Federal Reserve to Bail Out European Banks (Again!)

Starting in October, the Federal Reserve and other major central banks will begin auctioning allotments of dollars to the European Central Bank, which will then use the new money to shore up shaky European megabanks. The allotments, which will have three-month maturities and will be structured like typical repurchase operations ("repos"), will be issued against euro-denominated collateral and repaid, with interest, in dollars. That at least is the theory.

Currency swaps involving the Federal Reserve and other central banks are nothing new, and have been a focal concern of Fed opponents such as Congressman Ron Paul, who has long suggested that much of the Fed's financial chicanery has been carried out in the form of such currency deals with foreign central banks, in total secrecy. This time around, the deal is being touted openly as an unprecedented exercise in international coordination by the world's central banks, a decisive move to solve Europe's long-running sovereign debt crisis.

{modulepos inner_text_ad}

Under the terms of the arrangement, the Fed and other central banks will deal with the European Central Bank, which will then disburse dollars to European commercial banks as it deems necessary. There is no cap on the amount of dollars that the Fed may provide to the ECB under the terms of the swap arrangment, which was first agreed to in principle in May 2010. An earlier swap facility, created by the Fed in 2007 in response to the global financial crisis, had expired in February 2010.

Christine Lagarde, managing director of the International Monetary Fund, applauded the upcoming currency swaps, telling CNBC that the action "shows they will do what it takes to maintain stability in the financial system." John Ryding, a former economist for the Bank of England, also applauded next month's launch as a sign that Europe's finances were finally being brought under control. "They could open up the swap lines tomorrow if they wanted to," Ryder [told](#) CNN. "By starting in almost a month's time, it looks like there's no clear present danger."

The markets responded with ovations as well, with European bank stocks and American stocks generally being buoyed in the wake of the announcement. Wrote one analyst of the Fed's participation in the latest action, "Given how weak the U.S. economy is right now, we think the Fed is cognizant of the spillover risks from a European banking crisis. Providing dollar funding appears to be a low cost option."

As usual, the latest liquidity legerdemain from the Federal Reserve has elicited short-term effusions of optimism — surely this time, Bernanke and company will get it right! But currency swaps are just more smoke and mirrors designed to stave off — yet again — the inevitable collapse of Western economies drowning in debt and addicted to easy money and credit. This time around, the Fed isn't "injecting liquidity" into domestic finance, but into European banks, with the ECB as an intermediary. While other banks will be able to offer the ECB some of their holdings in dollars, the Fed can simply print as many dollars as it pleases and dump them on gullible Europeans. The consequence, of course, will be further erosion of the dollar worldwide.

Since Bretton Woods in 1944, the United States has enjoyed the unexampled ability to print dollars at will and export them to the rest of the world. The result has been transgenerational inflation against a backdrop of boom and bust, with every economic crisis being an opportunity to turn on the printing presses. That the rest of the world has accepted this state of affairs for so long is perplexing, since it has allowed the United States to enrich itself at the expense of everybody else — or at least, everybody willing to accept American fiat currency (a currency unbacked by a precious commodity).

But America has paid a price, too, in the form of an Olympian national debt that now threatens to drive our country into bankruptcy. And in spite of the abysmal failure of every effort by the Fed and the U.S. government to stimulate the economy back to life, the Fed is going to embark yet again on a program of bailing out financial elites with taxpayer-backed dollars.

And what if the ECB and the entire EU falls apart as a result of the debt crisis (which cannot and will not be solved by printing money)? Italy and Spain are faltering, and Greece has all but been given permission to default. A Greek default would likely trigger defaults in Ireland and Portugal for starters, events which by themselves could cause the entire EU to unravel. What then will happen to all of those loaned dollars which the ECB has promised to repay?

The Federal Reserve, without so much as a congressional by-your-leave (let alone constitutional authority) has been playing Russian roulette with the American economy ever since the onset of the financial crisis, throwing bad money after bad and producing no outcome other than lengthening and deepening the crisis. Sooner or later, in an event economists like to call "capitulation," the global markets will tumble to the reality that no amount of debt and stimulus will cure our malaise; only the shock therapy that the free market provides will do that. When that realization finally dawns, currencies will collapse, stocks and bonds will implode, and debtors, including sovereign debtors, will default. The world that will rise from the ashes of that event will look very different from the world we live in now.

When that time of reckoning arrives, we may at least hope that the Federal Reserve will finally be abolished, and that Americans will understand clearly the monetary fraud that has been perpetrated on them. Until they do, the Federal Reserve will continue to print dollars for bailing out foreigners.