European ‘bail-ins’ continue to fuel global crash

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Shares in major Italian bank Monte dei Paschi (MPS) fell 22 per cent on 20 January, reducing its stock value to one-fifth of net capital. On 18 January trading in MPS shares was suspended following a series of large daily falls. According to an article in the Italian daily *Il Fatto*, depositors who had more than €100,000 have pulled €1 billion out of the bank since 1 January. The rate of withdrawal is €2 billion a month. Liquidity at MPS has gone down from €20 billion to probably €17 billion, the “target” level of one-tenth of the assets. A default is not far away.

Prime Minister Matteo Renzi and his Treasury Minister appeared on television to say that Italian banks are safe, and there is no reason to panic, but Renzi did admit that MPS is up for sale. A number of prominent Italian political figures have called on Italy to declare a moratorium on the new European-wide bail-in agreement, the Bank Recovery and Resolution Directive (BRRD).

In a 20 January speech, American Federal Deposit Insurance Corporation (FDIC) Vice-Chairman Thomas Hoenig declared that bank bail-ins won’t work, and will further destabilise the financial system in an attempt to keep units of insolvent banks in operation. Hoenig focused on the latest rule proposed by the US Federal Reserve mandating that banks raise as much as $550 billion in “loss-absorbing capital”, informally called “bail-in bonds”. As big banks become insolvent in the crash, the “bail-in bonds” would instantly become stock of next-to-no value in a new holding company.

According to a Reuters report, Hoenig said, “‘Mandating increased levels of debt as part of a broad, prescribed resolution strategy has potential effects that, paradoxically, may undermine the very financial stability being sought. The proposal would force banks to issue hundreds of billions of dollars in new debt and encourage them to acquire riskier, higher-yielding assets or expand into non-bank activities to cover costs.’ The proposal ‘offers no assurance that the amount of debt required would prove sufficient to avoid a failure, or panic’, Hoenig added.”

In the last couple of weeks there has been a flurry of warnings of an economic downturn in 2016 from some of the most prominent financial institutions worldwide. The World Bank warned of the potential for a “perfect storm”; the IMF has said we face major challenges in 2016 and that global growth could be “derailed”; and various warnings were made by prominent figures at the Davos World Economic Forum held 20-23 January, such as mega-speculator George Soros, who declared that we are repeating the events of 2008. “It was a time of financial crisis and bear markets, and you have the same conditions again.”

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