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Donald Trump and the Next Crash: Making the Fed an Instrument for Disaster

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Warning: What you are about to read is not about Russia, the 2016 election, or the latest person to depart from the White House in a storm of tweets. It's the Beltway story hiding in plain sight with trillions of dollars in play and an economy to commandeer.

While we've been bombarded with a litany of scandals from the Oval Office and the Trump family, there's a crucial institution in Washington that few in the media seem to be paying attention to, even as President Trump quietly makes it his own. More obscure than the chambers of the Supreme Court, it's a place where he has already made substantial changes. I'm talking about the Federal Reserve.

As the central bank of the United States, the "Fed" sets the financial tone for the global economy by manipulating interest rate levels. This impacts everyone, yet very few grasp the scope of its influence.

During times of relative economic calm, the Fed is regularly forgotten. But what history shows us is that having leaders who are primed to neglect Wall Street's misdoings often sets the scene for economic dangers to come. That's why nominees to the Fed are so crucial.

We have entered a landmark moment: no president since Woodrow Wilson (during whose administration the Federal Reserve was established) will have appointed as many board members to the Fed as Donald Trump. His fingerprints will, in other words, not just be on Supreme Court decisions, but no less significantly Fed policy-making for years to come — even though, like that court, it occupies a mandated position of political independence.

The president's latest two nominees to that institution's Board of Governors exemplify this. He has nominated Richard Clarida, a former Treasury Department official from the days of President George W. Bush who later became a strategic adviser to investment goliath Pimco, to the Fed's second most important slot, while giving the nod to Michelle Bowman, a Kansas bank commissioner, to represent community banks on that same board.

Like many other entities in Washington, the Fed's Board of Governors has been operating with less than a full staff. If Clarida is approved, he will join Trump-appointed Fed Chairman Jerome Powell and incoming New York Federal Reserve Bank head John C. Williams — the New York Fed generally exists in a mind meld with Wall Street — as part of the most powerful trio at that institution.

Williams served as president of the San Francisco Fed. Under his watch, the third largest U.S. bank, Wells Fargo, created about 3.5 million fake accounts, gave its CEO a whopping raise, and copped to a $1 billion fine for bilking its customers on auto and mortgage insurance contracts.

Not surprisingly, Wall Street has embraced Trump's new Fed line-up because its members are so favorably disposed to loosening restrictions on financial institutions of every sort. Initially, the financial markets reflected concern that Chairman Powell might turn out to be a hawk on interest rates, meaning he'd raise them too quickly, but he's proved to be anything but.

As Trump stacks the deck in his favor, count on an economic impact that will be felt for years to come and could leave the world devastated. But rest assured, if the Fed can help Trump keep the stock market buoyant for a while by letting money stay cheap for Wall Street speculation and the dollar competitive for a trade war, it will.

History Warns Us

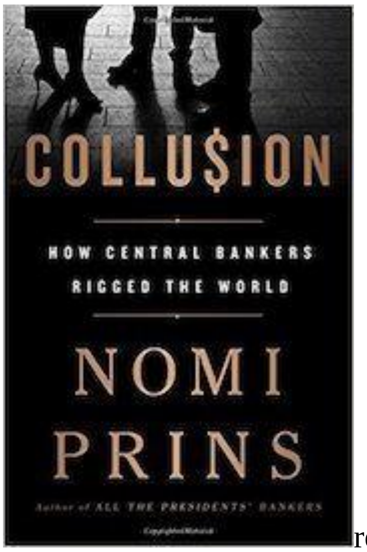
At a time when inequality, economic hardship, and household and personal debt levels are escalating and wages are not, why should any of this matter to the rest of us? The answer is simple enough: because the Fed sets the level of interest rates and so the cost of money. This, in turn, indirectly impacts the value of the dollar, which means everything you buy.

Since the financial crisis, the Fed has kept the cost of borrowing money for banks at near zero percent interest. That allowed those banks to borrow money to buy their own stock (as did many corporations) to inflate their value but not, of course, the value of their service to Main Street.

When money is cheap because interest rates are low or near zero, the beneficiaries are those with the most direct access to it. That means, of course, that the biggest banks, members of the Fed since its inception, get the largest chunks of fabricated money and pay the least amount of interest for it.

Although during the election campaign of 2016 Trump chastised the Fed for its cheap-money policies, he's since evidently changed his mind (which is, of course, very Trumpian of him). That's because he knows that the lower the cost of money is, the easier it is for major companies to borrow it. Easy money means easy speculation for Wall Street and its main corporate clients, which sooner or later will be a threat to the rest of us.

The era of trade wars, soaring stock markets, and Trump gaffes may feel like it's gone on forever. Don't forget, though, that there was a moment not so long ago when the same



banking policies still reigning caused turmoil, ripping through the country and devouring the finances of so many. It's worth recalling for a moment what happened during the Great Meltdown of 2008, when unrestrained mega-banks ravaged the economy before being bailed out. In the midst of the current market ecstasy, it's an easy past to ignore. That's why Trump's takeover of the Fed and its impact on the financial system matters so much.

Let's recall that, on September 15, 2008, Lehman Brothers crashed. That bank, like Goldman Sachs a former employer of mine, had been around for more than 150 years. Its collapse was a key catalyst in a spiral of disaster that nearly decimated the world financial system. It wasn't the bankruptcy that did it, however, but the massive amount of money the surviving banks had already lent Lehman to buy the toxic assets they created.

Around the same time, Merrill Lynch, a competitor of Lehman's, was sold to Bank of America for $50 billion and American International Group (AIG) received $182 billion in government assistance. JPMorgan Chase had already bought Bear Stearns, which had crashed six months earlier, utilizing a $29 billion government and Federal Reserve security blanket in the process.

In the wake of Lehman's bankruptcy, $16 trillion in bailouts and other subsidies from the Federal Reserve and Congress were offered mostly to Wall Street's biggest banks. That flow of money allowed them to return from the edge of financial disaster. At the same time, it fueled the stock and bond markets, as untethered from economic realities as the hot air balloon in *The Wizard of Oz*.

After nearly tripling since the post-financial crisis spring of 2009, last year the Dow Jones Industrial Average rose magically again by nearly 24%. Why? Because despite all of his swamp-draining campaign talk, Trump embraced the exact same bank-coddling behavior as President Obama. He advocated the Fed's cheap-money policy and hired Steve Mnuchin, an ex-Goldman Sachs partner and Wall Street's special friend, as his Treasury secretary. He doubled down on rewarding ongoing malfeasance and fraud by promoting the deregulation of the banks, as if Wall Street's greed and high appetite for risk had vanished.

Impending Signs of Crisis

A quarter of the way into 2018, shadows of 2008 are already emerging. Only two months ago, the Dow logged its worst single-day point decline in history before bouncing back with vigor. In the meantime, the country whose banks caused the last crisis faces record consumer and corporate debt levels and a vulnerable geopolitical global landscape.

True, the unemployment rate is significantly lower than it was at the height of the financial crisis, but for Main Street, growth hasn't been quite so apparent. About one in five U.S. jobs still pays a median income below the federal poverty line. Median household income is only up 5.3% since 2008 and remains well below where it was in 1998, if you adjust for inflation. Workforce participation remains nearly as low as it's ever been. Meanwhile, the top 1% of American earners saw their incomes go up by leaps and bounds since the Fed started manufacturing money — to more than 40 times that of the bottom 90%.

Just as before the 2007-2008 financial crisis, there's a scary level of confidence among politicians and regulators that neither the economy nor the banking sector could possibly go bust. Even the new Federal Reserve chair views the possible need for bailouts as a relic of a bygone time. As he said at his confirmation hearing, "Generally speaking I think the financial system is quite strong." When asked if there are any U.S. banks that are still too big to fail, he responded, "I would say no to that."

That's a pretty decisive statement, and not strikingly different from oneoutgoing Fed Chair Janet Yellen made last year. By extension, it means that Trump's new chairman supports laxer structures for the big banks and more cheap money, if needed, to help them. So watch out.

When a crisis hits, liquidity dies, and banks close their doors to the public. Ultimately, the same formula for crisis will surely send Wall Street executives crawling back to the government for aid and then Donald Trump will find out what financial negligence truly is.

A Time of Crisis and Financial Collusion

As signs of crisis emerge, few in Washington have delved into how we can ensure that a systemic crash does not happen again. That's why I'll never forget the strange message I got one day. It was in the middle of May 2015, about a year after my book, *All the Presidents' Bankers*, had been published, when I received an email from the Federal Reserve. Every year, the Fed, the International Monetary Fund, and the World Bank hold an annual conference where the most elite central bankers from around the globe assemble. To my shock, since I hadn't exactly written in a kindly fashion about the Fed, I was being invited to speak at the opening session about why Wall Street wasn't helping Main Street.

Two months later, I found myself sitting in front of a room filled with central bankers from around the world, listening to Fed Chair Janet Yellen proclaim that the worst of the crisis and its causes were behind us. In response, the first thing I asked that distinguished crowd was this: "Do you want to know why big Wall Street banks aren't helping Main Street as much as they could?" The room was silent. I paused before answering, "Because you never required them to."

I added, "The biggest six U.S. banks have been rewarded with an endless supply of cheap money in bailouts and loans for their dangerous behavior. They have been given open access to these funds with no major consequences, and no rules on how they should utilize the Fed's largess to them to help the real economy. Why should you expect their benevolence?"

After I returned home, I became obsessed with uncovering just how the bailouts and loans of that moment were only the tip of an iceberg, the sort of berg that had once taken down the *Titanic* — how that cheap money fabricated for Wall Street had been no isolated American incident.

What my research for my new book, *Collusion: How Central Bankers Rigged the World*, revealed was how central bankers and massive financial institutions have worked together to manipulate global markets for the past decade. Major central banks gave themselves a blank check with which to resurrect problematic banks; purchase government, mortgage, and corporate bonds; and in some cases — as in Japan and Switzerland — stocks, too. They have not had to explain to the public where those funds were going or why. Instead, their policies have inflated asset bubbles, while coddling private banks and corporations under the guise of helping the real economy.

The zero-interest-rate and bond-buying central bank policies prevailing in the U.S., Europe, and Japan have been part of a coordinated effort that has plastered over potential financial instability in the largest countries and in private banks. It has, in turn, created asset bubbles that could explode into an even greater crisis the next time around.

So, today, we stand near — how near we don't yet know — the edge of a dangerous financial precipice. The risks posed by the largest of the private banks still exist, only now they're even bigger than they were in 2007-2008 and operating in an arena of even more debt. In Donald Trump's America, what this means is that the same dangerous policies are still being promoted today. The difference now is that the president is appointing members to the Fed who will only increase the danger of those risks for years to come.

A crash could prove to be President Trump's worst legacy. Not only is he — and the Fed he's helping to create — not paying attention to the alarm bells (ignored by the last iteration of the Fed as well), but he's ensured that none of his appointees will either. After campaigning hard against the ills of global finance in the 2016 election campaign and promising a modern era Glass-Steagall Act to separate bank deposits from the more speculative activities on Wall Street, Trump's policy reversals and appointees leave our economy more exposed than ever.

When politicians and regulators are asleep at the wheel, it's the rest of us who will suffer sooner or later. Because of the collusion that's gone on and continues to go on among the world's main central banks, that problem is now an international one.

Nomi Prins's new book, Collusion: How Central Bankers Rigged the World *(Nation Books), has just been published. She is a former Wall Street executive.*

Special thanks go to researcher Craig Wilson for his superb work on this piece.

This essay originally appeared in TomDispatch.