Bernanke's apologia for the Fed

Patrick Martin
25 August 2009

Federal Reserve Board Chairman Ben Bernanke delivered a speech to the annual summer symposium of the world's central bankers, held August 20-21 in Jackson Hole, Wyoming, which combined a review of the past year of unprecedented financial crisis and a prognosis of the near-term prospects for the US and world economy.

It is fair to say that Bernanke was picking his way through a political minefield as he delivered his address: conceding the unprecedented intensity of the financial crisis and (implicitly) the failure of the Fed and other banking authorities to foresee it; defending the Fed's actions from September 2008 through the present in using trillions in public funds to bail out Wall Street; and promising, to the broader public audience, that better times lie ahead, despite the dismal state of the economy for working people.

Bernanke began by noting that he had presided over a similar gathering a year ago, at a time when the financial crisis was thought—at least by the spokesmen for capitalism—to be relatively under control. While there were signs of a slowdown, and some sharp financial shocks, like the forced liquidation of Bear Stearns, when Bernanke and his fellow bankers and regulators met at Jackson Hole in August 2008, "there was little to suggest that market participants saw the financial situation as about to take a sharp turn for the worse."

Instead, contrary to the central bankers' expectations, "In the weeks that followed, several systemically critical financial institutions would either fail or come close to failure, activity in some key financial markets would virtually cease, and the global economy would enter a deep recession."

The bulk of Bernanke's speech was devoted to detailing the measures undertaken by the Fed and other central banks to prop up financial institutions after the failure of Lehman Brothers on September 15, 2008 touched off a crisis of confidence in the global financial system. He made no effort to justify the decision to save the banks, nor was it necessary in a speech to an audience of like-minded administrators of world capitalism.

While moving might and main to save the banks, however, these economic authorities made no similar effort to save the jobs, living standards, social benefits or homes of tens of millions of workers. On the contrary, the destruction of the livelihoods of masses of working people has been a necessary consequence of the policies pursued to save the financial elite. The world working class has paid and will continue to pay for the bailout of the financial aristocracy.

Bernanke hailed the results of the intervention of the central bankers and cited "noteworthy progress." At the same time, he acknowledged that the "economic recovery" would be "gradual," with unemployment remaining at extremely high levels.

There is considerable data demonstrating that this prognosis of gradual recovery is far too rosy. Personal bankruptcy filings and home foreclosures in the US continue to break records month-by-month. US consumer spending is stagnant and consumer sentiment is more pessimistic than at any time since 1946. Household debt stands at 123 percent of income.

According to an account carried by the Associated Press Monday, Wall Street has resumed all the old methods of securitization of debts and mortgages through the creation of ever more complex and unintelligible financial instruments, such as those which triggered the crash of 2008. "In recent months investment banks have been repackaging old mortgage securities and offering to sell them as new products, a plan that's nearly identical to the complicated investment packages at the heart of the market's collapse," the news service reported.

A bourgeois critic of the Fed, economist Nouriel Roubini, warned in a column Monday in the *Financial Times* that there was now “a rising risk of a double-dip W-shaped recession.” He cited the inflationary implications of the massive credit injections by the central banks, combined with the collapse of consumer spending because of rising unemployment.

But there is a more telling case to be made against Bernanke’s posture of cautious optimism. Why should the Federal Reserve Board chief’s predictions in August 2009 be taken any more seriously than his predictions in August 2008?

In his account of the crash of 2008, Bernanke offered no explanation of why the assembled “wise men” of global capitalism were taken unawares. But what was apparently an unfathomable enigma to the central bankers was no surprise to the *World Socialist Web Site*.

Two months before last year’s Jackson Hole meeting, the WSWS commented on the conflicting policies of the Federal Reserve, which was loosening monetary constraints, and the European Central Bank, which was tightening. We wrote: (See “US Fed caught in global turbulence”)

“One of the most significant features of the present situation is how rapidly these processes have taken place. A year ago major reports from global financial bodies such as the World Bank and the IMF pointed to the risks of inflation and the possibility of financial turmoil. But they were still relatively small clouds on the horizon. The situation has now changed dramatically as the world economy faces its most serious crisis in more than three decades.”

In July 2008, after the Treasury bailout of Fannie Mae and Freddie Mac, the two giant lending institutions which backstop the bulk of the US home mortgage market, we wrote that failure of the two firms would have touched off a global crisis: (See “US bailout of mortgage giants: The politics of plutocracy”)

“US and global financial markets would face a meltdown, since thousands of US banks, hedge funds, pension funds and other institutions hold securities guaranteed by the two companies, and central banks, governments and private banks around the world are heavily invested in Fannie Mae and Freddie Mac debt.”

We warned of the implications of the new policy: “The bailout with public funds of Fannie Mae and Freddie Mac will set a precedent for a far broader use of taxpayer money to rescue major financial companies.”

Bernanke is by all accounts an intelligent man and an accomplished bourgeois economist, whose academic specialty was the study of US monetary policy during the Great Depression. Yet for all his research and the vast array of data available to the Federal Reserve Board, he did not foresee the greatest financial collapse since the 1930s. The WSWS, equipped with a Marxist world outlook, did foresee it, and the Socialist Equality Party prepared accordingly, holding its founding congress in August 2008.

Patrick Martin