Crush Labor and Impose Austerity: ECB Head Draghi's Real Goal for the Eurozone

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Imagine if your banker offered to lend you a $150,000 to make up for the money that you'd lost on your home since the housing bubble burst in 2006. And, let's say, he agreed to lend you this money for 3 years at rock-bottom rates of 1 percent provided that you post the contents of your garage (ie. rusty bikes, a bent basketball hoop, an old dollhouse, and rodent-infested luggage) as collateral on the loan.

Would that seem like a good deal to you?

On Wednesday, the European Central Bank (ECB) made this very same offer to over a hundred underwater banks in Europe, awarding them $640 billion (489 euros) in dirt-cheap 3-year loans in exchange for all manner of dodgy collateral for which there is currently no market. Now you, dear reader, know that when you try to sell something on Craig's List and there's very little interest; you have to drop the price in order to attract a buyer. That's just how supply-demand dynamics work in a free market, right?

Au contraire. In fact, this rule never applies to bankers. When the junk assets on a bank's balance sheet begin to fall in value, the banks just ring-up their big brother at the ECB or the Fed and demand a bailout, er, I mean, "swap liquidity for collateral that is temporarily impaired." But the truth is, the garbage that the banks have accumulated–particularly the sovereign bonds from Italy, Spain, Greece, etc–is not merely "impaired". These bonds will never regain their original value because the loans were made at the peak of a bubble. So, there's as much chance that Greek bonds will bounce back in three years as there is that that tacky $650,000 McMansion you bought in Encinito in 2005 will claw its way back to par.

That's not going to happen.

So, the $640 billion that the ECB forked out on Tuesday, is basically a whopping-big gift to the banksters that will probably never be repaid. And if you have any doubt about this, then just take look at the Fed's balance sheet which has exploded to nearly $3 trillion. You'll notice that the $1.45 trillion in mortgage-backed securities (MBS) that Bernanke bought from the banks two years ago has not gone down at all, mainly because no one in their right-mind would buy these turkeys. And, if the Fed were to put their stash of MBS up for auction; the sale would further depress the assets on the banks balance sheets triggering another financial crisis. (In fact, this actually happened about a year ago when the government experimented with bonds from the AIG fund. Not only did the auction fail, but it also sent the equities markets into a nosedive) So, just as the Fed will eventually have to account for the losses on their pile of MBS, so too will EU banks have to writedown the losses their sovereign bonds. That will push many of the banks into bankruptcy, which will undoubtedly trigger another round of loans. When financial institutions are insolvent, their only choice is to extend and pretend. Obviously, the ECB sees its job as helping with this fakery.

This is a familiar pattern with central banks. They create the easy money and loose regulatory environment where bubbles emerge, and then they provide "limitless" liquidity so their friends don't lose money on the inflated value of their assets. That's what Tuesday's $640 billion boondoggle was really all about, propping up toxic bonds that are worth a mere fraction of their original value.

So far, though, Draghi's Long-Term Refinancing Operation (LTRO) has been a spectacular flop. While interbank lending rates have dropped ever-so-slightly (3-month Euribor fell from 1.404 to 1.410 percent), the banks have not been using the loans to buy more sovereign bonds (which would push down bond yields for struggling sovereigns) or to increase their lending. Instead, they've parked a good portion of the money in overnight deposits at the ECB. Here's the scoop from the *Wall Street Journal*:

> "Use of the European Central Bank's overnight deposit facility reached a new record high for the year Thursday, suggesting recent measures by central banks and policy makers still aren't enough to restore confidence in inter-bank lending markets.
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> Banks deposited €346.99 billion ($453.38 billion) in the overnight deposit facility, up from €264.97 billion a day earlier and a previous high for the year of €346.36 billion, reached earlier this month.
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> The high level reflects ongoing distrust in inter-bank lending markets, where banks prefer using the ECB facility as a safe haven for excess funds rather than lending them to other banks.
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> The high deposit level also suggests markets aren't fully convinced that the ECB's massive long-term loan allotment is enough to fortify the currency bloc's banking sector. The central bank extended nearly half a trillion euros in long-term loans to euro-zone banks Wednesday, hoping to ease fears of a new credit crunch as banks struggle to borrow from markets." ("ECB Overnight Deposits Reach New 2011 High", Wall Street Journal)

Can you believe it? So, while most of the loans were used to roll over existing debt, $453.38 billion was stuck back in the vaults of the ECB for safekeeping. In other words, the banks are just as distrustful of each other as they were before the lending facility was launched. And the same is true of the yields on Spanish and Italian debt which Draghi thought would drop after he pumped a half a trillion euros into the banking system. Here's the story from Reuters:

> "Spanish and Italian bond yields crept higher on Thursday and underperformed German debt as markets grew sceptical that banks would use funds borrowed from the European Central Bank to buy lower-rated government bonds.
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> Banks borrowed a huge 489 billion euros from the ECB at an unprecedented offer of three-year loans on Wednesday, which some had expected to be reinvested in Spanish and Italian debt and help ease borrowing costs.
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> But, those looking for an immediate boost to Italy and Spain were likely to be

> disappointed. Traders said the preference was to reinvest some of the funds into safe-haven paper rather than pick up the higher yields on offer from some of Europe's more troubled states.
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> "What happened yesterday is not a silver bullet to the crisis… but it is too soon to see the impact yet," said Niels From, strategist at Nordea in Copenhagen." ("EURO GOVT-Spain, Italy yields rise; hope of ECB relief wanes", Reuters)

Unbelievably, the benchmark Italian 10-year BTP rose above the 7 percent mark again on Friday morning signalling renewed stress in the bond market. So while Draghi's program may have breathed new life into a few teetering banks, it has failed miserably of all its main objectives.

So why has Draghi handled the crisis the way he has? Why did he sit on his hands for so long while interbank lending slowed, overnight deposits climbed to new records, sovereign bond yields skyrocketed, and all the gauges of market stress got so much worse?

The obvious answer to this question is that Draghi's been using the crisis to pursue his own agenda. He wants to push through his so called "fiscal compact" that enshrines harsh budget discipline and labor-battering austerity measures into law so that national budgets will come under the control of financial elites (aka–ECB-designated "technocrats") Naturally, nations aren't going to surrender that kind of authority without a fight, so Draghi let the crisis get out-of-hand so there would be less resistance. Here's how economist Dean Baker sums it up:

> "The people who gave us the eurozone crisis are working around the clock to redefine it in order to profit politically. Their editorials – run as news stories in media outlets everywhere – claim that the euro crisis is a story of profligate governments being reined in by the bond market. This is what is known in economics as a "lie".
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> The eurozone crisis is most definitely not a story of countries with out of control spending getting their comeuppance in the bond market…It is a story of countries victimized by the mismanagement of the ECB….People should recognize this process for what it is: class war. The wealthy are using their control of the ECB to dismantle welfare state protections that enjoy enormous public support".

Draghi's real goal is to implement the labor reforms and "adjustments" that big finance demands. He's already succeeded in deposing two democratically elected leaders in Greece and Italy and replacing them with bank-friendly stooges that will carry out his diktats. Now, he's on to bigger things, like slashing the social safety net, crushing the unions, and reducing the eurozone to third world poverty.

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