European Central Bank promises unlimited liquidity

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In yet another concession to international banks and speculators, European Central Bank President Jean-Claude Trichet announced Thursday that the ECB would continue its policy of making unlimited liquidity available to the banks well into next year.

At the ECB's regular monthly press conference in Frankfurt, Trichet announced that the bank would continue to pump huge sums into the European banking system. The banks will be able to continue drawing money from the ECB at its record low interest rate of 1 percent.

To assure the markets that he meant business, Trichet ordered the ECB to buy large volumes of bonds from the two countries most directly under fire from speculators. The ECB undertook its most aggressive buying spree since May of this year, purchasing a total of €100 billion in mainly Portuguese and Irish government bonds.

Stock markets reacted with satisfaction to Trichet's comments and actions. All of the major European indices gained between 1 and 2 percent, and the Dow in America rose 0.76 percent. The euro also rose against the dollar, reflecting the positive reaction by bond markets to Trichet's remarks and the ECB intervention into the market.

These actions provide further evidence of the way in which international financial firms and rating agencies are dictating policy not only to national governments, but also to Europe's central bank.

Earlier this month, Trichet made clear to German and French officials that he was opposed to continuing the ECB policy of buying up large amounts of government bonds from ailing European countries at the inflated interest rates demanded by the bond markets. Having already purchased billions in Greek government bonds earlier this year, the ECB was under increasing pressure to buy Irish bonds to prevent the collapse of the Irish banking system.

EU finance ministers hurriedly put together an €85 billion bailout package for Irish banks attached to draconian conditions, including massive welfare cuts and the plundering of the country's pension fund.

In a series of rushed meetings, EU finance ministers also agreed to a proposal sponsored by Germany and supported by France for a new fund to replace the continent's existing €445 billion rescue fund, which expires in 2013. The new European Stability Mechanism (ESM) is aimed at providing European institutions with the power to implement the “shock therapy” tactics traditionally associated with the International Monetary Fund. The new mechanism also allows for the default of economies in dire straits, with resulting losses for bond holders and major creditors.

Faced with the prospect that they could be called upon to absorb losses, the financial markets reacted with a renewed offensive, pulling funds out of one European country after another. The rating agency Standard and Poor's issued a statement criticising the plans for an ESM that could entail losses for bond holders. To underscore its hostile stance, the agency announced this week that it was placing the Greek economy and leading Portuguese banks on its “down-grade watch.”

Trichet’s latest concession is unlikely to slake the money lust of the financial markets. The *Financial Times* noted Friday that some leading bankers were “left downcast” by Trichet's remarks, with an investment strategist declaring, “Trichet’s statement was disappointing. Markets were looking for more.”

The newspaper quoted one banker demanding: “The ECB needs to use the bazooka option to lift sentiment in a lasting way. That is the only way to stop this crisis spreading. We had a good day today, but yields are only coming down because the ECB is buying. It has got to continue doing so and in size.”

Details of such a “bazooka option” were provided by another financial strategist who advised the ECB to increase its spending on the bonds of ailing European countries by €1 trillion to €2 trillion.

Other senior bankers and financial experts view the prospect of such a strategy by the ECB with alarm. Trichet announced that the decision in favour of unlimited liquidity for the banks had been taken by a majority of the 22-member ECB board. It is believed that one of the dissidents is the head of the German central bank, Axel Weber, who has repeatedly warned against the inflationary dangers arising from massive interventions by the central bank into the bond markets and has argued for an alternative strategy.

In an editorial Thursday headlined “The Banks are Turning Europe into Scorched Earth”, Thomas Hanke, who heads the opinion section of Germany's leading business newspaper, *Handelsblatt*, wrote that the banks are threatening to plunge Europe into a catastrophe, with national governments unwilling to enforce a policy that involves a restructuring of debts and inevitable losses for the banks.

Hanke compared the current situation with the autumn of 1992, when a sustained onslaught by speculators ripped apart the European Monetary Union (forerunner of the euro) and led to drastic currency devaluations across the continent. This time the euro is at risk.

“For the past three years governments have found no way to quench the fire,” Hanke wrote, continuing, “Much has remained unchanged since 2007, or has got even worse. Through a policy based on unlimited liquidity, the central banks have poured more oil onto the fire.” If this policy remains unchanged, he concluded, “the fire will flare up and consume all of Europe.”

Hanke and German Central Bank head Weber are opposed to writing more blank cheques to the banks, but their own alternative is a political mechanism led by Germany to enforce a strict monetary regime and even more draconian austerity measures across Europe.