Fed gives banks green light to resume share buybacks

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The US Federal Reserve has given major banks the go-ahead to resume share buybacks starting in the first quarter of next year, signalling a victory for them in what has been a public campaign against restrictions imposed in June.

The Fed decision was made after "stress tests" conducted on the major banks showed they could withstand a major downturn in the economy.

It had been widely expected that the banks would pass the tests. But it had been thought that with the US continuing to report record COVID-19 infections and deaths and consequently a highly uncertain outlook for the US economy, the Fed would maintain its restrictions.

Susan Katzke, an analyst at Credit Suisse, told Bloomberg the Fed move was a "clear positive."

"Passing [the stress tests] was expected; the ability to buy back stock, within limits, was hoped for but not expected," she said.

Announcing the stress test results, Fed Vice-Chair for Supervision Randal Quarles said the banking system had been a "source of strength" during the past year and the stress tests confirmed that large banks could continue to lend "even during a sharply adverse turn in the economy."

The only dissenting voice among Fed governors was that of Lael Brainard. She said that for several large banks the projected losses under the tests took them "very close to the minimum requirement."

"Prudence would call for more modest payouts to preserve lending to households and borrowers during an exceptionally challenging winter."

The reaction to the decision was immediate. Within minutes of the Fed announcement, JP Morgan Chase announced that its board had approved up to $30 billion in share buybacks, with the timing and extent of the purchases subject to "various considerations." Morgan Stanley said that its board had authorised up to $10 billion of repurchases in 2021, starting in the first quarter.

Citigroup, Wells Fargo and Bank of America also said they intended to resume share buybacks.

There were significant increases in the share prices of major banks in after-hours trading on Friday following the decision by the Fed. JP Morgan shares rose 5.3 percent, Goldman Sachs 4.4 percent and Wells Fargo 3.5 percent.

The announcement was not a complete winding back of restrictions imposed by the Fed six months ago, but it represented a significant step in that direction, and the banks will no doubt continue to push for all impediments to be removed.

The decision is another expression of how the financial system operates as an institutionalised mechanism for siphoning wealth to the upper strata in the midst of the worst economic recession in the past-war period.

As a result of the ultra-cheap monetary policies pursued by the Fed, above all the injection of trillions of dollars into the Treasury bond market, the banks have been able cash in through market trading.

Back in October, JP Morgan Chase reported profits of $9.44 billion, or $292 per share – well above market expectations – and an increase on the profit of $9.08 billion for the corresponding quarter last year.

The bank's bond and stock trading operation accounted for a 20 percent increase in year-on-year revenues.

Now these profits, reaped from the largesse of the Fed, will now be distributed to wealthy individuals as well as investment funds that own bank shares. The effect of the share buybacks is to lift the price of the remaining shares, enabling their owners to realise a capital gain.

Share buybacks have been assuming greater importance in the banking industry in recent years and now make up around 70 percent of the capital payouts to shareholders.

There has been a rising clamour for easing of restrictions. This is because after falling sharply in March and April—more than 15 percent for JP Morgan and Bank of America and 29 percent for Wells Fargo—bank shares have not risen as fast as the rest of the market, where indexes have reached record highs.

The Fed decision was not a complete free-for-all. Dividends will continue to be capped and the repurchases in the first quarter cannot exceed the average annual quarterly profit for the four most recent quarters.

Reacting to the decision, the ranking Democratic on the Senate Banking Committee, Sherrod Brown, engaged in some "left"-sounding bluster.

"This public health and economic crisis is getting worse, not better," he said. "The Fed's decision allows billions in dividends and bonuses for a select few while millions of Americans are reeling."

That is perfectly true. But the fact remains the incoming Democratic Biden administration has no essential differences with the policy of malign neglect practised under Trump with regard to COVID-19. The Democrats also backed the CARES Act, which bailed out the corporations, and have supported all the measures of the Fed that have transferred billions into the hands of the banks and the financial oligarchy.