Obama administration announces plan to expand government bailout of the banks

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US Treasury Secretary Timothy Geithner on Tuesday outlined the Obama administration's plan for an expanded taxpayer bailout of the banks. The plan will not only inject tens of billions of additional dollars into financial firms, but also use Treasury funds and Federal Reserve loans to offload worthless bank assets onto the public by means of a so-called Public-Private Investment Fund.

The third major aspect of the plan announced by Geithner is a vast expansion of a program announced by the Fed last November to provide cheap loans and subsidies to hedge funds, private equity firms and other speculators to encourage them to buy bank securities backed by auto loans, credit card debt, student loans, commercial real estate and small business loans.

The plan, while it does not immediately call for funding beyond the second half of the $700 billion bailout approved by Congress last October, sets the stage for an even more massive transfer of public funds to the banks, potentially reaching trillions of dollars. As Obama did in his press conference Monday night, Geithner broadly hinted that the administration would soon request congressional authorization for billions more to rescue the banks. Senate Banking Committee Chairman Christopher Dodd was brought forward to introduce Geithner so as to provide assurance that the congressional Democratic leadership would support a new bailout bill.

The immense crisis facing the Obama administration, both economic and political, was underscored by the sharply negative response of financial markets to Geithner's announcement. They delivered a hostile verdict, signaling an initial consensus within the financial elite that the plan as outlined did not go far enough in making the American people pay for Wall Street's staggering losses.

Even as Geithner presented his plan, stock prices nosedived and they continued to fall while the treasury secretary testified later in the day before the Senate Finance Committee. When markets closed, the Dow Jones Industrial Average had dropped 382 points, or 4.6 percent, to its lowest close since November. The other major indexes also fell sharply. Bank stocks were particularly hard hit, with the Standard & Poor's financials index falling more than 8 percent. Shares of Bank of America fell 19 percent.

The financial markets' negative response heightens the political dilemma facing the Obama administration. Its entire financial rescue plan, like that of the Bush administration, is geared to protecting the interests of the financial elite and shoring up its ownership and control of the banking system. The plan assiduously avoids imposing any cost to bank shareholders or bondholders in return for government handouts.

It is designed to limit government equity in banks that receive cash injections, requiring the firms to recompense the government in convertible preferred securities rather than common stock. It does not require the banks to increase their lending to other businesses or consumers as a condition for receiving government funds.

At the same time, the Obama administration is well aware that it faces deep-seated and mounting public anger over the bailout of the very bankers and speculators whose pursuit of super-profits and personal enrichment drove their firms into the ground and threw the entire economy into the deepest crisis since the Great Depression, precipitating a recession that has already wiped out 3.6 million jobs and is certain to destroy millions more in the coming months.

Like Obama, Geithner attempted to portray the new financial rescue plan, dubbed the Financial Stability Plan, as a sharp departure from the Troubled Asset Relief Program (TARP) instituted by Bush's treasury secretary, Henry Paulson, claiming it included extensive provisions for transparency and accountability and harsh restrictions on banks that receive additional bailout funds. The supposed limits on executive pay and other requirements on the banks are, in fact, largely ephemeral, designed to assuage public opinion and obscure the reality of a vast new windfall for the financial elite.

The bogus nature of this pretense is underscored by the fact that Geithner, in his former position as president of the Federal Reserve Bank of New York, played a central role alongside Paulson and Federal Reserve Chairman Bernanke in devising the TARP program, which he now admits failed to resolve the financial crisis and merely handed over hundreds of billions to Wall Street without any controls over the banks' use of the taxpayer money.

The *New York Times* on Tuesday reported that Geithner opposed Obama political aides who were pushing for more serious restrictions on executive pay and costs to shareholders in a new bailout plan, out of concern over public anger and worries that the administration might be unable to secure congressional approval when it returns for new legislation to commit more taxpayer funds to rescuing the banks.

As the *Times* acknowledged, "And for all of its boldness, the plan

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largely repeats the Bush administration's approach of deferring to many of the same companies and executives who had peddled risky loans and investments at the heart of the crisis and failed to foresee many of the problems plaguing the markets."

The administration is loath, for political reasons in the face of broad popular opposition to the bailout, to be seen as directly setting vastly inflated prices for the purchase of so-called "toxic" mortgage-backed assets and other virtually worthless debt held by the banks, the key provision in its bailout plan. The public-private partnership announced by Geithner is an attempt to circumvent this problem by using Treasury funds and Fed financing to subsidize and insure private investors, mainly hedge funds and private equity firms, that agree to buy the illiquid assets weighing down the balance sheets of the banks.

Under this scheme, private investors and the banks would nominally set the price for the bad assets, rather than the government. In reality, the government would indirectly insure that the prices fetched by the banks were many multiples of the real market value of the assets by agreeing to cover most of any potential losses incurred by private investors who bought the bank debt.

This would create conditions for a massive profit windfall for both the private purchasers of the bad debt and the banks. The former would stand eventually to cash in on any recovery of the assets' value, while the latter would purge their portfolios of hundreds of billions of bad debt, setting the stage for a sharp rise in the value of their stock.

As Laurence H. Meyer, vice chairman of Macroeconomic Advisers and a former Federal Reserve governor, told the *New York Times*, "There is a great profit opportunity here."

In his announcement of the new bailout plan, however, Geithner was obliged to mask the reality of this scheme to further plunder the public treasury and provided no details as to how the plan would work. On the contrary, he indicated that the actual design of the plan had yet to be determined, saying, "We are exploring a range of different structures for this program…"

This lack of specificity and the absence of a direct and open pledge to offload the banks' losses at public expense fueled skepticism and outright hostility in the financial markets. This was despite Geithner's efforts to signal the markets that the government was prepared to spend unlimited sums to cover the banks' losses.

He declared, "This program will require a substantial and sustained commitment of public resources… We will consult closely with Congress as we move forward, and work together to make sure we have the resources and the authority to make this program work," and added, "this strategy will cost money, involve risk, and take time."

He further reassured Wall Street that nothing would be done to challenge ownership and control over the financial system by private capital, saying, "We believe our policies must be designed to mobilize and leverage private capital, not to supplant or discourage private capital. When government investment is necessary, it should be replaced with private capital as soon as possible.

"We believe that the United States has to send a clear and consistent signal that we will act to prevent the catastrophic failure of financial institutions that would damage the broader economy…"

In a subsequent interview on the CNBC cable television network, he added that the administration was seeking to "preserve the financial system in private hands."

However, this is not sufficient to satisfy the financial aristocracy, whose immense and controlling influence over the state has been revealed time and again since the financial crisis erupted. This tiny but extraordinarily rich and powerful social elite stands as an intractable obstacle to any rational solution to the economic crisis.

The major banks and Wall Street firms have refused to sell the bad mortgage-related debts on their books at anything near their real market value, insisting that investors prepared to speculate in their "toxic assets" pay the absurdly high valuations they have assigned to them. Holding these bad debts erodes their reserve capital and provides them with an excuse to hoard their cash injections from the government rather than increase their lending.

This amounts to a form of blackmail against the state. The banks are withholding capital, exacerbating the credit crisis and the downward spiral in the "real economy," confident that they can eventually force the government to absorb the full cost of their losses. They are thereby exploiting the crisis of their own making to further plunder the social wealth, holding the American people, who bear the full burden of the crisis, at ransom.

This is but the latest stage of a protracted period during which the most powerful sections of the ruling elite have amassed colossal wealth on the basis of the most parasitic forms of financial manipulation, dismantling the industrial infrastructure and impoverishing the working class in the process.

Solving the economic crisis is not a technical, but rather a political and class question. No rational solution can be found outside of a mass revolutionary movement of the working class to break the stranglehold of the financial aristocracy and abolish its wealth and privileges. Only a socialist policy can defend the interests of the working class, the vast majority of the population. This includes the nationalization of the banking system under the democratic control of the working population, so that the social wealth produced by the working class can be developed and utilized for the common good.

The prerequisite for such a struggle is a break with the two parties of big business and the fight for a workers' government.

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