German Bankers Bail But on a Sinking Ship

by Rainer Apel

Late on the night of Dec. 12, an emergency session of top German bankers and banking regulators came to an agreement that allows Sachsen LB, the troubled bank of the German state of Saxony, to escape instant default. The agreement foresees an extra state guarantee by the government of Saxony in the range of 2.75 billion euros ($3.97 billion), plus another 1.5 billion euros provided by the association of German savings banks and by the Bundesbank, the central bank of Germany. The agreement is the precondition for LBBW, the state bank of Baden-Württemberg, to realize its promise of late August, to take over Sachsen LB, which at that time was the second big victim in Germany's banking sector, after Industriebank (IKB), in the fallout from the acute U.S. subprime crisis that broke out in July.

At the end of August, LBBW had paid 250 million euros for the Saxon bank, which was threatened with default, because at least two of its "conduits" in Dublin, Ireland, had run foul over leveraged mortgages in the U.S.A., in the range of more than 22 billion euros. Banking insiders spoke of a 35-billion-euro-plus Sachsen LB mortgage bubble. These figures were denied by the Saxon bankers at the time, but were corroborated by a survey pointing to uncovered speculative paper involving 43 billion euros, which LBBW admitted after press leaks, on Dec. 9.

LBBW insisted that the only thing that would prevent it from pulling out of the takeover deal would be a Saxony state government guarantee to cover at least 10% of that bubble, which amounts to 4.3 billion euros. Saxony protested, pointing out that 4.3 billion euros would be 25% of the entire state budget for one fiscal year, and charging the Baden-Württembergers with blackmail. A fierce struggle ensued, threatening a pullout of LBBW and the prospect of a Sachsen LB default.

On Dec. 11, Jochen Sanio, head of the German banking regulatory office, Bafin, warned both sides to reach an agreement by Dec. 16, or he would shut down Sachsen LB on Dec. 17, with all the chain-reaction consequences that would imply. That ultimatum triggered a new round of hectic talks to find a "solution."

Although the threatened immediate shutdown has now been averted—for the time being—the new agreement is far from being any solution. It triples the per-capita debt burden of the citizens of Saxony, and it forces Saxony to bend its constitution, which has a ceiling of 1.75 billion euros on state banking guarantees. (The new agreement is 1 billion more than that.) The Saxony constitution previously was suspended for two days in late August, to circumvent an inconvenient parliamentary debate, and instead finalize the sale of Sachsen LB to LBBW, with a downpayment of 250 million euros.

Furthermore, the question of what to do with the bubble of 43 billion, remains as unresolved as the larger problem of what to do with the global bubble. Officially, LBBW has committed itself not to continue the conduit business, which has driven Sachsen LB into the abyss, but instead to return to "solid" project financing. However, LBBW itself has suffered admitted losses of 800 million euros in the third quarter of 2007, from engagements on the U.S. leveraged mortgage loan market. The announcement of those losses at the end of November torpedoed a potential merger of LBBW with the state bank of Bavaria, which was under discussion by both banks.

Opting out of the mortgage bubble will not do any good, as long as the banks stay tied to the speculative bubble as a whole. This is like someone who believes he is safe in his solid armchair, sitting on a sinking ship. The point that Lyndon LaRouche has made, that there is no solution without a profound policy change that eliminates the speculative aspects of the global financial system and restores a productive-credit system of banking, is proven once again by the disaster that has broken out in Saxony. Although a Sachsen LB default may have been averted for the moment, the just-signed emergency agreement will leave the new owner of the Saxony state bank, LBBW, unprotected against the next round of heavy market turbulence—which could come within weeks, or sooner. Who will bail out LBBW, then? And as the global financial collapse crisis keeps accelerating, who will bail out the bank that bails out LBBW?

Zepp-LaRouche: Defend the Common Good

The LaRouche movement in Germany, especially the LaRouche Youth Movement (LYM), has intervened repeatedly in Saxony, with a statement by Helga Zepp-LaRouche, the national chairwoman of the Civil Rights Solidarity Movement (BüSo), which calls for a defense of the Common Good and for LaRouche's new banking policy and a New Bretton Woods financial-monetary system. The LYM also brought the statement to the middle of the banking district in Frankfurt, Germany's "financial capital," on Dec. 13.

The BüSo will continue the campaign for the Common Good throughout the state of Hesse, including among bank employees, many of whom see their jobs threatened by the monetarist banking collapse, and are more open to LaRouche's proposal for a "bank protection act," as part of a state intervention to rescue the banks from the claws of "raptor capitalists," like hedge funds, and transform them into agencies that finance infrastructure and other projects that promote the Common Good.