The ECB's Noose Around Greece: How Central Banks Harness Governments

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Remember when the infamous Goldman Sachs delivered a thinly-veiled threat to the Greek Parliament in December, warning them to elect a pro-austerity prime minister or risk having central bank liquidity cut off to their banks? (See January 6th post here.) It seems the European Central Bank (headed by Mario Draghi, former managing director of Goldman Sachs International) has now made good on the threat.

The week after the leftwing Syriza candidate Alexis Tsipras was sworn in as prime minister, the ECB announced that it would no longer accept Greek government bonds and government-guaranteed debts as collateral for central bank loans to Greek banks. The banks were reduced to getting their central bank liquidity through "Emergency Liquidity Assistance" (ELA), which is at high interest rates and can also be terminated by the ECB at will.

In an interview reported in the German magazine Der Spiegel on March 6th, Alexis Tsipras said that the ECB was "holding a noose around Greece's neck." If the ECB continued its hardball tactics, he warned, "it will be back to the thriller we saw before February" (referring to the market turmoil accompanying negotiations before a four-month bailout extension was finally agreed to).

The noose around Greece's neck is this: the ECB will not accept Greek bonds as collateral for the central bank liquidity all banks need, until the new Syriza government accepts the very stringent austerity program imposed by the troika (the EU Commission, ECB and IMF). That means selling off public assets (including ports, airports, electric and petroleum companies), slashing salaries and pensions, drastically increasing taxes and dismantling social services, while creating special funds to save the banking system.

These are the mafia-like extortion tactics by which entire economies are yoked into paying off debts to foreign banks – debts that must be paid with the labor, assets and patrimony of people who had nothing to do with incurring them.

Playing Chicken with the People's Money

Greece is not the first to feel the noose tightening on its neck. As *The Economist notes*, in 2013 the ECB announced that it would cut off Emergency Lending Assistance to Cypriot banks within days, unless the government agreed to its bailout terms. Similar threats were used to get agreement from the Irish government in 2010.

Likewise, says *The Economist*, the "Greek banks' growing dependence on ELA leaves the government at the ECB's mercy as it tries to renegotiate the bailout."

Mark Weisbrot commented in the Huffington Post:

> We should be clear about what this means. The ECB's move was completely unnecessary . ... It looks very much like a deliberate attempt to undermine the new government.
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> . . . The ECB could . . . stabilize Greek bond yields at low levels, but instead it chose . . . to go to the opposite extreme — and I mean extreme — to promote a run on bank deposits, tank the Greek stock market, and drive up Greek borrowing costs.

Weisbrot observed that the troika had plunged the Eurozone into at least two additional years of unnecessary recession beginning in 2011, because "they were playing a similar game of chicken. . . . [T]he ECB deliberately allowed these market actors to create an existential crisis for the euro, in order to force concessions from the governments of Spain, Italy, Greece, Portugal, and Ireland."

The Tourniquet of Central Bank Liquidity

Not just Greek banks but all banks are reliant on central bank liquidity, because they are all technically insolvent. They all lend money they don't have. They rely on being able to borrow from other banks, the money market, or the central bank as needed to balance their books. The central bank (which has the power to print money) is the ultimate backstop in this sleight of hand. If that source of liquidity dries up, the banks go down.

In the Eurozone, the national central banks of member countries have relinquished this critical credit power to the European Central Bank. And the ECB, like the US Federal Reserve, marches to the drums of large international banks rather than to the democratic will of the people.

Lest there be any doubt, let's review Goldman's December memo to the Greek Parliament, reprinted on Zerohedge. Titled "From GRecovery to GRelapse," it warned:

> [H]erein lies the main risk for Greece. The economy needs the only lender of last resort to the banking system to maintain ample provision of liquidity. And this is not just because banks may require resources to help reduce future refinancing risks for the sovereign. But also because banks are already reliant on government issued or government guaranteed securities to maintain the current levels of liquidity constant.
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> In the event of a severe Greek government clash with international lenders, interruption of liquidity provision to Greek banks by the ECB could potentially even lead to a Cyprus-style prolonged "bank holiday". And market fears for potential Euro-exit risks could rise at that point. [Emphasis added.]

Why would the ECB have to "interrupt liquidity provision" just because of a "clash with international lenders"? As Mark Weisbrot observed, the move was completely unnecessary. The central bank can flick the credit switch on or off at its whim. Any country that resists going along with the troika's austerity program may find that its banks have been cut off from this critical liquidity, because the government and the banks are no longer considered "good credit risks." And that damning judgment becomes a self-fulfilling prophecy, as is happening in Greece.

"The Icing on the Cake"

Adding insult to injury, the ballooning Greek debt was incurred to save the very international banks to which it is now largely owed. Worse, those banks bought the debt with cheap loans from the ECB! Pepe Escobar writes:

> The troika sold Greece an economic racket …. Essentially, Greece's public debt went from private to public hands when the ECB and the IMF 'rescued' private (German, French, Spanish) banks. The debt, of course, ballooned. The troika intervened, not to save Greece, but to save private banking.
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> The ECB bought public debt from private banks for a fortune, because the ECB could not buy public debt directly from the Greek state. The icing on this layer cake is that private banks had found the cash to buy Greece's public debt exactly from…the ECB, profiting from ultra-friendly interest rates. This is outright theft. And it's the thieves that have been setting the rules of the game all along.

That brings us back to the role of Goldman Sachs (dubbed by Matt Taibbi the "Vampire Squid"), which "helped" Greece get into the Eurozone through a highly questionable derivative scheme involving a currency swap that used artificially high exchange rates to conceal Greek debt.

Goldman then turned around and hedged its bets by shorting Greek debt.

Predictably, these derivative bets went very wrong for the less sophisticated of the two players. A €2.8 billion loan to Greece in 2001 became a €5.1 billion debt by 2005.

Despite this debt burden, in 2006 Greece remained within the ECB's 3% budget deficit guidelines. It got into serious trouble only after the 2008 banking crisis. In late 2009, Goldman joined in bearish bets on Greek debt launched by heavyweight hedge funds to put selling pressure on the euro, forcing Greece into the bailout and austerity measures that have since destroyed its economy.

Ambrose Evans-Pritchard wrote in the UK Telegraph on March 2nd:

> Syriza has long argued that [its post-2009] debt is illegitimate, alleging that the ECB bought Greek bonds in 2010 in order to save the European banking system and prevent contagion at a time when the eurozone did not have a financial firewall, not to help Greece.
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> Mr. Varoufakis [the newly-appointed Greek finance minister] said the result was to head off a Greek default to private creditors that would have led to a large haircut for foreign banks if events had been allowed to run their normal course, reducing Greece's debt burden to manageable levels. Instead, the EU authorities took a series of steps to avert this cathartic moment, ultimately foisting €245bn of loan packages onto the Greek taxpayer and pushing public debt to 182pc of GDP.

The Toxic Central Banking System

Pepe Escobar concludes:

> Beware of Masters of the Universe dispensing smiles. Draghi and the … ECB goons may dispense all the smiles in the world, but what they are graphically demonstrating once again is how toxic central banking is now enshrined as a mortal enemy of democracy.

National central banks are no longer tools of governments for the benefit of the people. Governments have become tools of a global central banking system serving the interests of giant international financial institutions. These "too big to fail" behemoths must be saved at the expense of local banks, their depositors, and local economies generally.

How to escape the tentacles of this toxic squid-like banking hierarchy?

For countries with a bit more room to maneuver than Greece has, one option is to withdraw public and private deposits and put them in publicly-owned banks. The megabanks are deemed too big to fail only because the people's money is tied up in them. They could be allowed to fail if public funds were not at risk.

The German SBFIC (Savings Banks Foundation for International Cooperation) has proposed a pilot project on the Sparkassen model for Greece. Other provocative options have also been proposed, to be the subject of another article.

Ellen Brown is an attorney, founder of the Public Banking Institute, and author of twelve books including the best-selling Web of Debt. Her latest book, The Public Bank Solution, explores successful public banking models historically and globally. Her nearly-300 blog articles are at EllenBrown.com. Listen to "It's Our Money with Ellen Brown" on PRN here.

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