All eyes in financial markets on Deutsche Bank

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Deutsche Bank will be the focus of attention when markets open today after statements from the top levels of the financial and political establishment in Europe that it is sound, a sure sign it is in significant trouble.

The question being asked after the forced takeover of the Swiss global bank Credit Suisse a week ago is whether Deutsche is the next one to go.

In trading on Friday its shares dropped by as much as 15 percent at one stage, the third day of consecutive falls, before finishing the day more than 8 percent down.

The share fall was triggered by the announcement by Deutsche, which is Europe's eighth-largest bank by asset holdings, that it would redeem a group of outstanding bonds before their maturity in 2028. The aim of the decision appears to have been to demonstrate to financial markets that its liquidity position was sound.

It seems to have had precisely the opposite effect as investors remain unconvinced.

The rates on five-year credit default swaps for the bank, a financial instrument through which investors seek to insure themselves against a default on its debt, have risen sharply, implying that, at least for one group of bonds, the probability of a default is 30 percent.

This has been reported as being higher than the level reached in the 2008 crisis.

German chancellor Olaf Scholz was quick to intervene in response to the share market fall, rejecting comparisons between Deutsche and Credit Suisse.

Speaking after a European Union summit meeting in Brussels on Friday, when asked if it might go the way of the failed Swiss bank, he said: "Deutsche Bank has fundamentally modernised and reorganised its business and it is a very profitable bank. There is no reason whatsoever to be concerned."

History suggests otherwise. Like Credit Suisse, Deutsche Bank has a record of criminal-like activity and featured prominently in the 2011 US Senate report on the 2008 crash because of its heavy involvement in the sub-prime fraud.

Scholz said the European banks were "stable" and their capital adequacy "robust, thanks to the work of authorities over the past few years" and to "the efforts of the banks themselves."

In the past four years, Deutsche has carried out a restructuring which has resulted in thousands of job cuts and a move away from more risky operations. But there are concerns about its exposure to American commercial real estate, which is being heavily impacted by the interest rate rises of the US Federal Reserve over the past year and the decline in the demand for office space because of the pandemic.

In addition, the *Financial Times* has noted that "the bank's domestic retail lender is barely profitable."

Scholz was not the only European leader to weigh in.

French president Emmanuel Macron, who has made it clear he is using dictatorial measures to force through his attack on pensions, not least because of the demands of financial markets, suggested speculators were behind the fall in Deutsche shares before making the obligatory statement that the fundamentals of the European banking system were sound.

Dutch prime minister Mark Rutte also chimed in, saying the European banking union and its oversight system was sound and provided "absolute clarity that our European banks are safe."

The European Central Bank did not issue an official statement in a seeming continuation of the policy it adopted over Credit Suisse, when it reportedly decided that such action could make the situation worse.

But comments by ECB president Christine Lagarde to the eurozone summit were made known to the press. She reportedly told the meeting that the eurozone banking system was "resilient" with "strong capital and liquidity provisions."

She attempted to address concerns the interest hikes instituted by central banks in their so-called "fight against inflation" – in reality a policy aimed at trying to suppress the wages upsurge of the working class – were leading to mounting problems in financial markets.

The ECB, she claimed, could raise interest rates to fight inflation, while supporting banks with more liquidity.

"Our toolbox enables us to address rises to both," she is reported to have said.

Assessments by financial analysts of the broader significance of the Deutsche Bank developments are divided at this point.

Stuart Graham of Autonomous Research said while investors were worrying about the bank, his firm was "relatively relaxed" because of its "robust" capital and liquidity positions.

"We have no concerns about Deutsche's viability or asset marks. To be crystal clear – Deutsche is NOT the next Credit Suisse."

Such statements about the bank's safety only raise the question of why he felt the need to heavily emphasise it.

The FT reported comments by Andrew Coombs, an analyst at Citibank, who said investors were trying to make sense of the sharp fall in the share price and he viewed it as "an irrational market."

Others have a different view. The chief market analyst with the online trading firm IG Chris Beauchamp said: "Looks like the banking crisis hasn't been entirely put to bed. We are still on edge waiting for another domino to fall, and Deutsche, is clearly the next one on everyone's mind, fairly or unfairly."

The *Australian Financial Review* reported that Equiti Capital head macro economist Stuart Cole said Deutsche had been under a similar spotlight to Credit Suisse.

"It has gone through various restructurings and changes of leadership to get it back on a solid footing, but so far none of these efforts appear to have worked," he said.

The AFR also reported comments by Naeem Aslam, chief investment officer at Zaye Capital Markets, who has drawn attention to the rising costs of credit default swaps for Deutsche.

He wrote in an emailed note that Deutsche was "too big to fail" and if it went to a bailout this would "pave the way for many more in the very near future."

Whatever the reassurances issued by government leaders and financial authorities about the "resilience" of the banking system because of regulations and procedures adopted in response to the 2008 crisis, the wash-up from the unwinding of Credit Suisse has exposed this fiction.

The Swiss government, the regulatory authority Finma and the Swiss National Bank have been criticised for the way they overturned agreed procedures in organising the operation.

But in a series of statements over the past few days, defending themselves, the officials involved have said had they followed the rules and organised a government takeover and a stabilisation, a process called "resolution", a systemic crisis of the banking system would have resulted.

Finma was the first into the fray issuing a statement on Thursday that it had to act unilaterally because of the urgency of the situation.

On the same day, Swiss National Bank chairman Thomas Jordan further elaborated saying "resolution" would have risked a systemic crisis.

"Resolution in theory is possible under normal circumstances, but we were in a fragile environment with enormous nervousness in financial markets in general. Resolution in those circumstances would have triggered a bigger financial crisis, not just in Switzerland but globally."

Jordan may well have said more than he possibly intended, because if resolution is only possible in "normal" circumstances, but not in a crisis, then it is not ever possible in the event of a major failure, such as that of Credit Suisse, which, by its very nature, is a crisis.

The Swiss finance minister, Karin Keller-Sutter, elaborated further in an interview with the Swiss newspaper NZZ on Saturday, in which she called into question the entire global regulatory system developed after the 2008 crash, supposedly to prevent it happening again.

She said following the emergency protocols for the failure of big banks, as in the case of Credit Suisse, "would have triggered an international financial crisis."

"Personally I have come to the conclusion," she said, "that a globally active systemically important bank cannot simply be wound up according to the 'too big to fail' plan. Legally, this would be possible. In practice, however, the economic damage would be considerable."

The implications of this statement warrant the most serious consideration.

They signify that the countless hours of discussions, involving the top levels of government, financial regulators, representatives of major banks and financial corporations and the generation of complex computer models all supposed to stop a crisis like that of 2008, or even worse, have been completely worthless.

The enormous dangers posed by the toxic banking and financial system to the functioning of the economy and the jobs, living standards and livelihood of billions of workers and their families all over the world cannot be ended through some kind of "reform" of the system. There is none. The experience of the past 15 years proves it.

With every deepening of the banking and financial crisis, the socialist case for the ending of the private ownership of the banks and financial giants and bringing them into public ownership under democratic control has become undeniable.