Amid warnings of a new financial crash, Fed Chairwoman promotes illusions at Jackson Hole conference

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Yesterday's speech by Federal Reserve chairwoman Janet Yellen to the conclave of central bankers at Jackson Hole, Wyoming recalled events at the gathering 12 years ago. At that meeting, the growing signs of the devastating financial crisis that was to strike in 2008 were completely ignored. That was likewise the situation at this year's meeting, held under conditions where the surge in stock markets is bringing warnings of a major collapse.

The 2005 meeting was organised as a celebration of the achievements of the "Maestro," Fed chief Alan Greenspan, whose policies, it was claimed, had brought a new era of prosperity to the global economy. Only one discordant note was sounded in remarks by the then-International Monetary Fund economist Raghuram Rajan, who warned that easy money might be creating the conditions for a financial crisis. But he was firmly put in his place.

This year's address by Yellen is widely expected to be her last as Fed chairwoman, as her current term expires in February next year and President Trump, who decides on the position, has denounced her in the past.

The circumstances of this year's conclave are, of course, very different from those of 12 years ago, coming as they do after the eruption of the most serious financial crisis since the Great Depression of the 1930s. Nonetheless, there are similarities between the two.

Yellen's speech could be described as a celebration of the achievements of the Fed and other regulatory authorities in putting in place measures to prevent any recurrence of the events of 2008, while totally ignoring the growing signs of the buildup of conditions for another financial disaster.

Yellen began her remarks with a reference to the crisis of a decade ago and then went to a defence of the limited regulations introduced since then, which are now threatened by the plans of the Trump administration to introduce sweeping deregulation.

The measures introduced over the past decade both in the US and around the world had improved financial regulation "to limit both the probability and the adverse consequences of future financial crises," she claimed.

These reforms had strengthened the financial system. Credit was broadly available on good terms and lending had advanced in line with economic activity, "contributing to today's strong economy."

She did not even think it worthy of a reference, let alone an explanation, for why, in view of this "strong economy," hundreds of millions of ordinary working people in the US and around the world are seething with discontent and anger over an economic system that is continually reducing their living standards and social conditions, while the financial speculators, responsible for the crisis, accumulate vast wealth.

According to Yellen, the resilience of the financial system had been boosted, banks were safer, the problem of "too big to fail" had been reduced, and a system had been put in place "to effectively monitor and address risks that arise outside the regulatory perimeter."

"Our resilient financial system is better prepared to absorb, rather than amplify, adverse shocks, as has been illustrated during periods of market turbulence in recent years," she declared.

Of course, Yellen could not maintain, as was the case 12 years ago, that the threat of financial crisis had been overcome. The memories are still much too fresh amid the ongoing impact of the disaster, and, as she herself acknowledged, even at the Jackson Hole gathering of 2007 the discussion was "fairly optimistic about the possible economic fallout from stresses in the financial system."

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So, while “we can never be sure that new crises will not occur,” if the lessons of the past are kept in mind, “we have reason to hope that the financial system and economy will experience fewer crises and recover from any future crisis more quickly, sparing households and businesses some of the pain they endured during the crisis that struck a decade ago.”

Yellen’s speech was the promotion of illusion over reality. It was entitled “Financial Stability a Decade after the Onset of the Crisis,” but the Fed chairwoman passed over without comment one of the most significant financial developments in economic history—the massive accumulation of financial assets by the Fed and other central banks around the world.

One of the reasons Yellen did not even touch on this issue could well be that markets are now so fragile that any indication of how the Fed plans to reduce its asset holdings could itself touch off a financial panic by reducing the cash flows on which speculation has fed.

The Fed’s balance sheet has expanded to $4.5 trillion from around $800 billion before the crisis, while the combined balance sheets of the top four central banks--the Fed, the ECB, the Bank of Japan and the Bank of England--now exceeds $13 trillion. These assets comprise 36 percent of the combined gross domestic product of these countries, triple the share in 2007.

Last year, according to a report by Bloomberg, the world’s 10 largest central banks increased their asset holdings to $21.4 trillion, a 10 percent increase over the previous year.

This further increase in central bank holdings has coincided with the global rise in equity markets, fuelling growing concerns that the formation of a new financial bubble is well advanced.

The warnings come from a number of quarters. In a report prepared for its most recent meeting, Fed staff stated that “vulnerabilities associated with asset valuation pressures had edged up from notable to elevated.”

A report published this week in the *Financial Times* noted: “The cyclically adjusted price-to-earnings ratio of the US stock market has been higher only during the peak of the dotcom boom, and with bond yields still near record lows, there is mounting evidence of investors turning to convoluted, potentially risky bets in search of precious returns.”

Among those risky bets is a return to investment in credit default swaps, which played a critical role in the financial crisis of 2008, along with new forms of speculation such as purchases of the cryptocurrency bitcoin.

This week, Bloomberg published a report that three major banks--HSBC, Citigroup and Morgan Stanley--see mounting evidence of a major downturn in the business cycle.

“Analysts at the Wall Street behemoths cite signals including the breakdown of long-standing relationships between stocks, bonds, and commodities as well as investors ignoring valuation fundamentals and data. It all means stock and credit markets are at risk of a painful drop,” the report stated.

Andrew Sheets, a market strategist at Morgan Stanley, linked conditions to those that prevailed between 2005 and 2007.

But even as they warn of what is to come, the major banks and finance houses continue on the path to disaster, recalling the infamous remarks of Citigroup chief Chuck Prince in July 2007 that “as long the music is playing, you’ve got to get up and dance.”

The 2008 financial crisis caught the American and international working class by surprise and it was unprepared for the social devastation that followed. Now, the lessons of the past decade must be drawn and acted upon. Not only do the ruling political and financial elites have no answer to the contradictions of the profit system over which they preside, their very actions have prepared the conditions for an even bigger disaster.

No one can predict when a new financial crash will strike, but the conditions for it are well advanced. It will bring an eruption of social struggles and intensified class conflicts in which the decisive question is the fight for a socialist program and the construction of a revolutionary leadership.

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