Punishing Thrift and Rewarding Risk

Mark Carney and the Bank of Canada responded to the US credit crisis by radically lowering interest rates as a way to stimulate Canadian borrowing and consumer spending. However, the bank made no allowances for those, mostly working people, who chose the conservative course of simply depositing their savings in a bank in the hope of earning a modest return.

Only recently has Finance Minister Flaherty moved to caution banks about what he called excessively low borrowing rates. These cautionary warnings, recently echoed by Bank Governor Carney, have not succeeded in discouraging Canadians from plunging deeper into debt and the world of market speculation. As Chris Sorenson wrote in the October 3, 2011, issue of *Maclean’s*, “Those who’ve opted to be austere with their personal finances have found themselves on the losing end as governments and central banks have worked to get people to borrow and spend.” In this atmosphere of low interest rates, “the dynamics of risk and reward have been [and continue to be] severely distorted.”

A novel way to describe the hit taken by savers is,

to measure the impact [by looking] at how much interest income is being lost as a result of low rates... with roughly $1.2 trillion on deposit at the banks and rates roughly three percentage points below their historical level, savers are losing out on $30 to $40 billion every year in interest income... this amounts to a massive subsidy for the country’s banks since the rate depositors are paid to part with their money is far less than what the banks can earn lending that money out... as mortgages... someone else is paying the price and it’s little old ladies and people on fixed incomes who can least afford it (ibid.).

Canadian bank “Bail-ins”

Apparently, though, Canadian taxpayers needn’t fear a future of US-style bank bailouts because the Harper government carefully buried what they call a “bank bail-in” plan in the latest federal budget. For undisclosed reasons the government has suddenly decided that it might be a good idea if Canadian banks took steps to protect themselves from market instability with their own money rather than depend on taxpayers like their US counterparts. The frightening aspect of this revelation is its late and sudden arrival on the scene and the implicit suggestion that such measures were previously absent from the calculations of both banks and government. Apparently this budget inclusion was a way of placating public fears about the government’s recent announcement that Canada’s major banks were “systemically important.” Worse, rather than directly legislated self-help
for banks, the Harper government, as columnist Kate Heartfield wrote in the April 6, 2013, Ottawa Citizen, “proposes that banks set aside rainy-day assets, which they would then use to shore themselves up if the worst happened.” I must ask, what will eventually happen if banks continue to avoid saving sufficient funds to weather inevitable rough patches?

Corporate pundits like Heartfield reflexively apply the term “conspiracy theory” to the thinking of anyone who dares voice dark suspicions about the intentions of Canada’s financial titans. For those who would lightly dismiss the idea that powerful interests actively conspire to marginalize the public, I offer the following remarks from dissident US writer Norman Finklestein:

Although the explanatory value of conspiracy theories is marginal, this does not mean that, in the real world, individuals and institutions don’t strategize and scheme... Indeed, [the accusation of] “conspiracy theory” has become barely more than a term of abuse to discredit a politically incorrect sequencing of facts...

Perhaps Heartfield might also benefit from reference to the widely quoted but mainly unread Adam Smith who said,

the people who own the society make policy. The people who own the place are the ‘merchants and manufacturers.’ They’re the ‘principal architects’ of policy, and they carry it out in their own interests, no matter how harmful the effects on the people of England [or in this case Canada]...

(Smith in Chomsky, 2013.)

As Chomsky explains, “Power is no longer in the hands of ‘merchants and manufacturers’ but of financial institutions and multinationals. The result is the same.” Am I a “conspiracy theorist” if I speculate about the possible implications of the fact that Post Media, the Ottawa Citizen’s parent company, is owned in part by the Royal Bank of Canada?

Canadian Banks’ Façade of Respectability and Stability

Rather than detail the minor suffering of Bay Street and the financial sector, I will present a few representative examples of the harm caused by their irresponsible conduct. According to Bruce Livesey (2012) in Thieves of Bay Street:

Canada’s financial industry is a behemoth, a titan that generally escapes scrutiny, employs armies of lobbyists, lawyers and advertising mercenaries to do its bidding, and, with rare exceptions, benefits from a media that doesn’t examine its structural failures. It has acquired a strutting arrogance as a result of having weathered the credit crisis better than its American counterpart, but what gets overlooked – as the industry bamboozles the public about its virtues – are the people it runs over in the dead of night.

While Canadian banks are not exactly Ponzi schemes, some parallels exist, as Livesey writes,

no bank has enough money in reserve to meet the demands of depositors if too many of them suddenly withdrew their savings or investments. For every $20 a typical bank lends out or invests, it has about $1 in cash reserves. A loss of 5 percent of asset value is all it would take to sink a Canadian bank.

While this seems a frightening prospect, banks are secure in the knowledge that they are underwritten by the Canadian taxpayer through the Bank of Canada, although individual depositors enjoy only minimal protection. While this is bad enough, according to economist Benoit Desrochers of Desjardins Financial, “The equivalent ratio among U.S. banks is over 25, while that of European banks is approximately 30, and the ratio of the largest banks in the world is over 40.” Such comparisons by institutions like Desjardins influence the public to look favorably upon Canadian banks.
How much is enough? RBC's Record Profits and Foreign Workers

Apparently, RBC is either having difficulties finding enough Canadian employees to fill the ranks of its burgeoning part-time, benefit-free workforce, or it prefers to outsource jobs to even lower-wage foreign nationals. The CBC reported that back in November 2012, the bank is laying off 45 employees in its RBC Investor Services division in Toronto and training foreign workers hired through IT outsourcing firm iGATE Corp. to take over some of those jobs in Canada while the majority of the roles will eventually be transferred abroad (Financial Post: April 8, 2013).

In response, “The Royal Bank of Canada denied reports that it has hired temporary foreign workers to take over its own employees’ job functions,” adding that it “does work with ‘external suppliers’ to provide certain services both in Canada and globally” (ibid.). RBC does admit to using outside companies to improve “operational efficiencies,” and according to an RBC statement in the April 8, 2013, Ottawa Citizen, “those who will take on the work are going to be the supplier’s employees.” Is it really necessary to highlight the fact that those 45 Torontonian employees will lose their jobs not to official RBC employees but to private contractors?

Considering the fact that RBC enjoyed a 2012 annual profit of $7.5 billion in net earnings, up from $6.44 billion in 2011, I must ask: how much is enough profit, and will they ever be satisfied? How does one comprehend the chilling ruthlessness behind firing 45 people just to “improve operational efficiencies”?

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Examples of Canadian Bank Misconduct in the Developing World

Offshore misbehavior by Canadian banks is nothing new. As Todd Gordon writes in Imperialist Canada, “Canadian banks such as Scotia and Royal (RBC) have a long history of imperialist practice…as one Scotiabank executive remarked a decade ago, ‘We stopped screwing Canadians. Now we’re screwing foreigners’.”

Scotiabank in Argentina

The fall of 2001 saw Argentina plummet into “one of the worst economic meltdowns of the global neoliberal era” (ibid.). Especially troubling to neoliberal ideologues was the fact that Argentina had become the poster child for, “the benefits of the tough economic medicine of IMF-imposed aggressive restructuring and market liberalization” (ibid.). After the Argentine government forbade foreign banks operating in that country from seizing the assets of debtors, “the value of Scotiabank’s assets dropped by $1 billion” (ibid.). and the bank adopted a strategy designed to “exploit the financial chaos and hardships Argentinians were enduring” (ibid.). The bank was accused of attempting to move money out of the country and Canadian Prime Minister Paul Martin applied pressure to his Argentine IMF counterpart to treat Scotiabank with greater gentility. Eventually, Scotiabank was charged in an Argentine court with legal disobedience after refusing a court order to release funds for its employees and depositor pensioners. It also refused back pay to 1800 Argentine employees and would not disburse the US$35 million in severance to which they were entitled. In spite of Scotiabank’s public protestations, “execu-
tive Peter Godsoe noted that the losses associated with Quilmes will have no material impact on the health of the bank” (ibid.). Nonetheless, Scotiabank went on to sue the Argentine government for over $600 million.

**RBC Ventures in the Middle East**

While Canada has not admitted its military role in the early phase of the 2003 U.S. invasion and occupation of Iraq, “RBC was recruited to act as a conduit to Canadian business” (ibid.). “In the fall of 2003, RBC joined a consortium of fourteen major international companies, headed by the American bank J.P. Morgan Chase and Co.” (ibid.). This group was delighted by the U.S. invasion because it brought excellent private sector opportunities in a nation where state agencies had dominated the economy. In spite of political repression and secret police brutality, Iraq under Saddam Hussein had been the most advanced and stable of the Arab states.

Fortunately for RBC, its investments were risk-free since its venture was 100% underwritten by funds from the American-controlled Development Fund for Iraq which is financed by Iraqi oil exports. “In other words, the Iraqi people – severely impoverished, malnourished and insecure as a result of the invasion and occupation – are guaranteeing the financial security of the wealthy Canadian multinationals’ investment” (ibid.). Beyond this, RBC’s Iraqi venture was further backstopped with Canadian tax dollars by Export Development Canada. The only Iraqis who stood to benefit from RBC’s presence were the tiny elite with pre-existing links to Western business. Increasingly, private profit is being facilitated by public risk in a world of harsh free market discipline for working people and generous socialism for corporations.

**An Example of Canadian Banking Malfeasance: Canadian Imperial Bank of Canada’s (CIBC) Adventures in Asset-backed Commercial Paper (ABCP)**

By 2008 Canadian banks, including CIBC, had lost close to $12 billion, “in bad subprime mortgage debt.” Most of the suffering was felt by small investors who were horrified to hear that “CIBC disclose[d] for the first time that it was on the hook for U.S. subprime residential mortgages amounting to US $12 billion and facing a meltdown” (Livesey, 2012).

Nevertheless, CIBC president Gerry McCaughey minimized the problems in spite of the bank’s inability to cover the losses. A sixty-five page report was written by Dr. Gordon Richardson of the University of Toronto’s Rotman School of Management, which concluded that the bank, failed to comply with Generally Accepted Accounting Principles (GAPP) disclosure requirements... and the information provided pertaining to credit risk was...wholly misleading to the market in general and to class members who invested in CIBC (ibid.).

By the end of 2008, the total market value of CIBC’s shares plummeted to $20 billion from $36 billion. Nevertheless, CIBC executives continued to be the highest paid in the banking industry.

With the exception of TD Canada Trust, every major Canadian bank and a number of large European lenders dove into the toxicity of ABCPs and, eventually, mostly small investors bought “$5.8 billion worth of this toxic product in their money market funds and brokerage accounts” (ibid.). At least 1,800 of these small investors lost everything when the market tanked,
and it was revealed that “the Canadian banking industry had been eager to encourage investors to buy products the bankers themselves knew to be unsafe, and then they threw those clients under the bus when it all went south” (ibid.). To make matters worse, these abuses occurred in Canada’s supposed regulated and reputable financial sector.

Hopeful Developments in Economics

Hopeful developments in economics may create a saner investment climate that acknowledges the delicate reality of the biosphere and the dangers of the unrestricted growth model that currently dominates elite business thinking. The social science of economics is currently facing a revolutionary transformation that is being stubbornly resisted by the academic establishment of most European and North American universities. As Robert Heilbroner said, “Before economics can progress, it must abandon its suicidal formalism.” He was referring to classical economics’ obsession with abstruse mathematical formulas that have little to do with reality but seek to squeeze the round world into its square holes. This dependence on mathematics legitimates the dominant version of economics and to a certain extent protects it from criticism. Financial journalist and Oxford University PhD. candidate Simon Mac offers a number of suggestions to modernize economics and alter it to serve the needs of real people:

1. Introduce far more historical analysis to the undergraduate curriculum.

Two notable examples of plain-spoken economists are John Maynard Keynes and John Kenneth Galbraith who both endured their colleagues’ wrath for daring to transcend the needlessly-complex jargon of a social science masquerading as an empirical discipline.

Fate of Revolutionary Economists

According to Adbusters contributor Patricia Cohen of the New York Times, economists who have challenged free market theory have been the Rodney Dangerfields of the profession. Often ignored or belittled because they questioned the orthodoxy, they say they have been shut out of many economics departments and the most prestigious economics journals. They get no respect.

Mathematical models and anti-regulation sentiment still dominate most economic departments, although the credit crisis has generated some fresh thinking on economics, including
behavioral economics and the acknowledgement that environmental and social costs must be included in calculations of the Gross Domestic Product. Unfortunately, economists like the pro-stimulus John Maynard Keynes and Hyman Minsky, who predicted the ruinous effects of risky financial speculation, are excluded from graduate level courses. Randall Wray, an economist at the University of Missouri, calls the mathematical model “the frontier of nonsense,” and states that, “A real shift in economics will come only if there is a wholesale collapse.” Since government insists on seeking guidance from the authors of chaos, perhaps that wholesale collapse may yet occur.

The Occupy Movement’s Perspective on the Market Meltdown

While the Occupiers in Canada and the US may not form the next government, their open and consultative organizational style offered us a useful lesson in genuine participatory democracy, sometimes called anarcho-syndicalism. Most detractors condemned the Occupiers’ ostensible failure to provide ‘solutions’ and fault them for rejecting the formal mechanisms of governance.

In order to challenge financial or any other form of tyranny it is necessary to recognize that, “It’s costly to oppose power…it’s going to carry a personal cost. Power systems, whatever they are, very rarely abdicate their power cheerfully” (Chomsky, 2013). Therefore, a long term commitment to facing and managing fear is vital to any form of activism involving powerful organizations and collusive governments that are quite prepared to use and abuse power to defend their interests. “So fear is understandable. Nowadays its being enhanced by pretty severe attacks on basic civil liberties. A system of control and repression is in place” (ibid.). Progress against such vast power is necessarily slow but when publications like the Financial Times begin advocating for a tax on day trades it becomes apparent that positive change is possible.

The American Occupiers and their Adbuster advocates are the first ripple of a coming wave of social activism dedicated not to stealing money from ‘successful’ people but to ending corporate domination of the political process by “a demand that Obama ordain a Presidential Commission tasked with ending the influence money has over our representatives in Washington” (ibid.). As previously mentioned, Obama’s recent choice of major campaign fundraiser Bruce Heyman of Goldman Sachs as ambassador to Canada indicates that the US political system will be lubricated with corporate cash for the foreseeable future. The Canadian situation differs only in magnitude and the subtlety of the nation’s regime of campaign finance. Effective and permanent solutions to Canada’s fiscal challenges will
never emerge from the councils of those who stand to benefit from financial and social chaos.

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