How London's Euromarket killed Bretton Woods

By Elisa Barwick

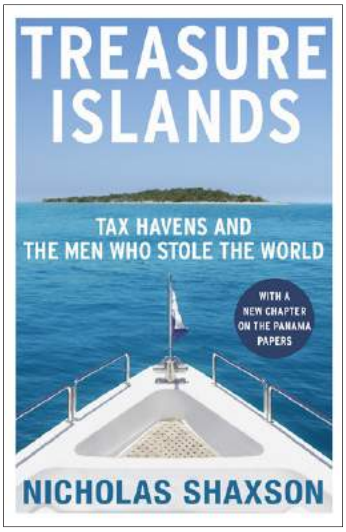
The deregulation of the global financial system, which reached a pinnacle in 1999 when the US Congress repealed the *Glass-Steagall Act*, was set into motion in 1971 with the dismantling of the 1944 Bretton Woods Agreement. This is the story of the driver behind that deregulation, which unleashed the cancer of financial speculation which in turn caused the 2008 global financial crash (GFC), and is about to unleash a new, even worse crisis. This could be triggered by today's currency crises in emerging markets, made possible due to the demise of Bretton Woods.

The plan to subjugate productive national economies to a global system that enabled elite bankers to loot wealth through speculation began in earnest in the mid-1950s. British elites schemed to create a new financial market outside of any national jurisdiction, but controlled at arm's length by the City of London—the Eurodollar Market. This led to: the destruction of the Bretton Woods fixed exchange rate order, allowing rampant currency speculation to interfere with markets and trade; the dismantling of Glass-Steagall regulations that prevented banks from speculating, setting us up for the GFC; and the establishment of a global spider's web of tax havens that facilitated the expansion of criminal activity worldwide by providing an extensive, secret and impenetrable legal infrastructure for tax dodging and money laundering.

The 1944 conference of 44 nations at Bretton Woods in New Hampshire, USA, created an international monetary system as an agreement between sovereign nations. The agreement established a system of fixed currency exchange rates relative to the US dollar which was pegged to gold, in order to ensure a stable international trading system and prevent currency speculation. Institutions and regulations to uphold the agreed order were established. Under the agreement a US citizen or institution, for instance, could not maintain an account outside of the United States in which dollars were deposited, without documentary proof that it was for the purpose of settling trade accounts. Banks could purchase foreign currency to transact trades for their clients, such as long-term investments, but could not take deposits in foreign currencies. Countries used capital controls to regulate the inflow and outflow of investment capital.

The Bretton Woods system began to be eroded no later than the late 1950s, with the creation of the Eurodollar, a London-based "dollar" currency for global speculation. In his landmark book, *Treasure Islands: Tax Havens and the Men Who Stole the World*, British author Nicholas Shaxson notes that "The terms 'Eurodollar' and 'Euromarkets' are actually misnomers. The markets have nothing really to do with today's euro currency, nor do they trade only in American dollars; all the world's main currencies are traded like this today. It was at this point that the modern offshore system really began. And, as is usual with so much that happens in the offshore system, almost nobody noticed."

It was a deliberate action to wreck the Bretton Woods system, by attracting US dollars to London with higher interest rates (US interest rates were capped) and creating loopholes to allow US banks to get around strict regulations associated with Bretton Woods, Glass-Steagall and the US *Bank Holding Company Act of 1956*. Attracting vast volumes of US dollars to London, the British declared those dollar operations were not occurring in the UK at all, but "elsewhere"—the undefined, unregulated offshore space where the Eurodollar market grew.



How it began

In the mid 1950s unusual offshore activity sprouted in the City of London. According to Shaxson, in 1955 the Midland Bank started offering higher interest rates on US dollar deposits than were allowed by US regulations. The Bank of England noticed this happening, but did not intervene to stop it as it represented a new potential for international business. British banks were also finding ways around exchange controls in their currency trading.

This was happening against the backdrop of the growing influence of the Mont Pelerin Society (MPS) which was launched in April 1947. Directed top down by the City of London financial oligarchy, it propagandised against the mechanisms associated with Bretton Woods in favour of unregulated free markets and economic liberalism.

Even if it forced the UK into recession, London was committed to retaining the dominance of the pound sterling—in which some 40 per cent of world trade was still conducted in 1957—by ramping up interest rates to attract capital. The Prime Minister at the time, Harold Macmillan, found he had no ability to force the Bank of England (BoE) to change course despite the fact that it had been nationalised in 1946. When he threatened to change the law to attain control over the banks, BoE governor Lord Cobbold declared that he alone had the power to direct the banks, insinuating he would bankrupt the government if it tried to muscle in. The only measure Macmillan was able to achieve was to limit the lending in pounds of London banks, which threw a significant dampener on their activities. However, the banks merely shifted their international lending into US dollars, an arena unregulated by British authorities. For regulatory purposes such transactions did not technically take place inside British sovereign space. "The private bankers had found an escape route from the close confinement imposed on them after the Second World War", observed Shaxson.

George Bolton, a foreign exchange dealer in the City who became the head of the BoE's foreign exchange department, was in the driver's seat as this new market was developed. Bolton had once remarked, "If we could throw away the stranglehold of the economists' demand management, and extinguish the disease of socialism, we could become a proud people once more." He observed that the Eurodollar market was created by "a conscious effort by a number of us to create a money market from the bits and pieces that were floating about". The new "offshore" financial market was a regulatory vacuum which, Shaxson makes clear, could have been regulated had the BoE wished. The Euromarket was essentially a "bookkeeping device" as one academic put it, to keep transactions off the books.

Shaxson explainined that most studies of London's history as a global financial centre start with the "Big Bang" financial deregulation of 1986 by PM Margaret Thatcher. But British economist and City of London spokesman Tim Congdon declared the Big Bang "a sideshow, indeed almost a by-product of, a much Bigger Bang which has transformed international finance over the last 25 years". That was the creation of the Euromarket, he said, "which has no physical embodiment in an exchange building or even a widely recognised set of rules and regulations, ... [yet is] the largest source of capital in the world". Referencing the role of British economist John Maynard Keynes in negotiating the terms of the Bretton Woods agreement for the UK, academic Gary Burn (author of *The re-emergence of global finance*) called it "the first shot in the neoliberal counter-revolution against the social market and the Keynesian welfare state".

By its very existence this lawless zone forced nations and jurisdictions across the world to liberalise and deregulate in order to compete. Shaxson describes it as "the invisible financial counterpart of the Mont Pelerin Society's ideological insurgency". Referring to the post-World War II movement towards decolonisation, Shaxson said that Britain's formal empire had given way "to something more subtle". This was the origin of Britain's identity as an "informal financial empire", as expressed in a 1995 Royal Institute of International Affairs report, "Economic Opportunities for Britain and the Commonwealth".

Euromarkets take over

"From these beginnings, the London offshore market exploded", Shaxson reported. Jurisdiction after jurisdiction got in on the game, from Zürich to the Caribbean. "Before, countries had been relatively well insulated against financial calamities that happened elsewhere, but the Euromarket connected up the world's financial sectors and economies. A shock rise in interest rates in one place would, as if transmitted by electricity, almost instantly affect anywhere else plugged into the system. And, as it grew and grew, tides of hot money once again began to surge back and forth across the globe." Renowned

With the destruction of Bretton Woods regulations Foreign Exchange turnover grew to exceed most other markets. Photo: DailyFX.com

US economist Alexander Sachs called it "a new banking order ... transforming the rubric of accounting".

By 1975 the Euromarket exceeded the turnover of all foreign exchange worldwide; in 1988 it was worth US$2.6 trillion. By 1997 nearly 90 per cent of international loans were made in dollars from London—i.e. the complete domination of international lending. The Bank for International Settlements even gave up trying to estimate its size.

The Bretton Woods system was undermined well before 15 August 1971 when US President Richard Nixon removed the dollar from its peg to gold, as London had already been exchanging gold for dollars at a depreciated value of the dollar. Given that it was becoming cheaper in London, nations, particularly in Europe, screamed that Bretton Woods was artificially inflating the dollar. The Bank of England Governor, Lord Cromer, declared in 1963, "Exchange control is an infringement of the rights of the citizen. I therefore regard it ethically as wrong."

Also spelling trouble for Bretton Woods was that banks operating through the Euromarket could easily outcompete

The real Goldfinger

British journalist Oliver Bullough wrote an article for the 7 September *Guardian* under the headline, "The real Goldfinger: the London banker who broke the world", adapted from his book published this month, *Moneyland: Why thieves and crooks now rule the world and how to take it back*.

Drawing a parallel with Bond villain Auric Goldfinger, who threatened the global financial system by undermining its gold reserves, Bullough describes the actions of British banker Siegmund Warburg who created the Eurobond market (main article), by finding ways to "defang the taxes and controls designed to prevent hot money flowing across borders". The first bond issue was actually made at the Schiphol airport in the Netherlands, the interest paid in Luxembourg to avoid British taxes, and the London Stock Exchange was convinced to list the bonds despite their not being issued or redeemed in the UK. Soon, the practice became commonplace and jurisdictions changed their rules to accommodate. Now, hidden wealth in Switzerland "could buy these fantastic pieces of paper, which could be carried anywhere, redeemed anywhere and all the while paid interest to their owners, tax free. Dodge taxes and make a profit, worldwide".

Prior to the creation of this market, "people struggled to move their money out of the taxman's reach". To explain why, Bullough uses a metaphor of an oil tanker which has several separate compartments for oil, rather than one large tank where the oil can "slosh backwards and forwards in ever greater waves, until it destabilises the vessel, which overturns and sinks. "At the Bretton Woods conference", he says, "the oil was divided between smaller tanks, one for each country. The liquid could slosh back and forth within its little compartments, but would be unable to achieve enough momentum to damage the integrity of the vessel."

The bankers' moves to get around these controls eroded the system and the Bretton Woods arrangement fell apart. "As long as one country tolerated offshore, as Britain did, then the efforts of all the others came to nothing. If regulations stop at a country's borders, but the money can flow wherever it wishes, its owners can outwit any regulators they choose." And with an expanding sea of US dollar lending creating more and more dollars, it was impossible for the USA to keep buying gold to back it up. The dollar peg had to go.

all other banks. With no reserve requirements they could re-lend 100 per cent of all deposits, rather than a reduced percentage. A BoE statement reported that "reliance is placed on the commercial prudence of the lenders". The Euromarket "made it possible for credit quality to deteriorate out of sight of the regulators", observed Shaxson, displacing better-regulated markets.

US President John F. Kennedy challenged this use of dollars outside the USA, raising with his aides the flouting of capital controls on the dollar in London, and the fact that more dollars were being created and circulated in London than the USA. Kennedy told Congress in 1961 to "drive these tax havens out of existence". Responding to a US complaint, a BoE official responded, "It doesn't matter to me whether Citibank is evading American regulations in London. I wouldn't particularly want to know." US banks moved their international divisions to London, where they remain today, and from where they engaged in much of the derivatives gambling that led to the 2008 global financial crisis. In the UK they were shielded from the controls of government.

In 1963 offshore markets were boosted with the advent of Eurobonds—unregulated and unrecorded bonds held offshore. This was the brainchild of the German-born British financier Siegmund Warburg, who realised many investors would prefer the higher earnings of bonds from their Eurodollars, and this way they avoided the fees ands taxes associated with buying US dollar denominated bonds in New York (box, p. 13). A BoE memo of that year stated, "However much we dislike hot money, we cannot be international bankers and refuse to accept money."

Following Nixon's 1971 action, speculation was allowed to run free and ravage national currencies, undermining the physical trade of nations. Carry trades—the practice of borrowing at near zero interest rates in one location, to relend anywhere in the world that offers higher yields—followed later.

Today, there is an estimated US$5.3 trillion a day in currency speculation transactions. According to dailyfx.com, the foreign exchange market (forex) is the "largest and most liquid market in the world"; the US dollar comprises the majority share of trades; and "roughly 90 per cent of this volume is generated by currency speculators capitalising on intraday price movements", i.e. speculation.

Shaxson observed that the Euromarket had become a kind of "global transmission belt making short-term capital movements more sensitive, rippling interest-rate changes instantly around the globe and allowing enough money to pool together in one place to allow large speculative attacks against currencies that flighty speculators decided were vulnerable." It was in this shadow banking environment, Shaxson expanded, that many of the entities that created the 2008 global financial crisis, such as structured investment vehicles and conduits, were invented.

Via the Euromarket, American banks were able not only to get around Bretton Woods rules but also to circumvent US regulations including the 1933 *Glass-Steagall Act*. This was a major factor in the erosion of Glass-Steagall standards well before its repeal in 1999, which was a turning point for speculation. Banks could then use deposits as the basis for dangerous derivatives gambling, and would be bailed out if they ran into trouble. Before its repeal in 1999, global derivatives contracts recorded by the BIS had taken 13 years, 1986-1999, to grow to US$100 trillion; after the repeal, when banks were free to use deposits as collateral for their gambling, derivatives grew by US$100 trillion per year!

Using the same methods, the Euromarket system spread through a network of former and remaining British colonies, through British Crown Dependencies in the British Isles, the Caribbean Overseas Territories and colonial outposts in Asia and the Pacific atolls. These "offshore Euromarket booking centres" evolved into the large network of tax havens and hot money laundering centres, recently exposed by the Panama Papers.

Over time US authorities succumbed to the Euromarket, as it had granted unprecedented power to the US dollar and a capability for the USA to finance its deficits. Some two-thirds of the foreign exchange reserves of nations are invested in dollars. The Euromarket helped rebuild the London-New York financial axis that had existed prior to the Great Depression, and prior to the regulatory interventions of US President Franklin Roosevelt, the UK government of Prime Minister Clement Attlee and Australia's Labor leaders John Curtin and Ben Chifley. It was all about establishing a new form of imperialism, with London as a world financial hub, under whose thumb every nation struggles today. London became "the capital of a world ruled in the interests of an elite of investors", said Shaxson. "At the moment of its apparent destruction, the British empire began to rise from the dead."

Corbyn will take on the City

In an RT News article on 3 September, ex-Labour MP and former Greater London Mayor Ken Livingstone reviewed the long struggle to keep banks in check. "Back in the 1930s", Livingstone wrote, referring to the *Glass-Steagall Act* of 1933, "the US government responded to the Great Depression by introducing new laws that made it illegal for the local high street banks, in which we all deposit our own money, to make risky gambling decisions". Today, the financial sector is more powerful than ever before and as a result inequality is rising and so too is the anger of the population.

Upon the Labour Party's inception in 1900, Livingstone said, opposition to the City was one of its central planks. Towards the end of WWI, leading Labour party figure Herbert Morrison, referring to the City as "the home of the devilry of modern finance", asked rhetorically, "Is it not time London faced up to the pretentious buffoonery of the City and wipe it off the municipal map?"

Soon-to-be PM Clement Attlee, campaigning for the 1945 election, reminded Britons that "Over and over again we have seen that there is in this country another power than that which has its seat at Westminster. The City of London ..."

The Attlee government succeeded in nationalising the Bank of England in 1946, but it was still run by the same elite merchant bankers. The government had the power to issue directions to the bank; but, according to Livingstone, it admitted in 2010 that "Thus far the power has not been used."

Livingstone told how PM Harold Wilson in 1964 "gave in to pressure from the bank's governor to slash most of his spending promises, causing him to say, 'Who is prime minister of this country Mr Governor, you or me?'"

When Tony Blair became PM he made reforms in their favour and dropped the Party manifesto's pledge to abolish the City of London Corporation (the private municipal body representing the City's bankers), but current Labour leader Jeremy Corbyn has promised to curb the City of London's power. "[W]e can expect the financial sector to do everything in its power to stop Jeremy getting into Downing Street", Livingstone concluded.