billion bailout of the savings and loans industry less than two decades ago—are not credible. An indication of the sums envisioned by US policy makers is the fact that the legislation passed last July giving Paulson the power to bail out Fannie Mae and Freddie Mac raised the

US debt limit by $800 billion, increasing the cushion between the debt limit and current government indebtedness to $1.1 trillion.

Some sense of the social priorities of the US ruling elite and its two parties can be gleaned from a comparison between the sums being extended to bail out just these two companies and those allocated by the federal government in 2008 for education ($67.5 billion), unemployment benefits ($37.3 billion), highways and mass transit ($53.1 billion) and housing ($7.4 billion).

Moreover, the bailout of Fannie Mae and Freddie Mac is only the prelude to a far broader use of public funds to bolster the balance sheets of major corporations. Democratic presidential candidate Barack Obama and his Republican opponent John McCain are both supporting a $50 billion bailout of the US auto companies, which will inevitably entail further cuts in jobs and wages. And the plunge of the Wall Street investment bank Lehman Brothers toward bankruptcy—the firm's stock fell by 45 percent on Tuesday—poses another rescue operation similar to the $29 billion bailout of Bear Stearns last March.

It is already being widely broached that the government establish a permanent mechanism for using taxpayer funds to buy billions of dollars in failing assets from major banks and financial companies. The *Wall Street Journal* wrote on Tuesday, "Creating a government-backed entity to buy up these assets could jump-start the market for home loans and relieve banks and other financial institutions, which are taking big hits to their balance sheets as they fall in value."

The *Financial Times* sounded the same theme, declaring, "The US government might end up having to support the recapitalization of a much wider range of financial institutions in order to curb the credit crunch."

These statements give the lie to the attempt to portray Fannie Mae and Freddie Mac as aberrations, which in their reckless speculation and pursuit of super profits departed from the norm. On the contrary, they typify the financial parasitism and outright criminality that have become pervasive characteristics of the workings of American capitalism and the social physiognomy of the US corporate elite.

The operations of the two government-sponsored firms are entirely in line with the unbridled speculation, based on an immense expansion of debt, that has become the hallmark of American capitalism. Their role in the housing and credit boom that has now come crashing down was of a piece with the creation of the vast edifice of paper values, engineered through the so-called "securitization" of debt, which sustained the super profits and immense salaries raked in by Wall Street.

In the wake of the bailout, press reports have noted the bloated salaries of the companies' CEOs. Before they were sacked as part of the government takeover, Fannie Mae CEO Daniel Mudd and Freddie Mac chief Richard Syron took in between them $29.5 million over the several years they headed their respective corporations. And they stand to receive another $29 million as part of their exit packages.

But these sums are by no means exceptional. The *Financial Times* reported last week that compensation for major executives of the seven biggest US banks totaled $95 billion between 2005 and 2007.

The collapse of Fannie Mae and Freddie Mac is a paradigm of the US economy as a whole. Over the past three decades, the decay of American capitalism has taken the form of a vast growth of financial parasitism. At its heart, this involves the separation of wealth creation from the creation of real value in the production process. The American ruling elite has largely dismantled the productive base of the US economy, ruthlessly downsizing manufacturing at the cost of millions of jobs and the destruction of working class living standards, in order to reap higher profits from increasingly reckless forms of financial speculation.

The indices of the growth of financial speculation in the US economy are staggering: In 1982, the profits of US financial companies accounted for 5 percent of total after-tax corporate profits. In 2007, they made up 41 percent of corporate profits.

This process has generated ever greater levels of social inequality, the most telling symptom of the degenerate state of the US profit system. A report by the Congressional Research Service, updated July 31, provides a measure of the ever growing chasm between the ruling elite and the broad mass of the American people. It states that the share of national income accounted for by the top 1 percent of earners (as reported on tax returns) reached 21.8 percent in 2005—a level not seen since 1928. The report further noted that in 2006, corporate profits totaled 12.4 percent of national income, a level not reached in 50 years.

The cost of the ever-expanding bailout of American big business will be borne squarely by the working class. Even in the midst of growing unemployment and poverty and a flood of home foreclosures, there is much talk in the media about the American people "living beyond their means."

That the next administration, whether headed by McCain or Obama, will sharply intensify the assault on working class living standards was spelled out by the *New York Times*, which editorialized Tuesday: "Senators John McCain and Barack Obama have both voiced support for the bailout, which shows good judgment. But what the next president will need to worry about, and both candidates need to talk about, is the depth of the country's economic problems. It will take discipline and sacrifice to address them."

The only alternative to a rapid lowering of working class living standards and the only rational and progressive solution to the financial crisis is a socialist program of nationalization of the entire financial system under the democratic control of the working people, with provisions to secure the investments of small depositors and share-holders. The wealth and resources of the country must be developed and allocated to meet the social needs of the population, not the money-mad strivings of financial speculators.

This policy can be carried out only through the independent political mobilization of the working class in opposition to the two-party system and the financial aristocracy which it serves. The Socialist Equality Party is dedicated to the building of such a mass socialist movement of the working class.