THE IRISH DEBT CRISIS: TIME TO THINK OUTSIDE THE BOX

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The Public Banking Forum in Ireland
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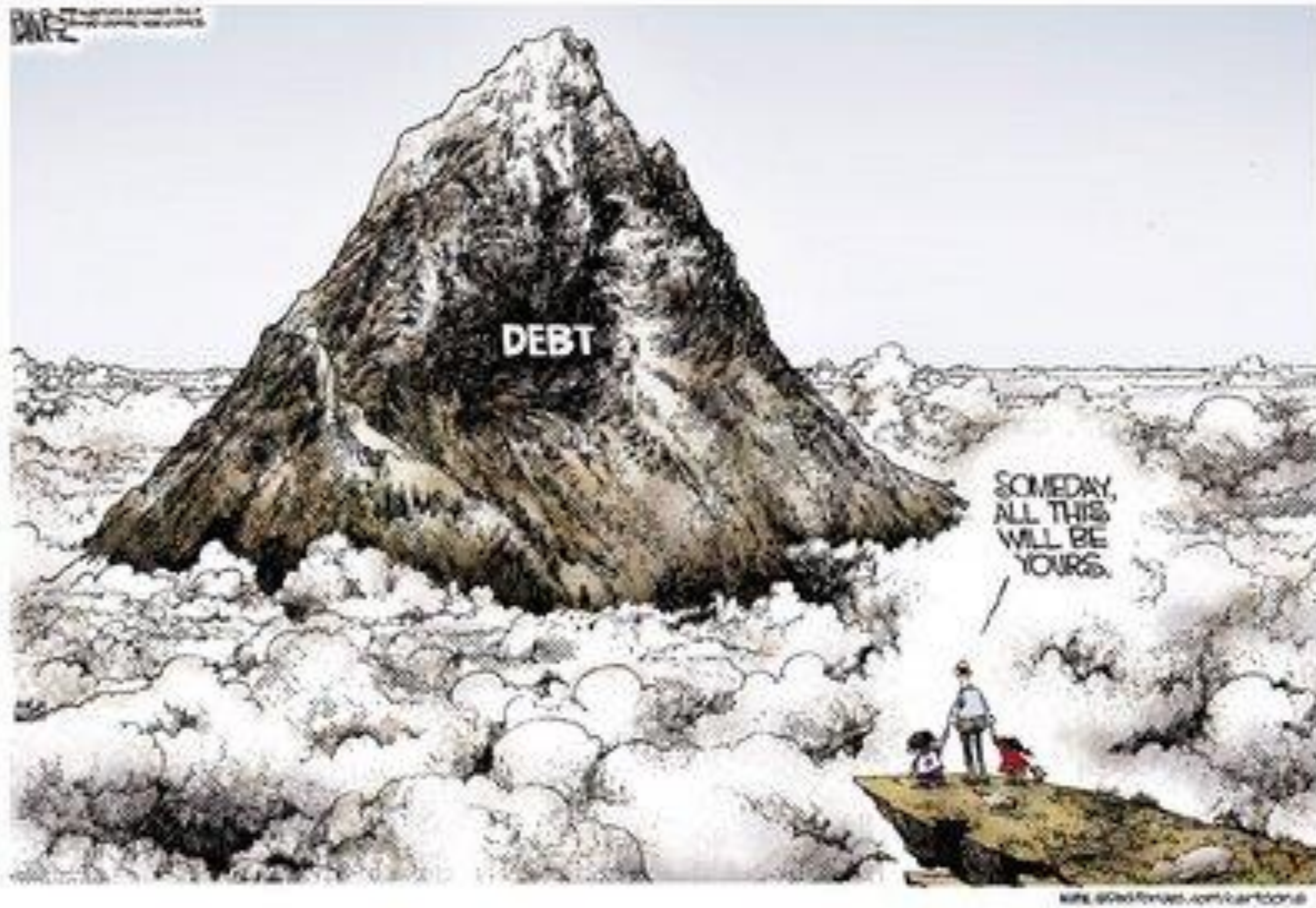
Ireland is facing an insurmountable mountain of debt.



The Irish Debt Bomb

- General government debt in 2012: €192.5 billion
- Debt to GDP: 117.4%
- Government income (2010): €40 billion
- Government expenditures: €64 billion
- Deficit: €24 billion, 15% of GDP
- Balance of Trade: €40 billion positive (mostly food exports)—national profits the country could enjoy if it were free of debt or owed the debt to its own bank.

The EU's prescribed medicine is cutbacks and austerity.

Requirements of ESM and Fiscal Treaty

- Deficit must come down to 3% of GDP
- Cuts of €4 billion/year until this achieved (nearly what Ireland spends yearly on schools)
- Ireland must contribute €11 billion to ESM fund – which means additional borrowing – and this contribution amount can be increased at any time.
- If requirements aren't met, ECB can dictate details of the national budget. All national assets can be sold off to pay debts (forests, water, hospitals, highways...)
- But the austerity pill isn't working. It has just created ever-increasing debt, unemployment, and loss of assets.

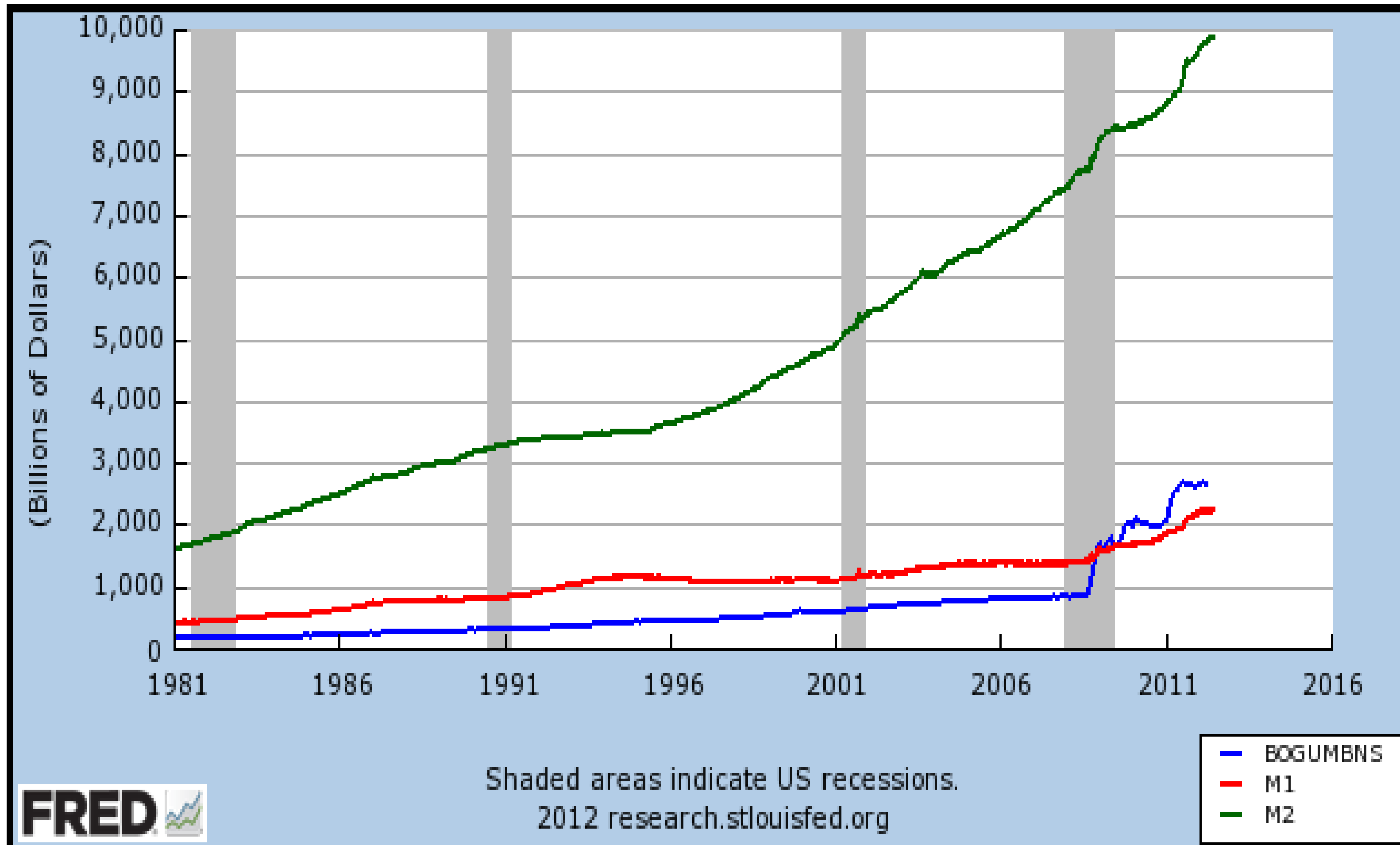
Why isn't it working? Because the diagnosis is wrong. The whole Eurozone is in debt! How can that be? Who are they in debt to?

To understand that, we need to understand where money comes from.

To understand that, we first need to understand where money comes from.

Most people think it is issued by governments.

But governments or their central banks issue only coins and notes, which make up only a small part of the money supply.



Where does the rest come from? It is created by banks. So say many authorities.

"I am afraid the ordinary citizen will not like to be told that the banks can, and do, create and destroy money. The amount of money in existence varies only with the action of the banks in increasing or decreasing deposits and bank purchases. We know how this is effected. Every loan, overdraft or bank purchase creates a deposit, and every repayment of a loan, overdraft or bank sale destroys a deposit."

– The Right Honorable Reginald McKenna, former British Chancellor of the Exchequer, 1924

"[W]hen a bank makes a loan, it simply adds to the borrower's deposit account in the bank by the amount of the loan. *The money is not taken from anyone else's deposit*; *it was not previously paid in to the bank by anyone. It's new money, created by the bank for the use of the borrower*."

-- U.S. Treasury Secretary Robert B. Anderson, 1959

How? By double-entry bookkeeping. The bank “monetizes” your promise to pay, turning it into a "spendable IOU."

$500,000 Home Loan

Bank Ledger

Liabilities	**Assets**
Customer Account $500,000	Customer’s Home Mortgage – $500,000

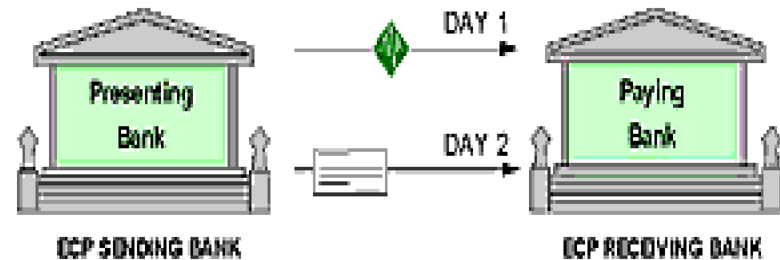
Net result: 0.

The shell game of check-clearing

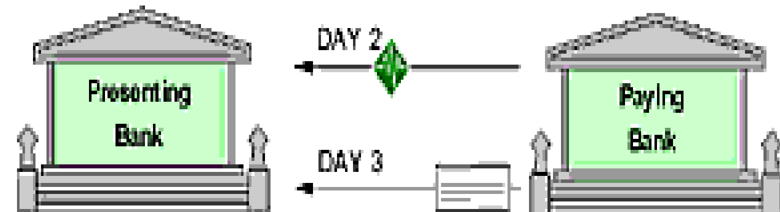
- Checks fly back and forth all day. The balance is cleared at the central bank with an overdraft in the bank's reserve account.
- The bank then borrows to clear the deficit. Banks can borrow very cheaply from each other.
- The bank, in effect, can borrow back the money it just created.

Late Evening Exchange

ECP Forward



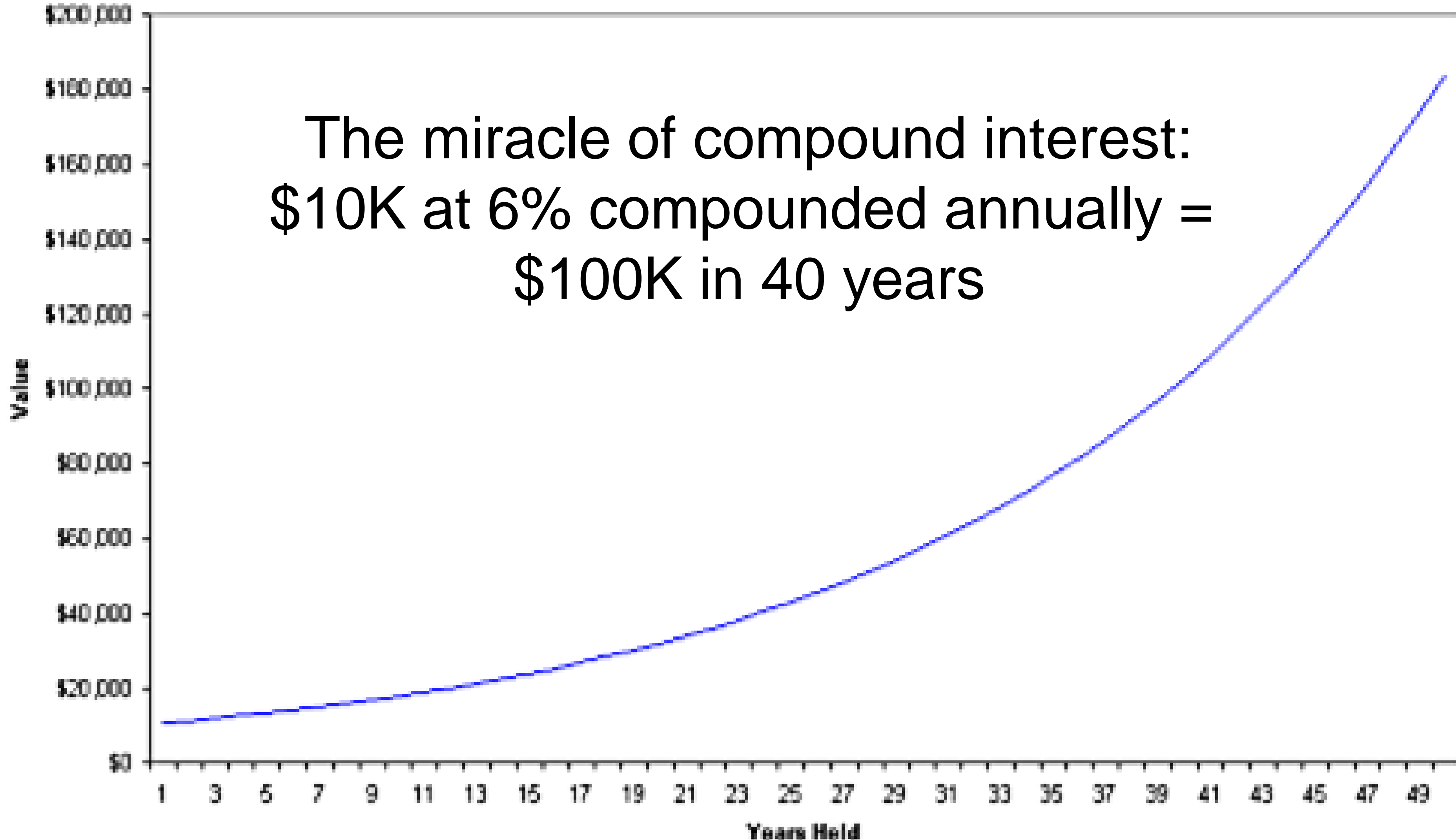
ECP Return



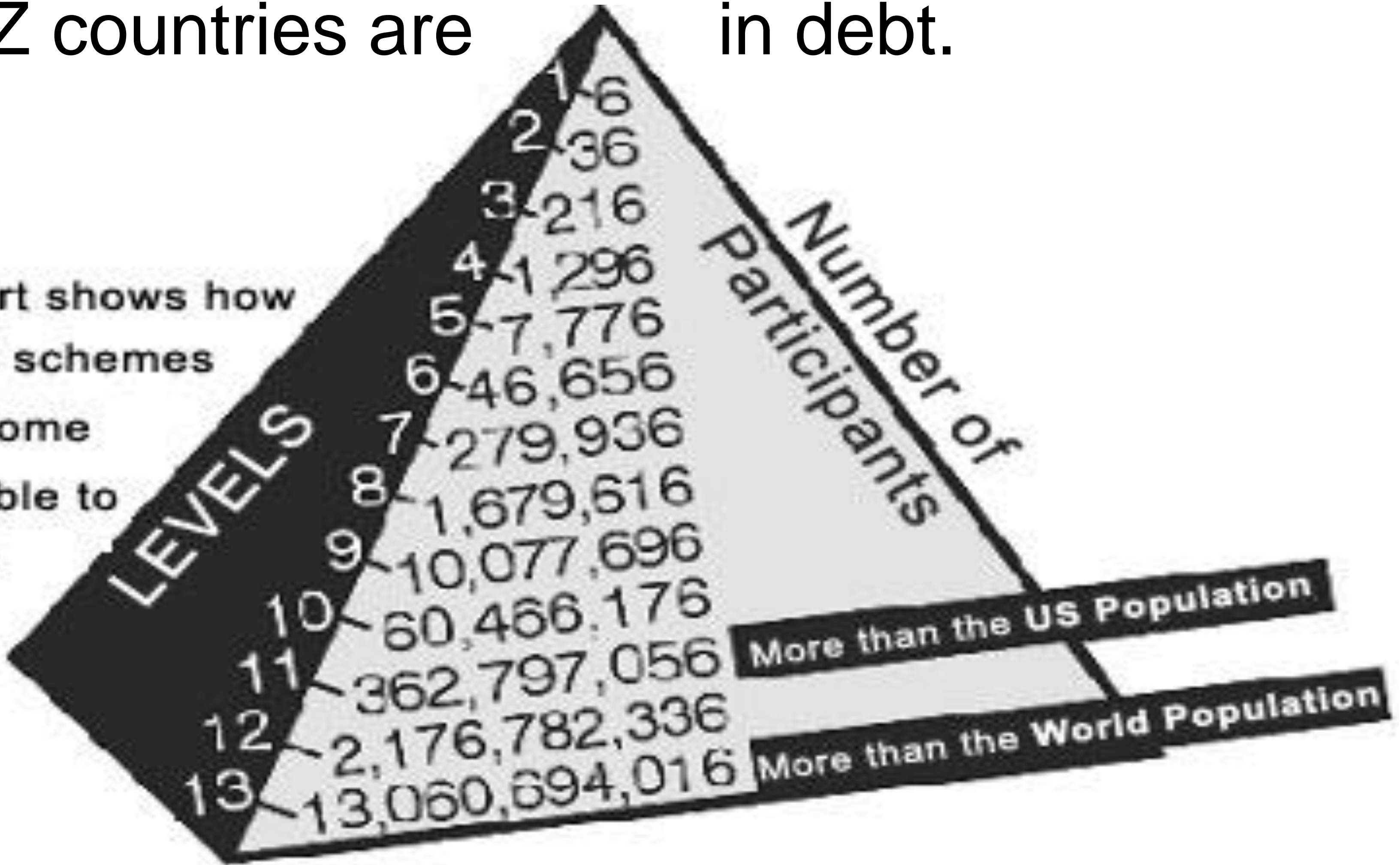
Most of our money consists merely of "bank credit.” The true function of the bank is to:

- Determine the creditworthiness of the borrower, and
- Turn the borrower’s promise to pay into a spendable IOU.

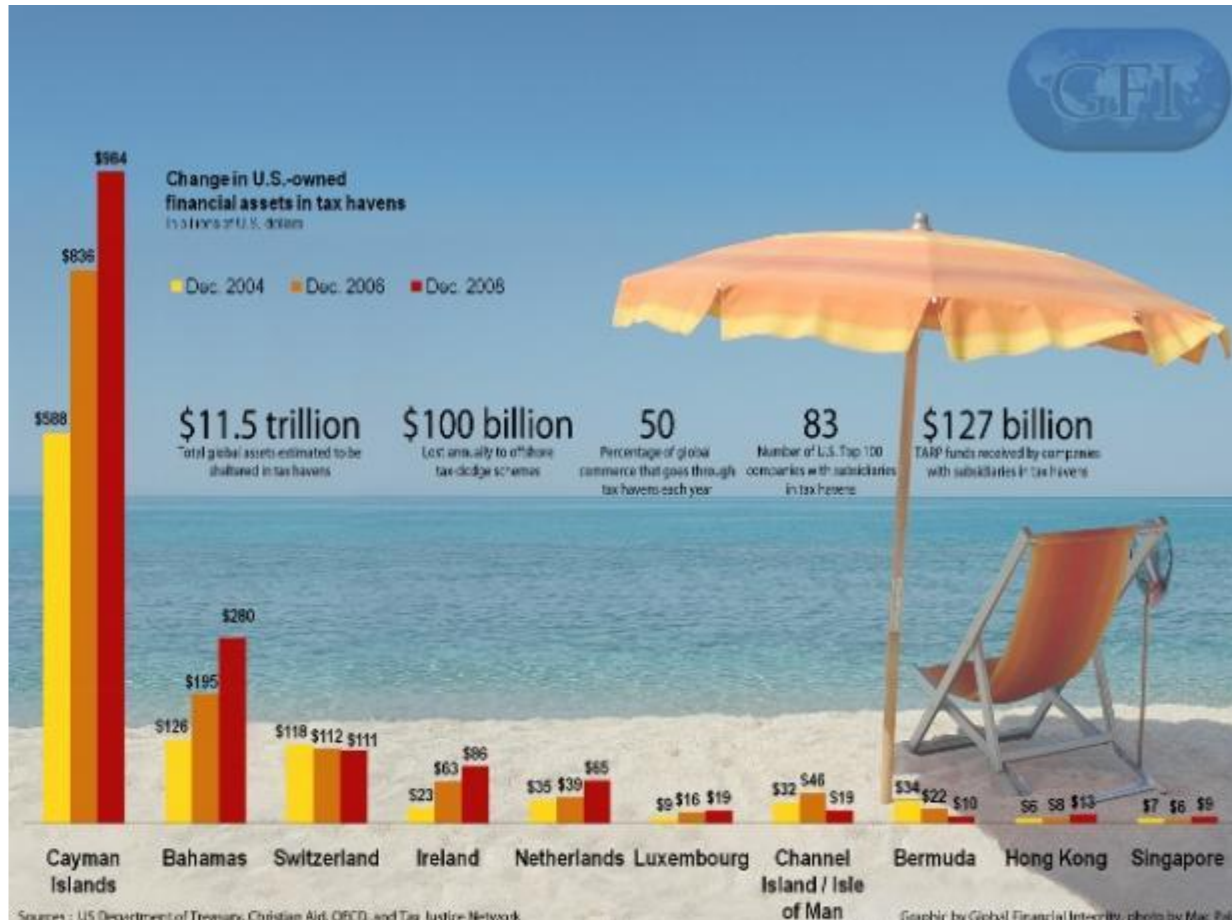
For this service, the bank charges interest.



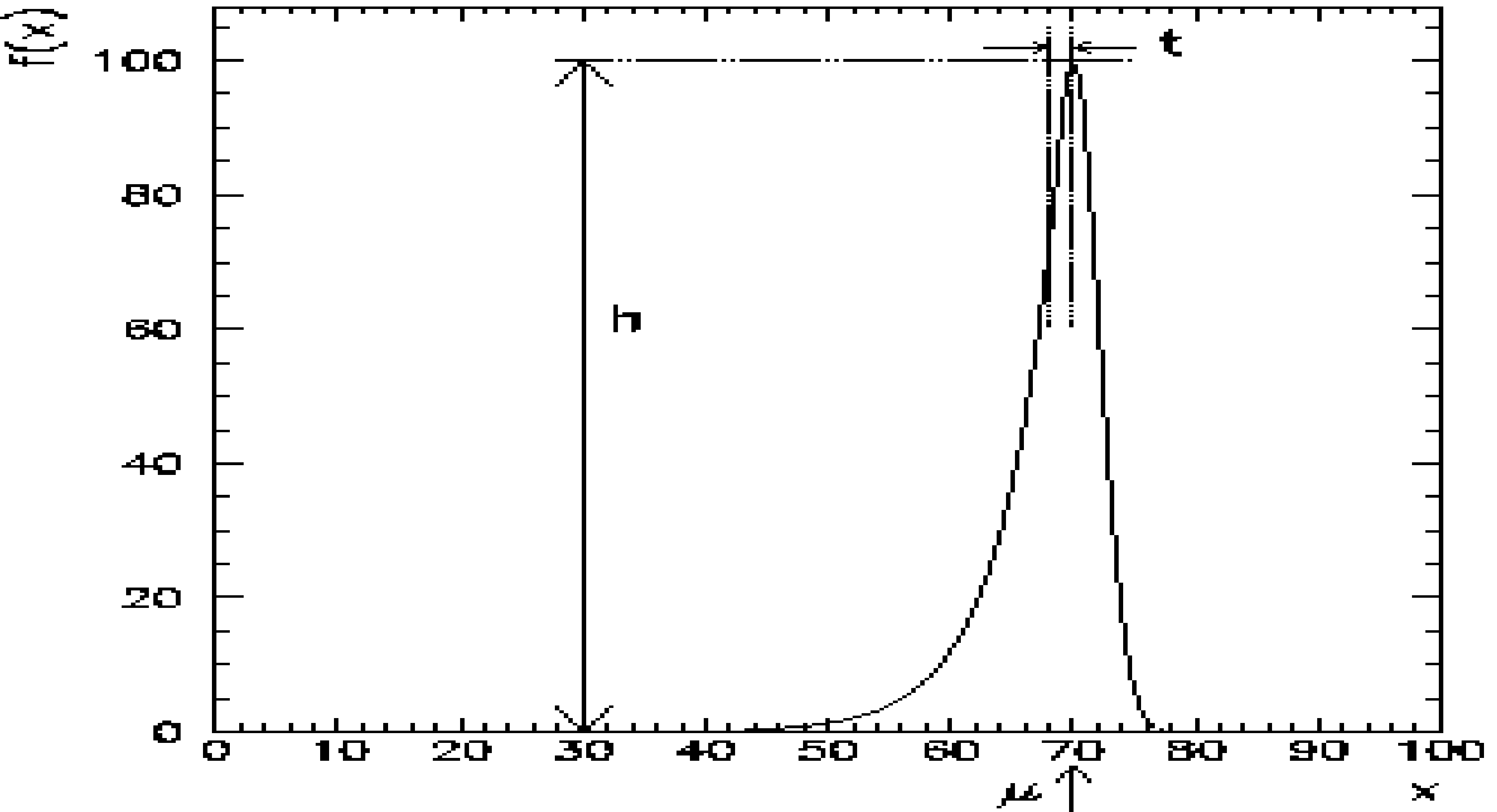
Where does the interest come from? Banks create the principal but not the interest, which can only come from more debt. And that's why all EZ countries are in debt.



Where does the interest go? $21-$32 trillion (€15-24 trillion) are now in offshore tax havens.



The pyramid scheme works until the system runs out of borrowers. And that's where we are today.



Governments have been strong-armed into bailing out the banks, but this has only fed the problem.

- Hurwitt '08

Bailouts worked to save the banks, but 5 years into a stagnant recession, governments and taxpayers are saying "no more." Where will the money come from next time?

The EU/BIS/big-bank solution: the "bail in," first seen in Cyprus. Banks are to confiscate the funds of creditors – including depositors.

Cyprus was just the beginning. The bail-in protocol was established by the Financial Stability Board in Basel in 2011. The G20 agreed to be regulated by the FSB in 2009.

Can they do that? Isn't it our money?

- No. Once your money is deposited, the bank owns it.
- You own an IOU.
- Banks are no longer a safe place to keep our money, public or private.

The root of the problem: not enough money to go around

- Insufficient money is created by banks as loans to pay back principal plus interest.
- Insufficient money is paid as wages and incomes to pay costs plus profits.
- The difference must be made up by borrowing.
- Bankers like it that way. Debt is their business, and they control the tap.

The solution: there is another way to design a money system. Two competing systems have vied for dominance for thousands of years.

- Money created privately by moneylenders or banks
- Money created publicly by communities or governments

The public model was proved in colonial Pennsylvania.

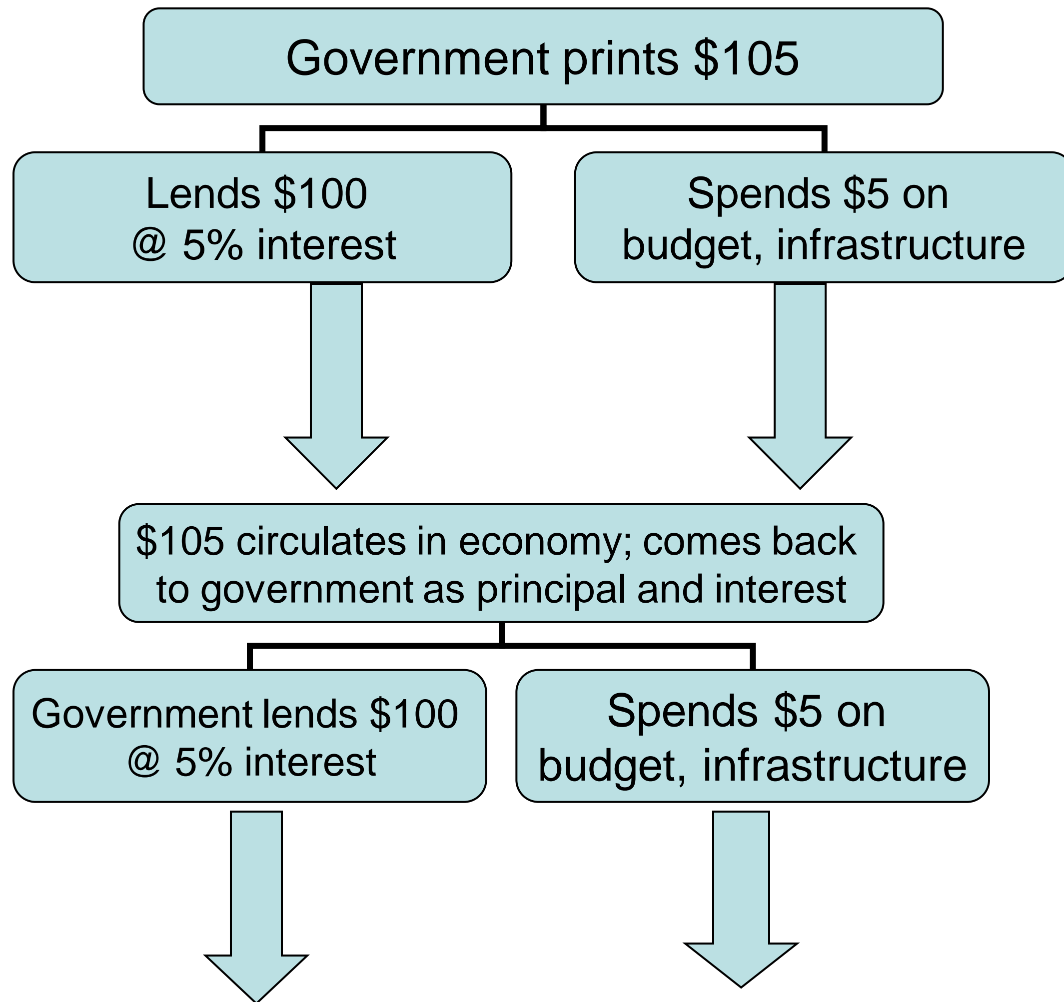
- Bills of credit were issued by the Philadelphia land bank and LENT to the farmers.
- Additional bills were issued and SPENT into the economy.

Led by William Penn, the Quakers sought religious freedom in the New World.

It all came back as principal and interest.

The result:

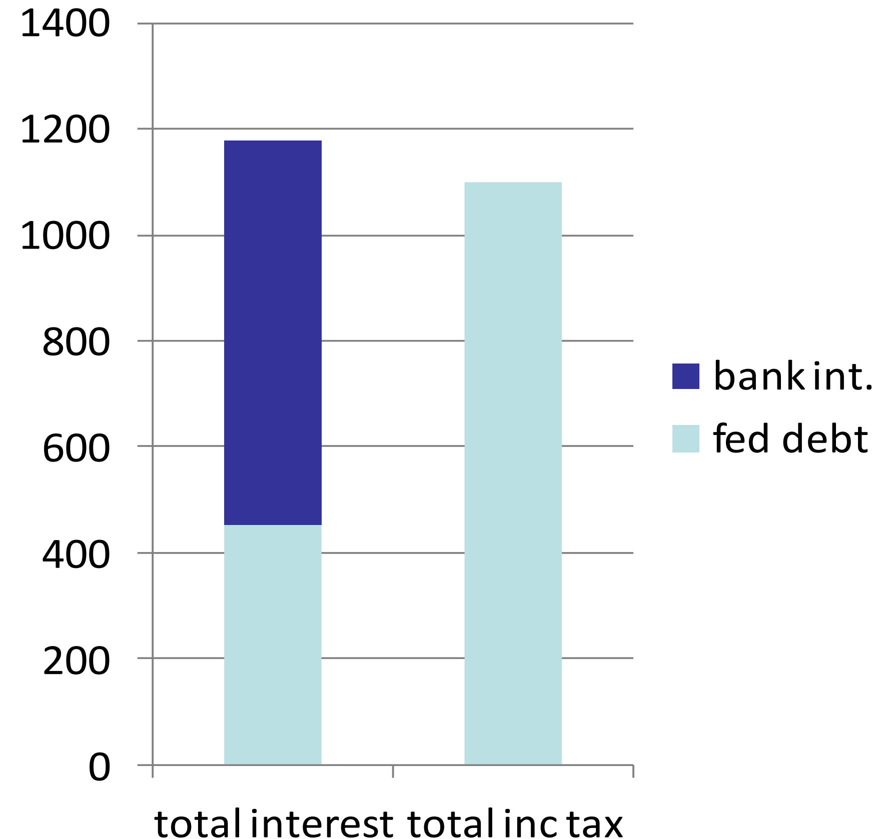
- No taxes
- No price inflation
- No government debt!



Could that work today? Yes!

Consider the U.S. figures for 2011:

- Total U.S. personal income taxes paid: $1,100 billion.
- Interest collected by U.S. banks: $725 billion.
- Interest paid on the federal debt: $454 billion.
- $725 + $454 = $1,179 billion.



The Bank of England circa 1740

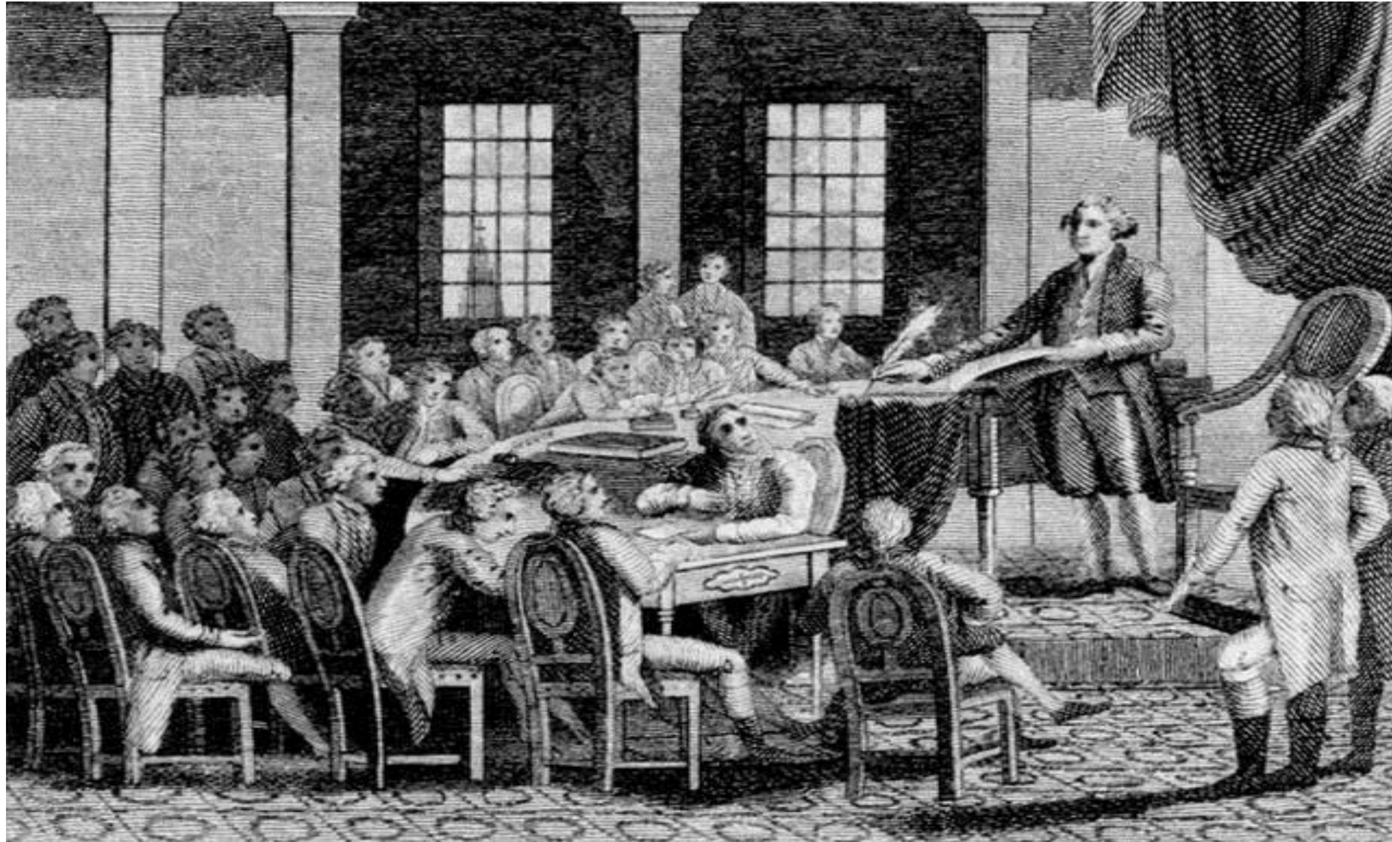
Unfortunately, the colonial scrip competed with the banker-issued money of the Bank of England, which leaned on the King to forbid it.

The Bank of England was founded in 1694, when William III needed money to fund a war. The bank issued banknotes and lent them to the government. Only the interest had to be paid. In effect, the national currency was RENTED from private bankers. The Bank controlled the money tap.

The Bank of England created money out of nothing just as the colonists were doing, but they did it by sleight of hand. The Bank issued many more notes than it had gold to back them—called “fractional reserve” lending. The unbacked notes were essentially counterfeit.

When King George forbade new issues of scrip in all the colonies, the result was depression and the American Revolution.

The colonists won the Revolution but lost the power to issue their own money. Private banks issued banknotes at interest on the fractional reserve model.



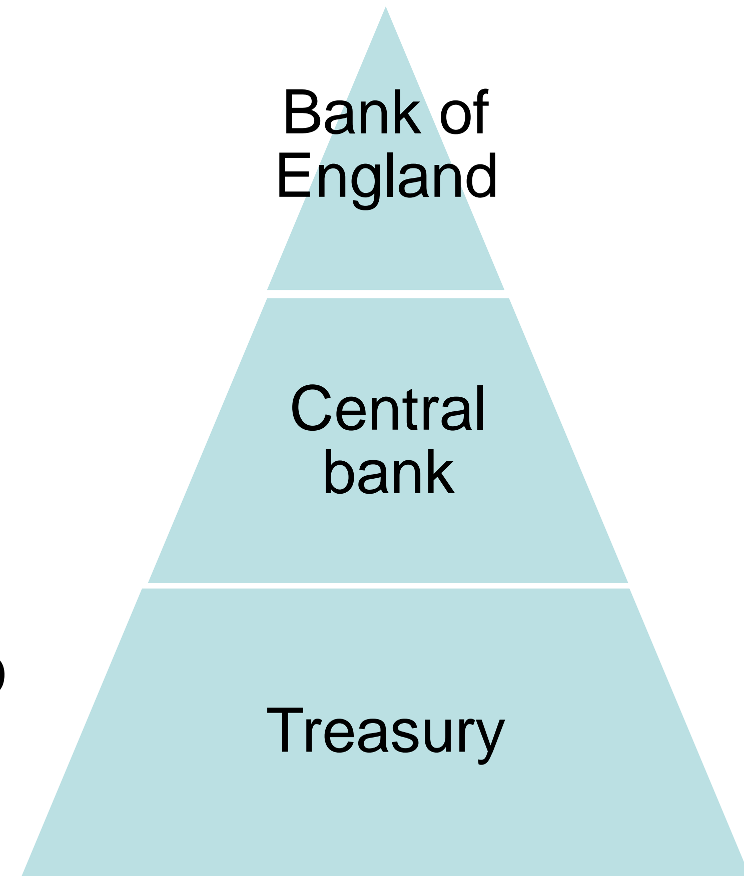
The Federal Reserve was instituted in 1913, patterned after the Bank of England. But public banking was successfully pursued in other ex-British colonies – Australia, New Zealand and Canada – until the Bank of England again suppressed it.

The Commonwealth Bank of Australia was wildly successful . . .

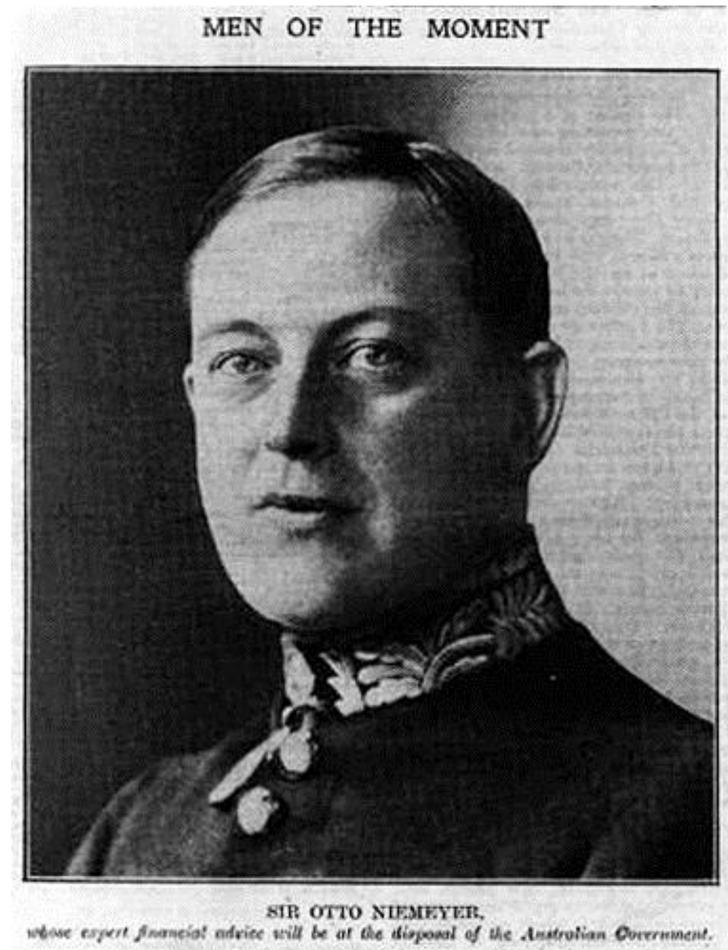
until Governor Denison Miller made the mistake of touting its virtues in London, killing the golden goose.

The birth of "central banking"

- The Bank of England devised a new plan for taking back control of the money tap: it would arrange for a system of "central banks" to take over the power to issue national currencies.
- This money would be LENT to the government and people.
- The apex of the system would be the Bank of England.

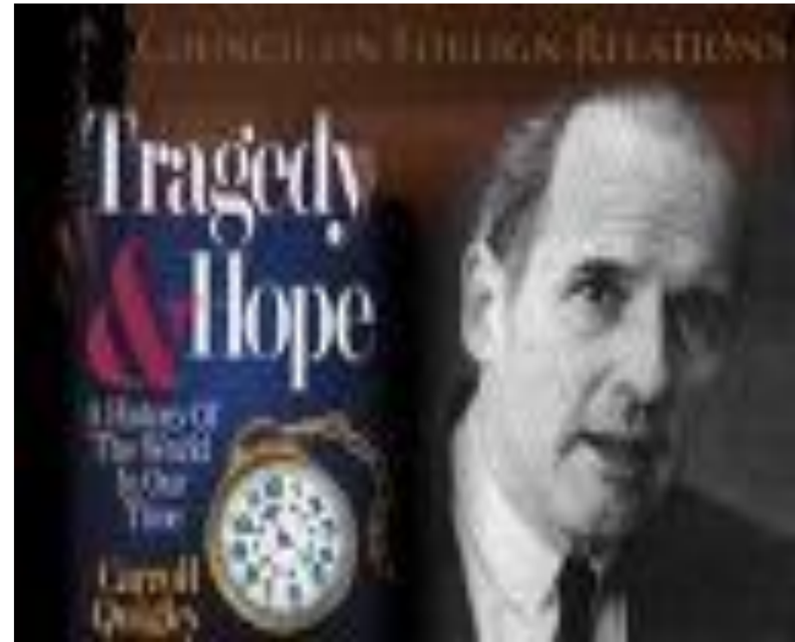


- The BOE sent Sir Otto Niemeyer to advise Australia and New Zealand.
- In 1937, he became chairman of the Bank for International Settlements in Switzerland.
- The apex of the system moved to the BIS.



The BIS game plan was revealed in 1966 by Prof. Carroll Quigley of Georgetown Univ., who wrote in "Tragedy and Hope":

"The powers of financial capitalism had another far-reaching aim, nothing less than to create a world system of financial control in private hands able to dominate the political system of each country and the economy of the world as a whole. . . .



"The apex of the system was to be the Bank for International Settlements in Basel, Switzerland, a private bank owned and controlled by the world's central banks which were themselves private corporations. Each central bank . . . sought to dominate its government by its ability to control Treasury loans . . . ."

- That was the plan, but the Reserve Bank of New Zealand was taken over by a money reform party and used to issue "national credit."
- Again the experiment was hugely successful, until the BOE intervened: NZ was threatened with being cut off from trade with the Commonwealth if it did not cease these "unsound practices."

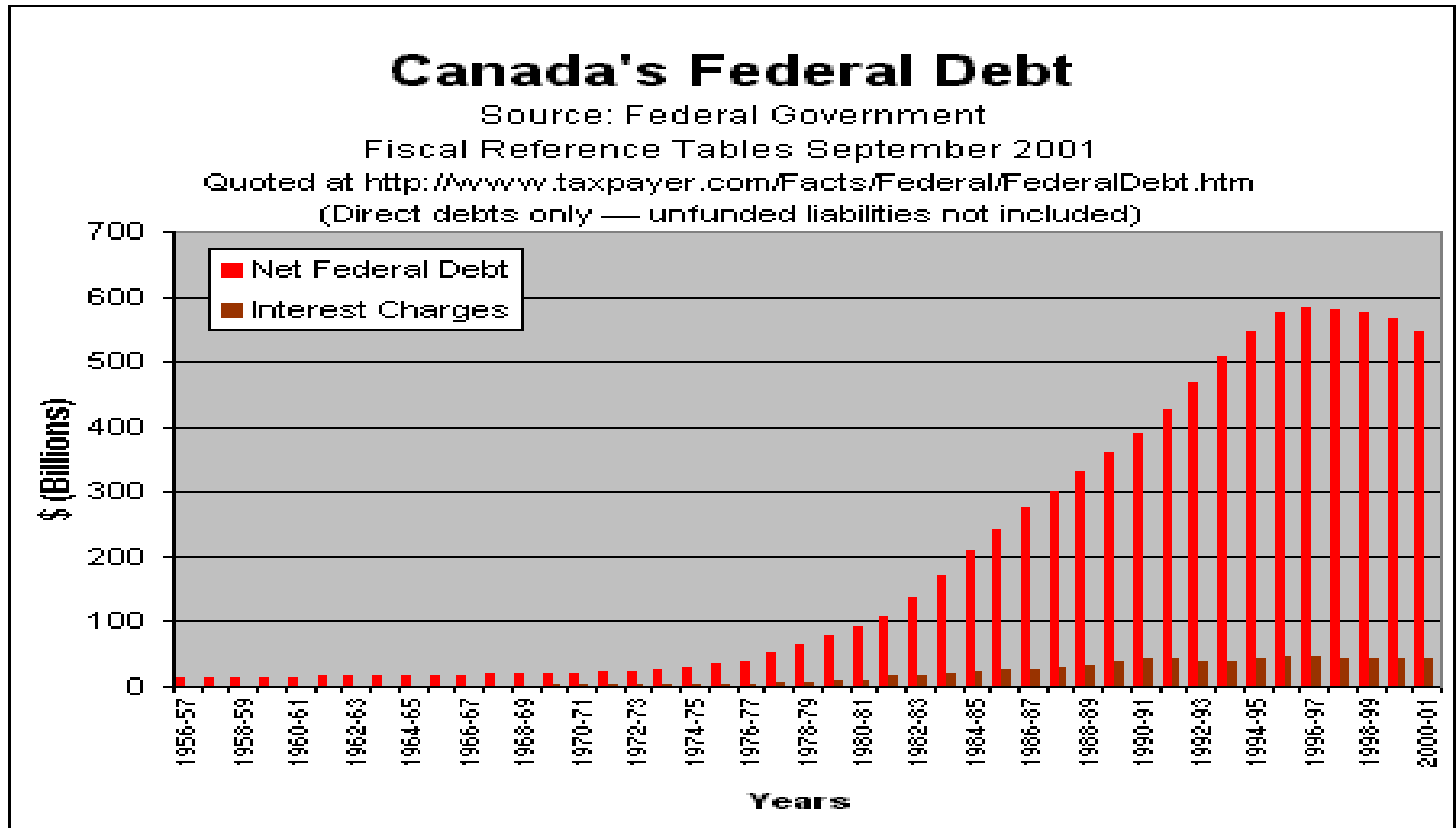
- But the Commonwealth had no control over the Germans and the Japanese, who were also issuing "national credit" in the 1930s and thriving, while the rest of the world suffered a major depression.
- Like the American colonists, they were stopped by war.

Japan gets universal electrical power, 1935.

Canada, however, was carrying on with the public banking model, very successfully.

- In 1935, the Bank of Canada Act allowed the Canadian Central Bank to create the credit to finance federal and local projects.
- It did this from 1939 to 1974, again to brilliant effect.

In 1974, the Canadian Government quit borrowing from its own central bank. Result: by 2000, the federal debt had shot up to $585B.



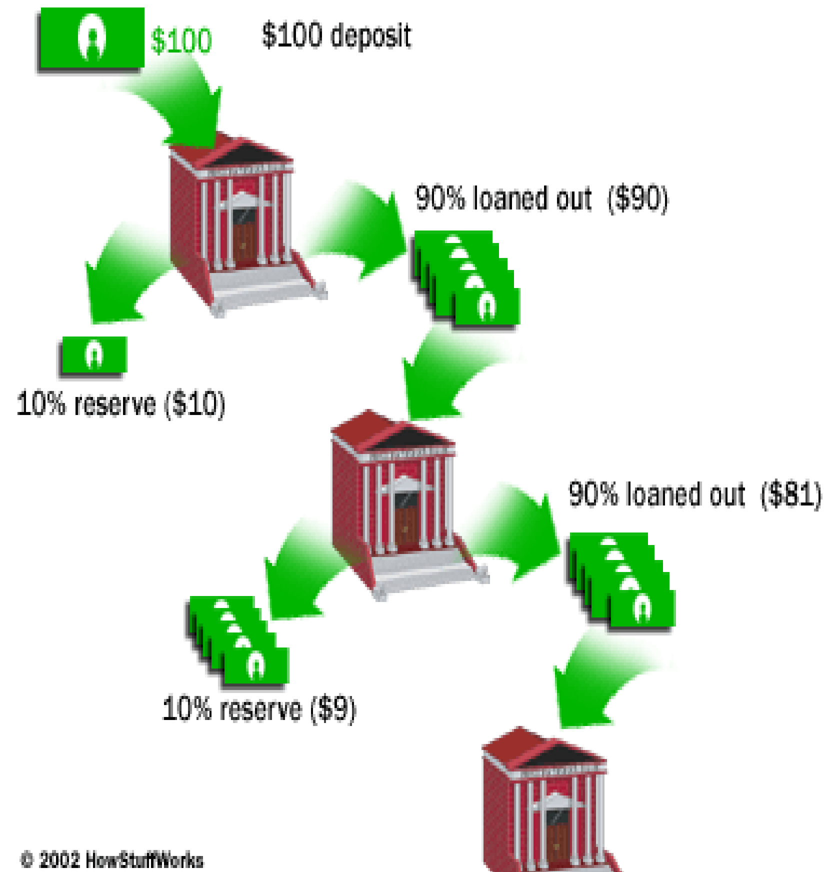
What happened in 1974?

The banks regained control of the money tap, when the Basel Committee was established by the central-bank Governors of the Group of Ten countries of the BIS.

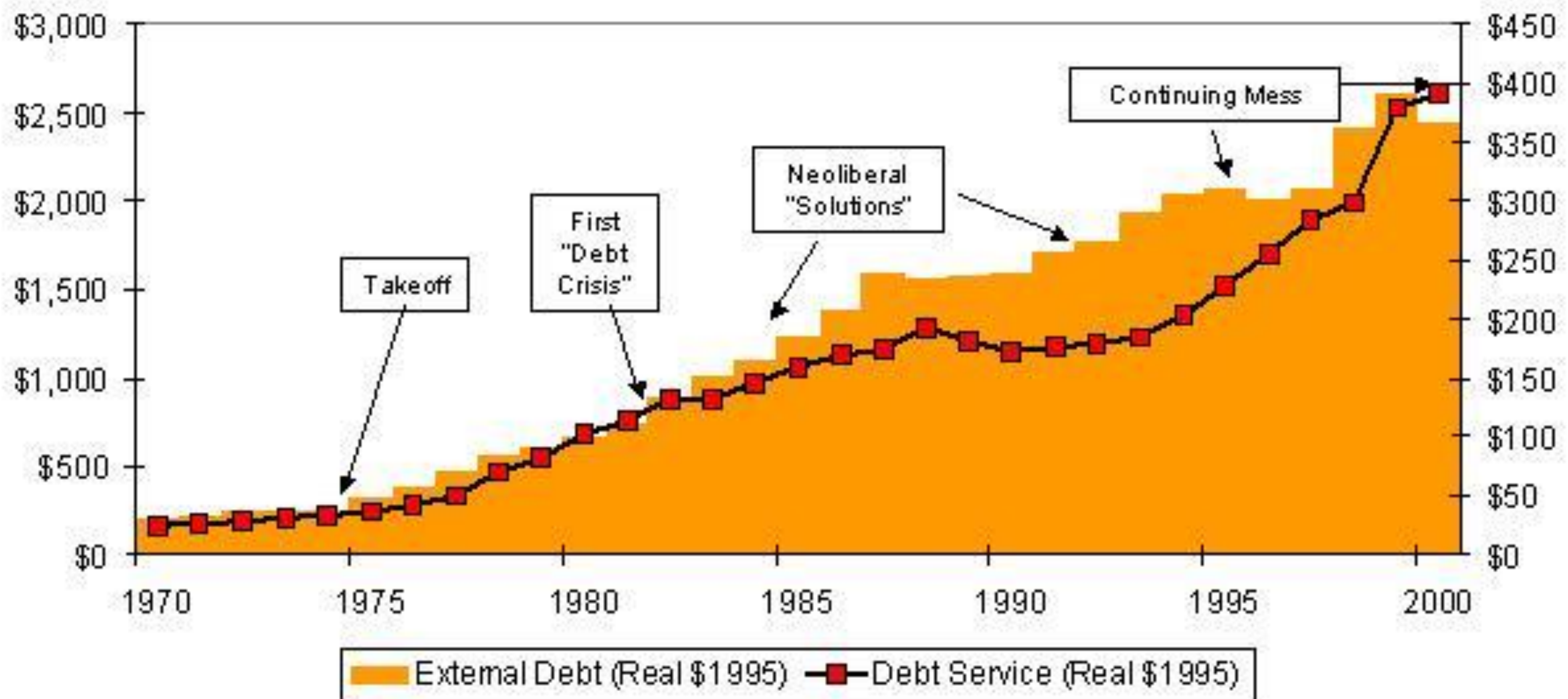
- Canada joined the BIS and the Basel Committee the same year.
- One of the key objectives of the Committee was to "maintain the stability of the currency."
- That meant no more printing money or borrowing from the nation's own central bank. Borrowing had to be private.
- It was based on a fallacious argument . . .

The presumption was that government-issued money was inflationary, while money borrowed privately was not.

But private-bank-created money is actually MORE inflationary than government-created money, since additional debt-money continually has to be created to cover the interest not created in the original loans.



Today, global control has been achieved by locking countries in debt to the international bankers. This chart shows the growth of Third World foreign debt from 1970-2000.



The debt trap was set in stages

- 1971 – The dollar went off the gold standard internationally.
- 1974 – US Secretary of State Henry Kissinger entered into a secret deal with the OPEC countries to sell oil only in dollars. The price of oil was then suddenly quadrupled. Countries lacking oil had to borrow dollars from U.S. banks.
- 1980 – interest rates were raised to 20%.

At 20% compound interest, debt doubles in under four years.

Rate of Return (%)	Years to double the initial investment
1	69 years 8 months
2	35 years
3	23 years 5 months
4	17 years 8 months
5	14 years 3 months
6	11 years 11 months
7	10 years 3 months
8	9 years
9	8 years
10	7 years 3 months
11	6 years 8 months
12	6 years 1 month
13	5 years 8 months
14	5 years 3 months
15	5 years
16	4 years 8 months
17	4 years 5 months
18	4 years 2 months
19	4 years
20	3 years 10 months

When debtor nations could not pay the banks, the **International Monetary Fund** stepped in with loans – with strings attached.

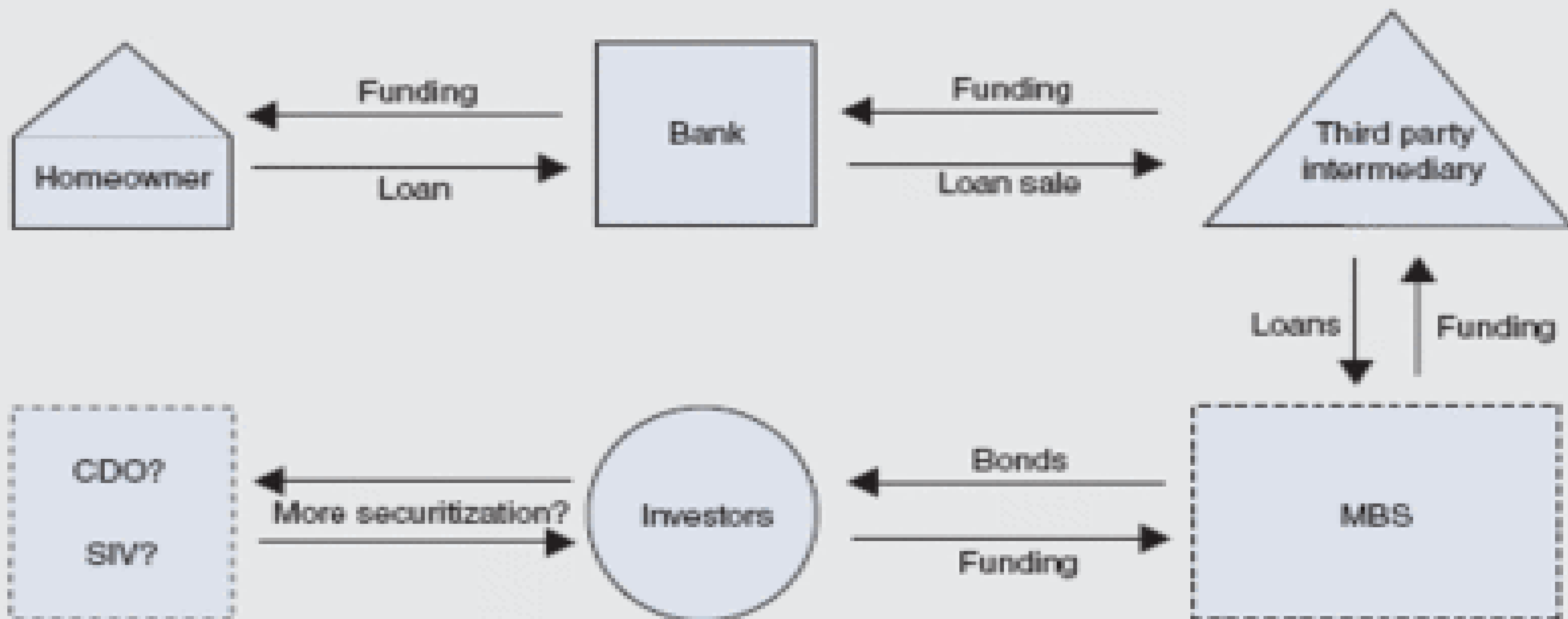
The debtor nation had to agree to “austerity measures,” including:

- cutting social services,
- privatizing banks and public utilities,
- opening markets to foreign investors,
- letting currencies “float.”

The role of BIS regulation in credit crises

- The BIS now has 55 member nations.
- In 1988, in an accord called Basel I, it raised the capital requirement of its member banks from 6% to 8%.
- The result was to cripple the Japanese banks, which until then were the world's largest creditors. Japan entered a recession from which it has yet to recover.

U.S. and other Western banks escaped -- for the time being. They dodged the capital requirement by moving loans off their books, bundling them up as "securities" and selling them to investors.



Securitization: making sausage of homes

- Investopedia definition: “The process through which an issuer creates a financial instrument by combining other financial assets and then marketing different tiers of the repackaged instruments to investors.”
- Example: mortgage-backed securities.
- What it means: bankers bundle many IOUs or promises to pay secured with collateral (e.g. mortgages), slice and dice them like sausages, and sell them off to investors.

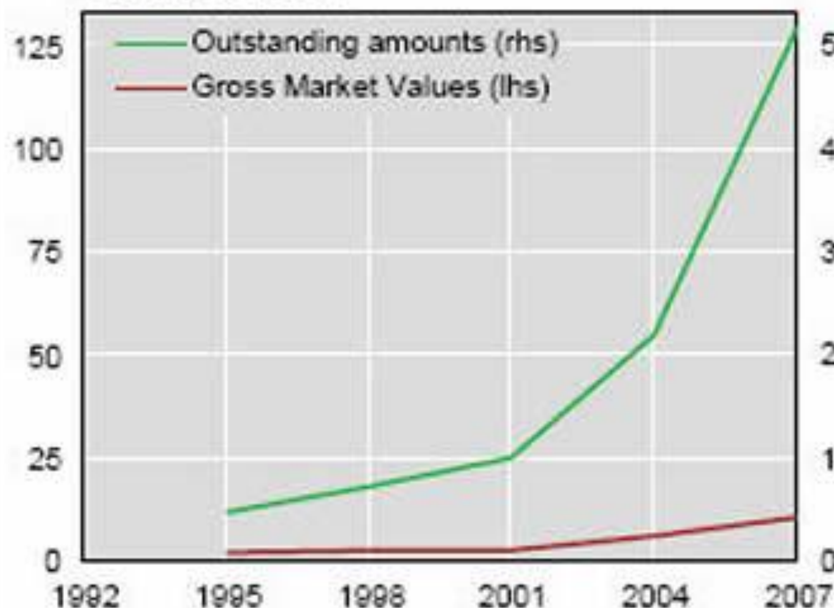
But these bundled mortgages were “toxic” – not worth what they were claimed to be worth. To persuade investors to buy them, they were protected against default with “derivatives” – which are basically just bets.

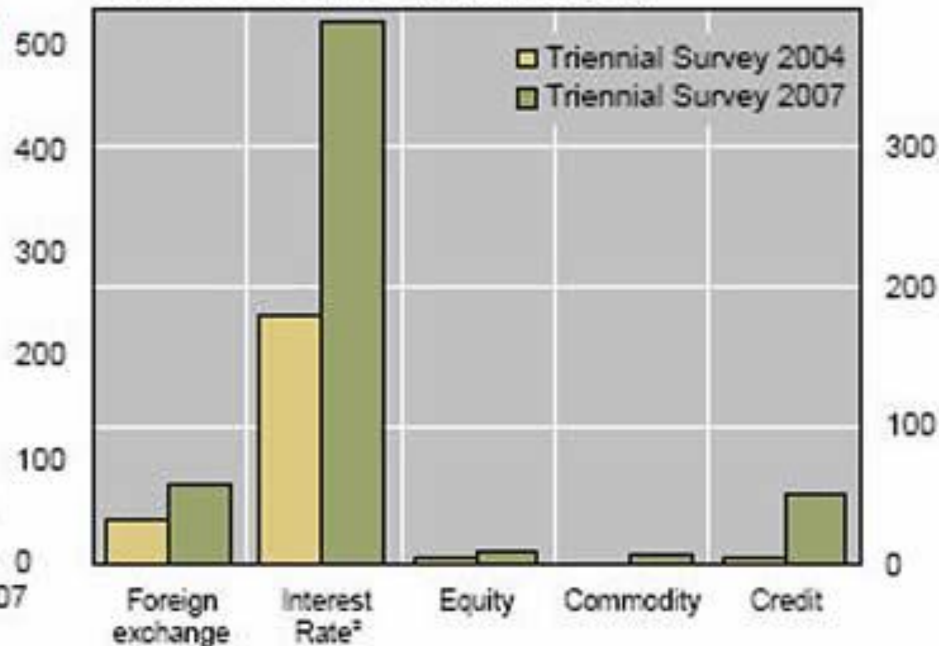
Here’s how derivatives work --
The “protection seller” collects a premium for agreeing to pay in the event of default. He’s betting against default. The “protection buyer” buys the premium. Like gamblers at a horse race, derivative players can bet without owning a horse.

Derivatives became a very popular form of gambling, creating the mother of all bubbles – exceeding $500 trillion (€300 trillion) by the end of 2007.

Positions in OTC derivatives markets

In trillions of US dollars[1]





Note: Based on the results of the Triennial Survey

[1] All figures are adjusted for double-counting. [2] Single currency contracts only.

Graph 1

http://www.marketoracle.co.uk/images/2008/financial-sector-staying-alive-april08_image001.jpg

Because of securitization and derivatives, credit mushroomed. Banks were so unconcerned with risk that virtually anyone who walked in the door got a loan.

http://21stcmb.typepad.com/

The tipping point came in August 2007 with the collapse of 2 Bear Stearns' hedge funds, exposing the derivatives scheme. The market for derivative-protected securities suddenly dried up.

http://www.inkcinct.com.au

U.S. banks were captured in the credit crunch with Basel II and the mark to market rule.

- In November 2007, new accounting rules were imposed requiring U.S. banks to revalue their capital.
- Result: The credit bubble popped suddenly.
- The rule grew out of the Basel II Accords imposed by the BIS in 2004, requiring "value at risk" accounting. Called "mark to market" accounting, it required banks to value their assets according to market demand that day.
- Since there was no longer much demand for mortgage-backed securities, many banks no longer had enough capital to make new loans.

The result was an instant credit freeze, crippling U.S. banks just as Basel I had crippled Japanese banks. Governments responded by bailing out the banks, and by handing global regulation to the BIS.

The BIS has become global regulator, just as Quigley predicted.

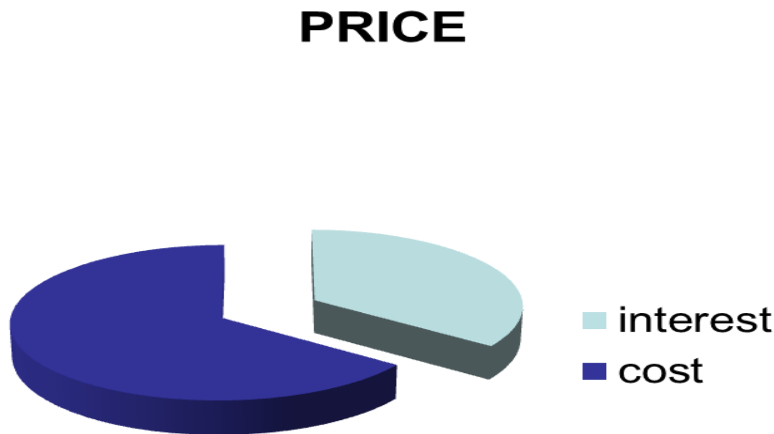
In April 2009, the G20 nations agreed to be regulated by a Financial Stability Board *based in the Bank for International Settlements*.

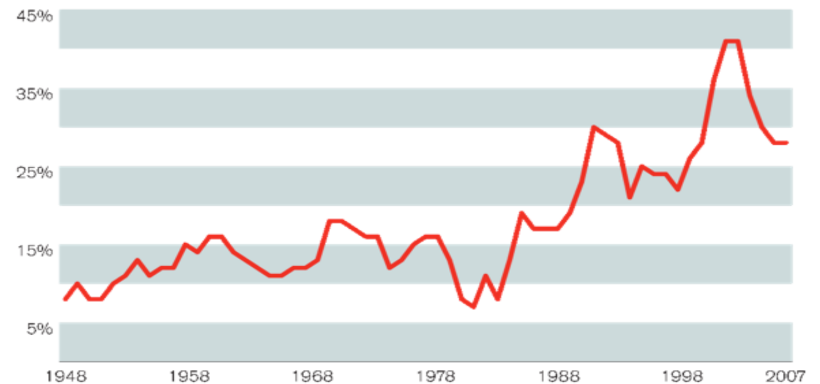
The G20 agreed to comply with "standards and codes" set by the Board.

That means the bail-in template (confiscating depositor funds in the event of insolvency) has the force of law.

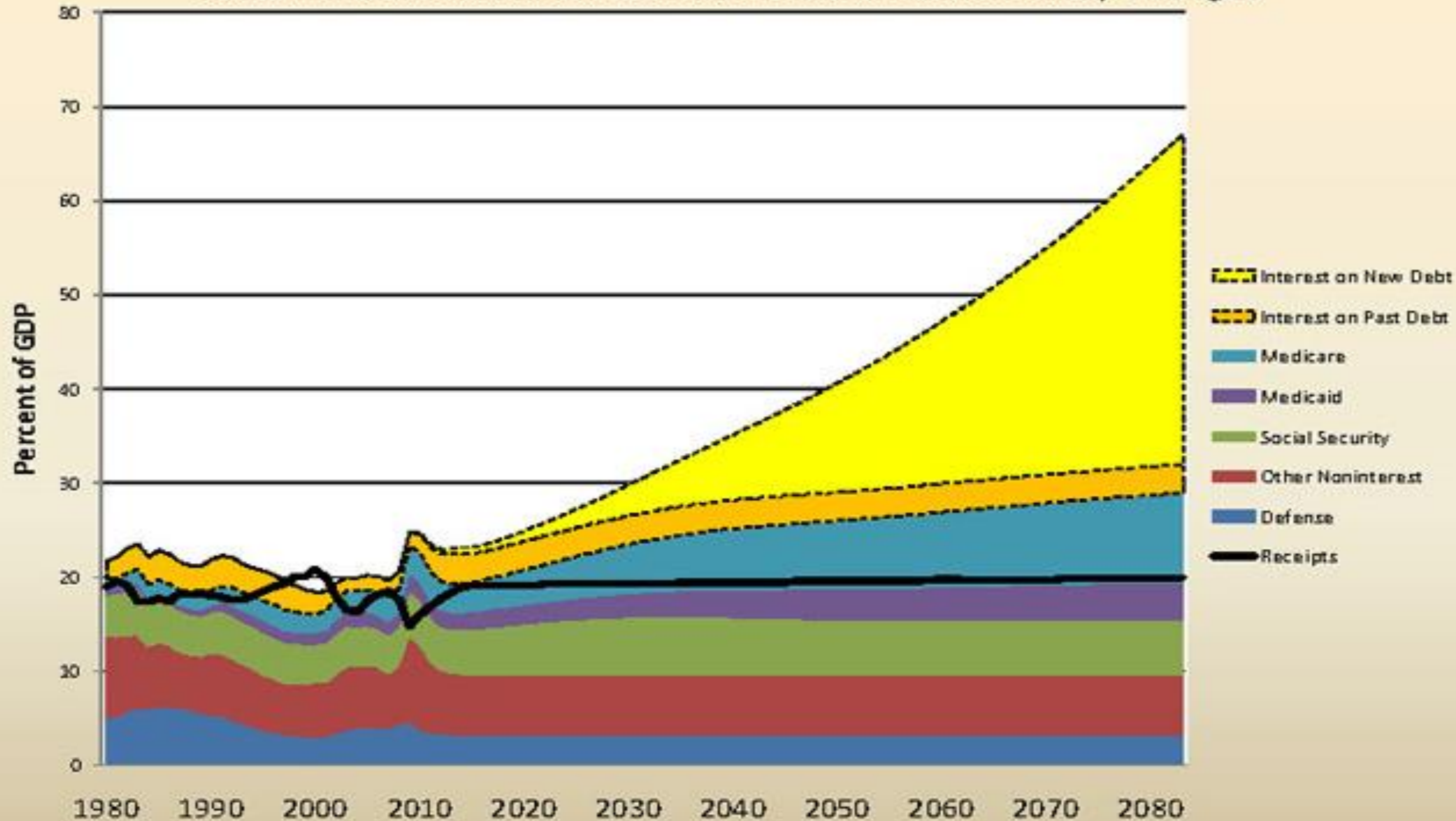
How to get out of this debt trap? Instead of propping up the banks, eliminate the middleman.

Today, 35%-40% of everything we buy goes to interest, and 29% of business profits go to the financial industry.

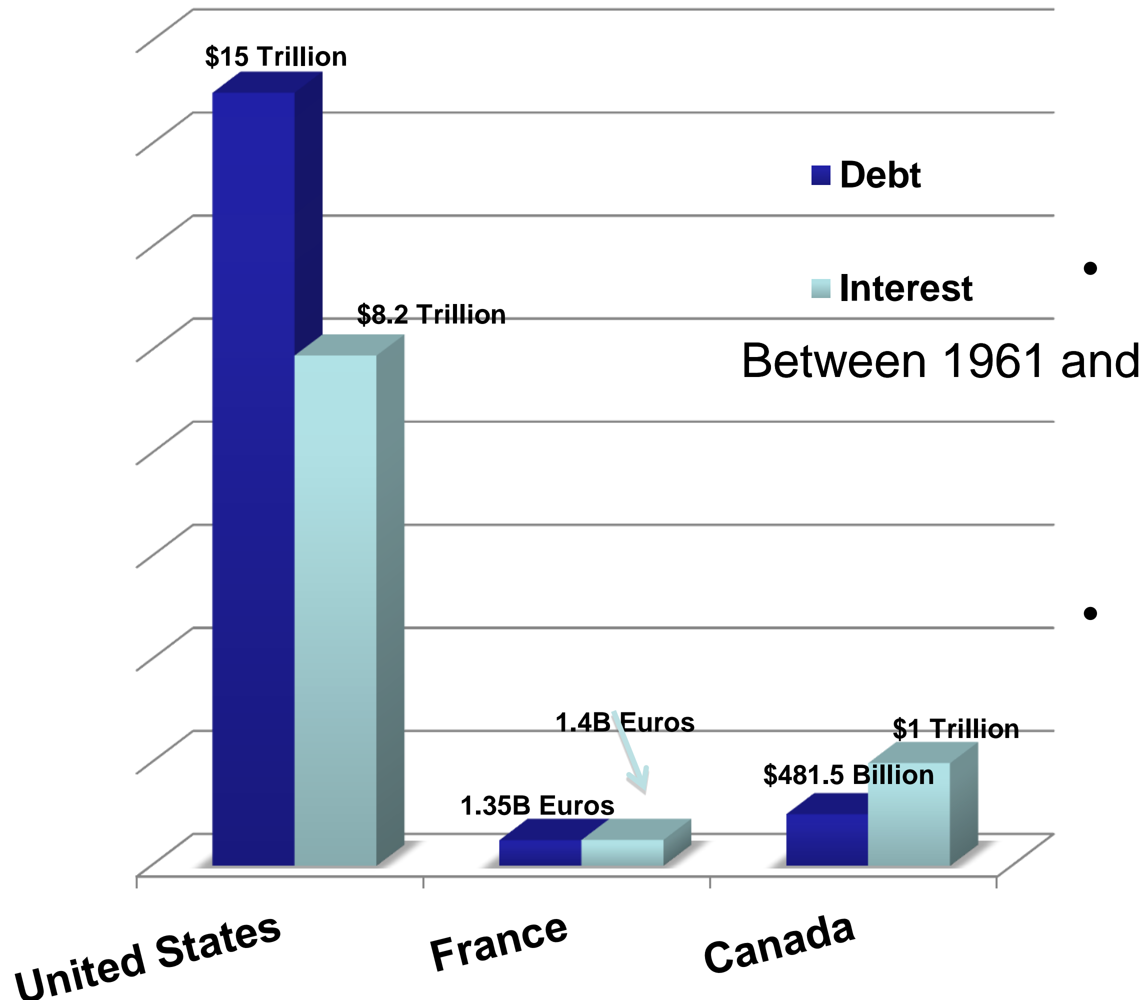




Without interest, even a large federal debt might be sustainable.

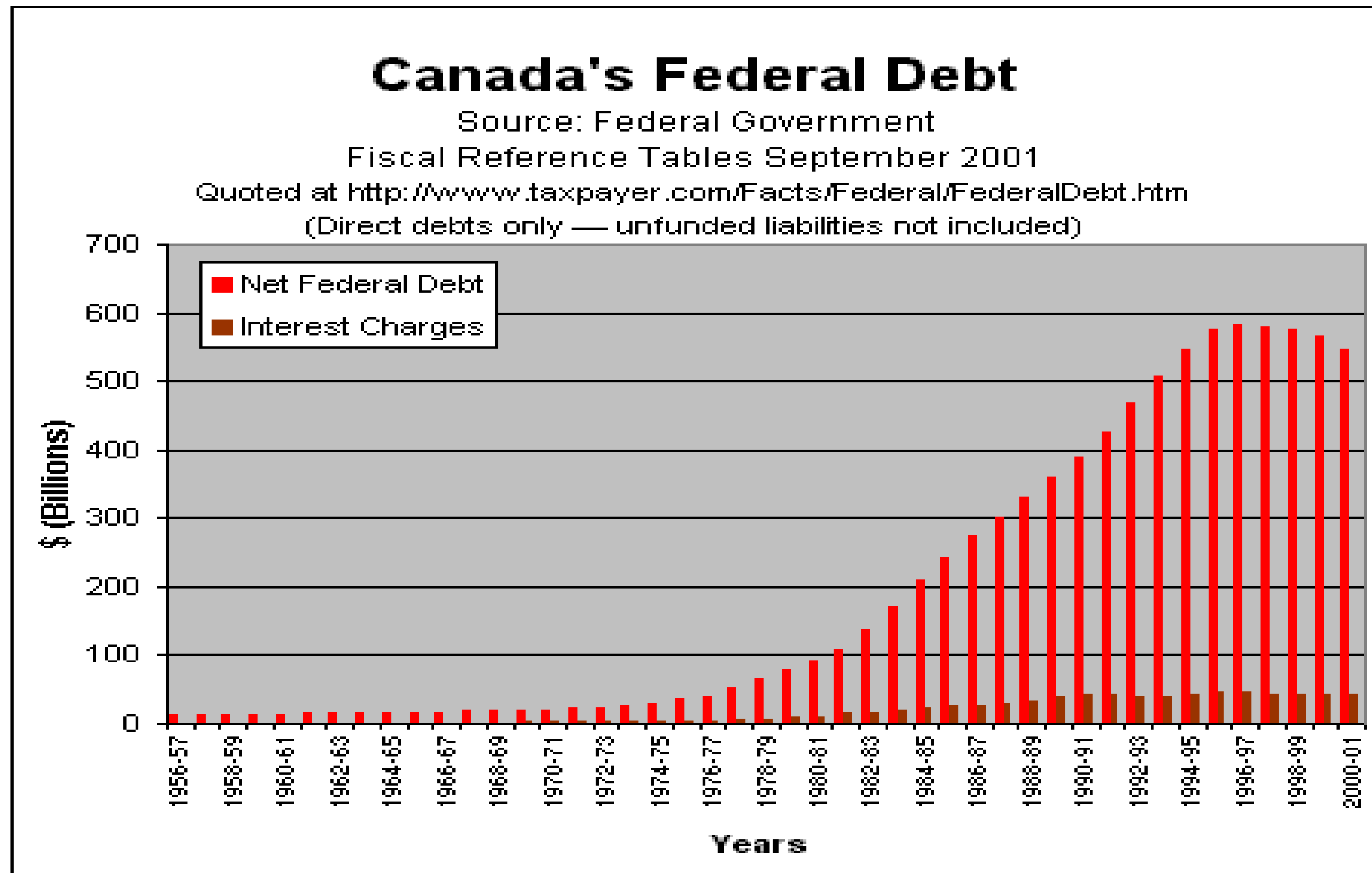


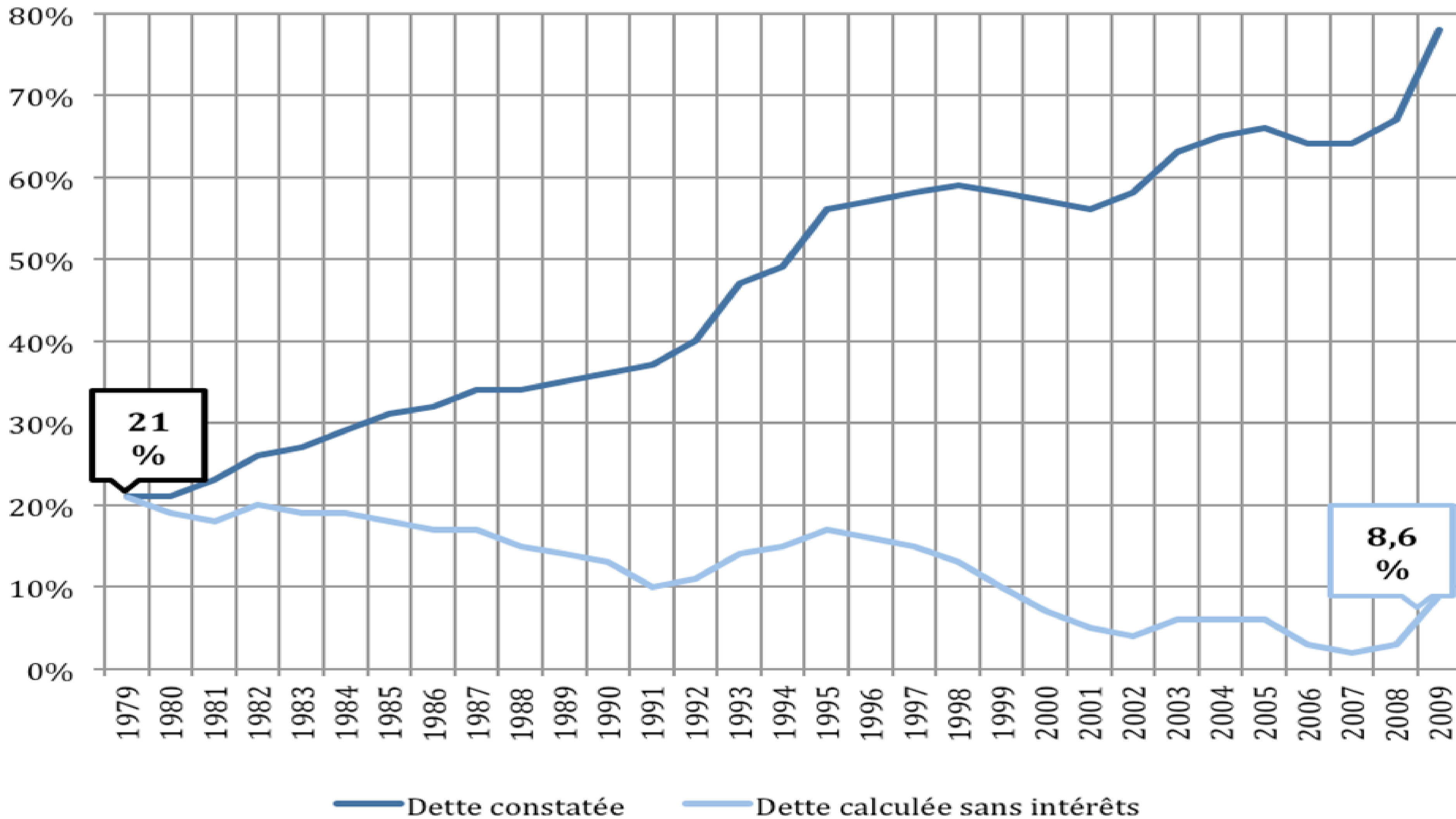
Without interest, there might not even be a national debt.



- U.S. debt is $15T. $8.2T has been paid in interest in 24 years. http://www.treasurydirect.gov/govt/reports/ir/ir_expense.htm
- France's debt increased 1.35B Euros since 1973. 1.4B Euros paid in interest since then. https://www.youtube.com/watch?v=P8fDLyXXUxM&feature=player_embedded
- Canada had a debt in 2006 of C$ 481.5 billion, and had paid almost C$ 1 trillion in interest since 1961. http://www.enterstageright.com/archive/articles/1006/1006cdndebt.htm

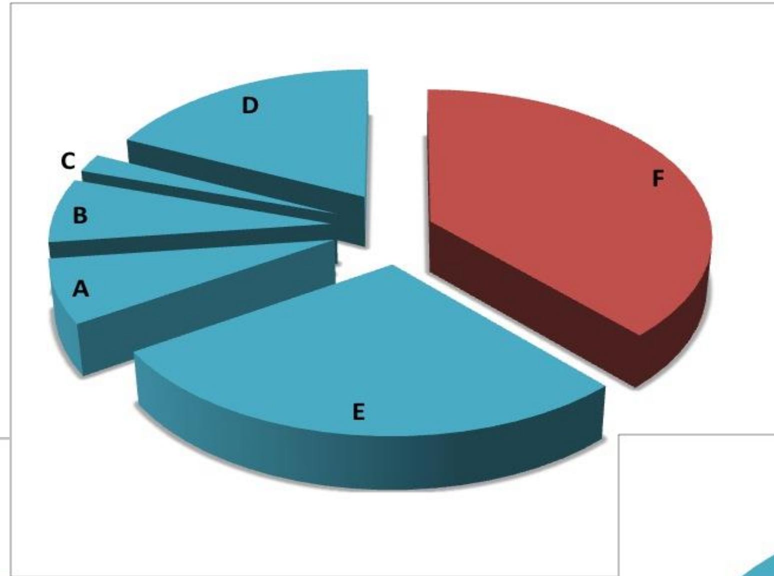
In 2006, the Canadian government paid over twice its debt just in interest.



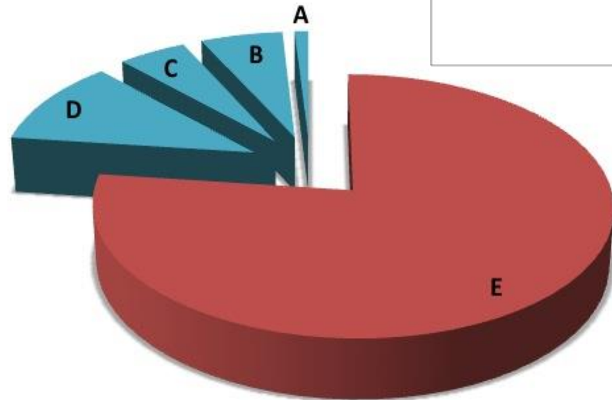


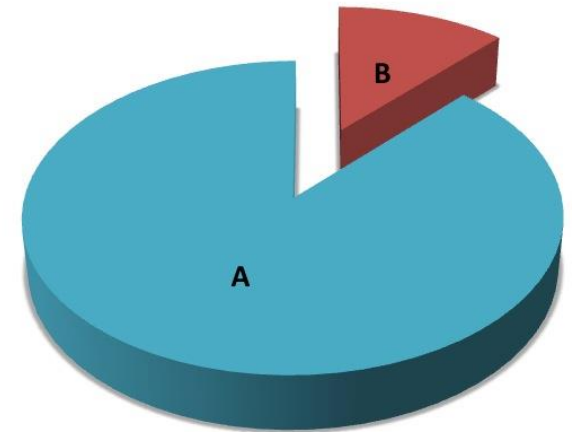
From Bernard Lietaer, et al., “Money and Sustainability” (2012)

Cutting out interest cuts the average cost of public projects by 40%.



Drinking Water
Cost of interest on capital 38%





Garbage Collection Fees
Cost of interest on capital 12%

Rent in Public Housing
Cost of interest on capital 77%

From Margrit Kennedy, http://www.monneta.org/upload/pdf/Pres_MK_CompC.pdf

EU governments, like US states, cannot issue their own money. But they can still cut out interest. How? By borrowing from their own publicly-owned banks.

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One billion big ones

State budget outlook predicts huge surplus, $70 oil

By DALE WETZEL
Associated Press Writer

A new forecast of North Dakota's tax collections predicts a $1 billion budget surplus in July, continuing a robust financial trend that has defied a national recession and budget deficits in most states.

Oil prices, a key contributor to the state's wealth, are expected to average $70 a barrel for the next two years, the forecast finds.

Revenues are expected to rise almost 10 percent during the same period. An even higher spike is expected in sales tax collections, which provide the biggest share of the budget for North Dakota government.

"I think it's good news, but it's not unexpected," Lt. Gov. Jack Dalrymple said Tuesday. "It shows the economy in North Dakota is still in good shape."

North Dakota's current two-year budget is $8.84 billion, a figure that includes federal aid to the state.

The forecast was compiled by the state Office of Management and Budget and Moody's Economy.com, a West Chester, Pa.-based consultancy, to prepare Gov. John Hoeven's budget recommendations. Its numbers will be updated in November, a month before the governor's spending plan is presented to the Legislature, said Pam Sharp, the state budget director.

The forecast includes estimates of state tax collections for the rest of the current 2009-11 budget period, which ends June 30, and a forecast of revenues for the *Continued on 9A*

Only one U.S. state actually owns its own bank – North Dakota.

- It is also the only state to escape the credit crisis, sporting a budget surplus every year since 2008.
- It has the lowest unemployment rate, foreclosure rate, and default rate in the country.

North Dakota has had its own bank since 1919.

- The farmers were losing their farms to the Wall Street bankers.
- They organized, won an election, and passed legislation.

The Bank of North Dakota (BND) model

- The BND has a massive, captive deposit and capital base.
- All state revenues are deposited in it by law.
- The bank is a dba of the state ("North Dakota doing business as the Bank of North Dakota"), so all the state's assets are technically the bank's assets.

Governance

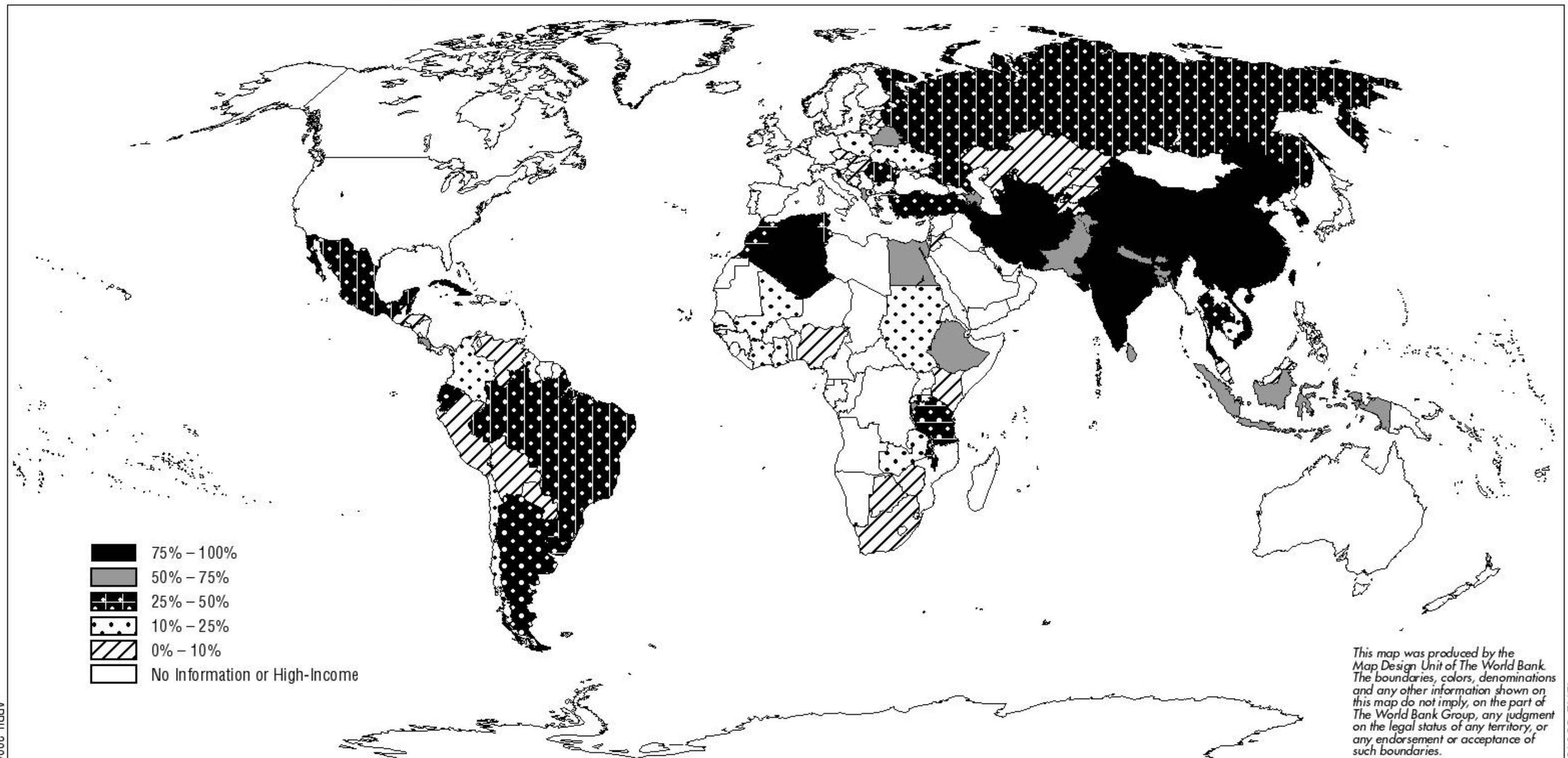
- Completely transparent
- Completely accountable – frequent audits
- Mandate to serve the public
- No bonuses, fees, commissions
- No derivative speculation
- Operated by bankers, not politicians

What the BND does for ND:

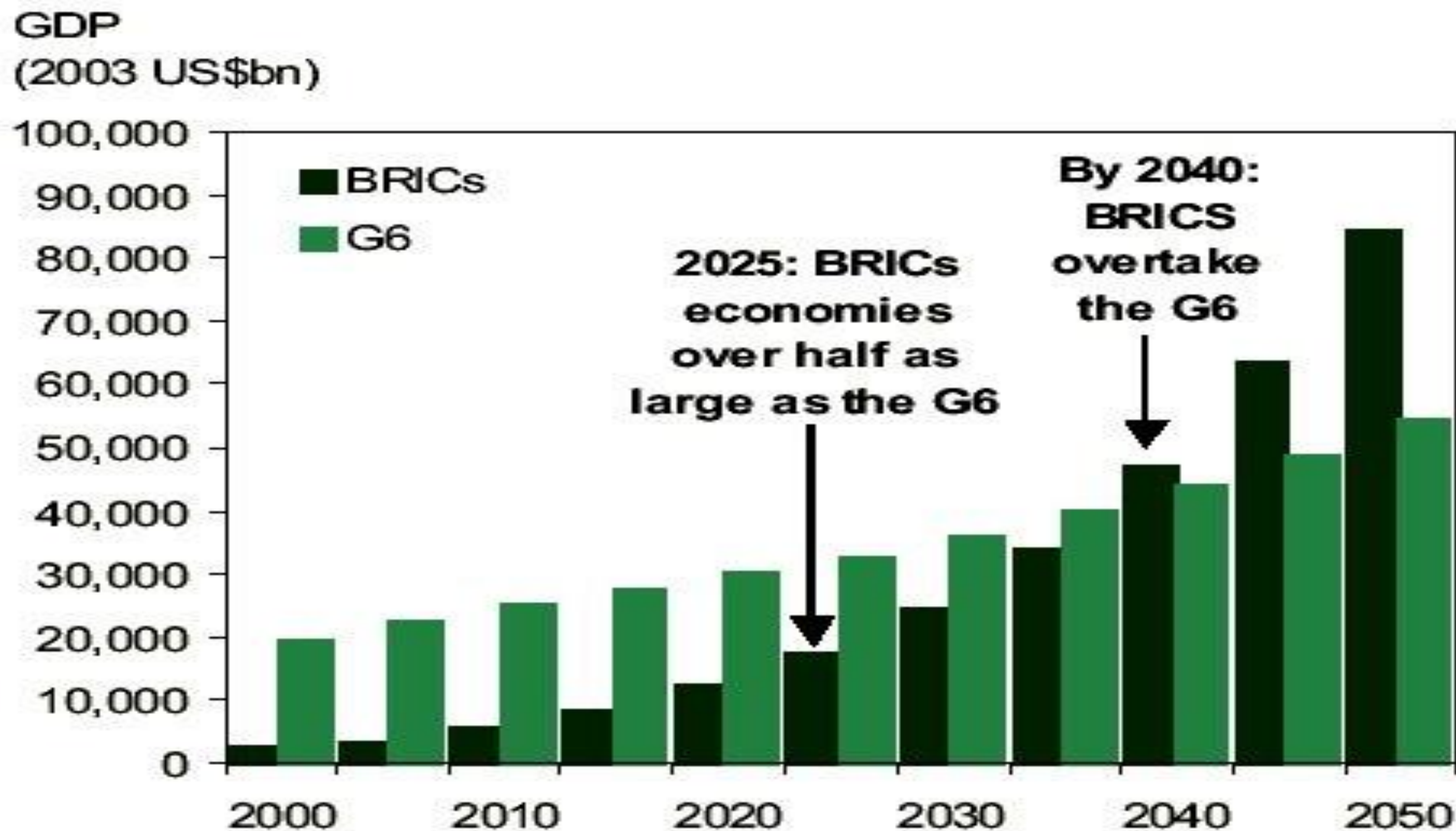
- Pays a dividend to the state of $30M/year (population 640,000).
- The BND has had a return on equity since 2008 of 19-26%.
- Pays competitive interest on state deposits.
- Partners with local banks to increase local lending.
- Cheap credit lines to state and local government agencies.
- Low-interest loans for designated local projects.
- Redirects credit away from speculation toward local lending; mandate to serve the public interest.
- Underwrites municipal bonds, avoiding high cost of fees, “insurance” (swaps), and bond market speculation.

The BND is only one bank. But globally, 40% of banks are publicly-owned.

State Ownership in Banking, 2000–2002



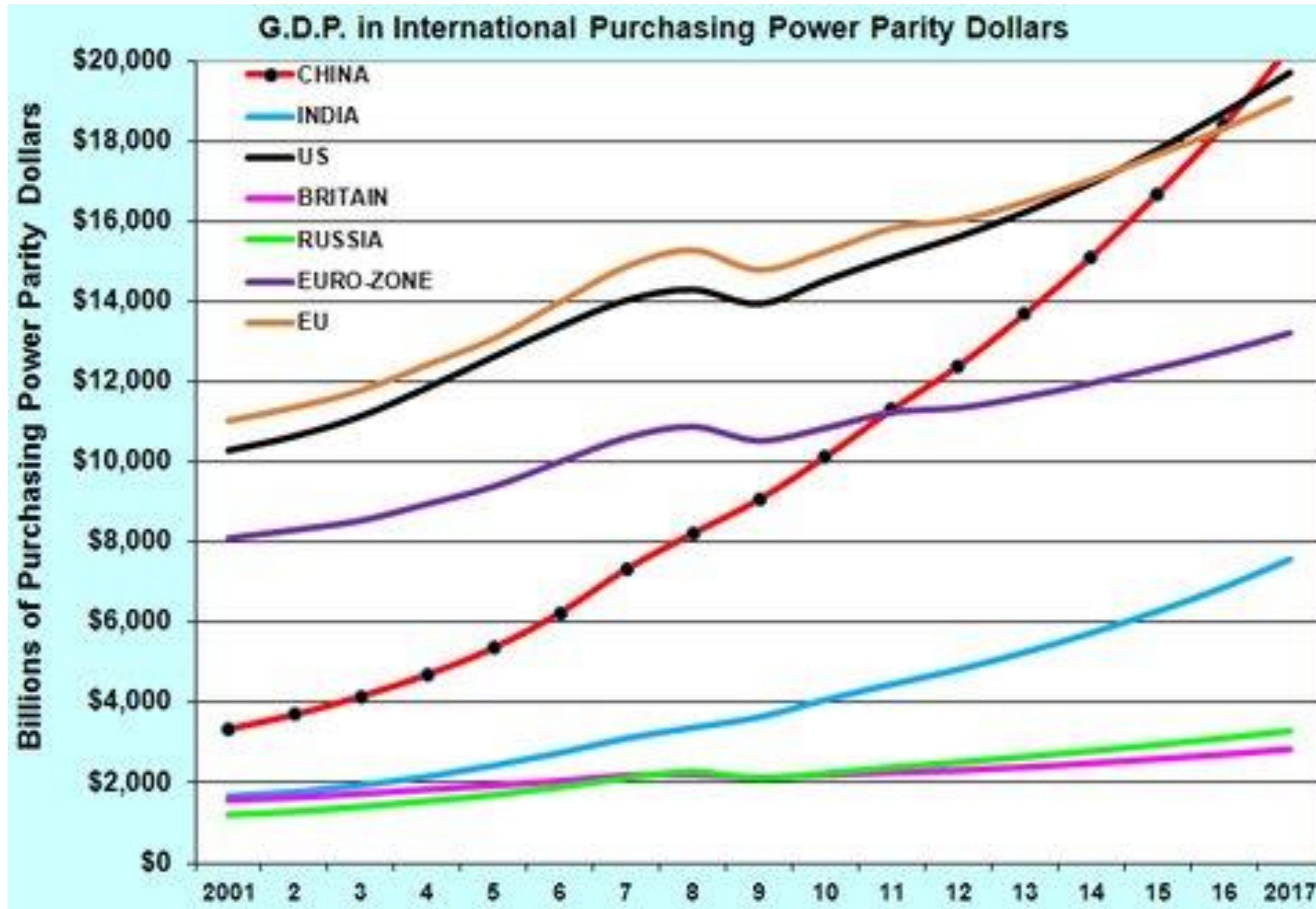
These are largely in the BRIC countries, which all escaped the credit crisis.



“Economic miracles” have occurred in countries with strong public banking sectors.

- China
- Korea, Taiwan, Singapore, Hong Kong
- Post-war Germany and Japan
- Brazil, Argentina

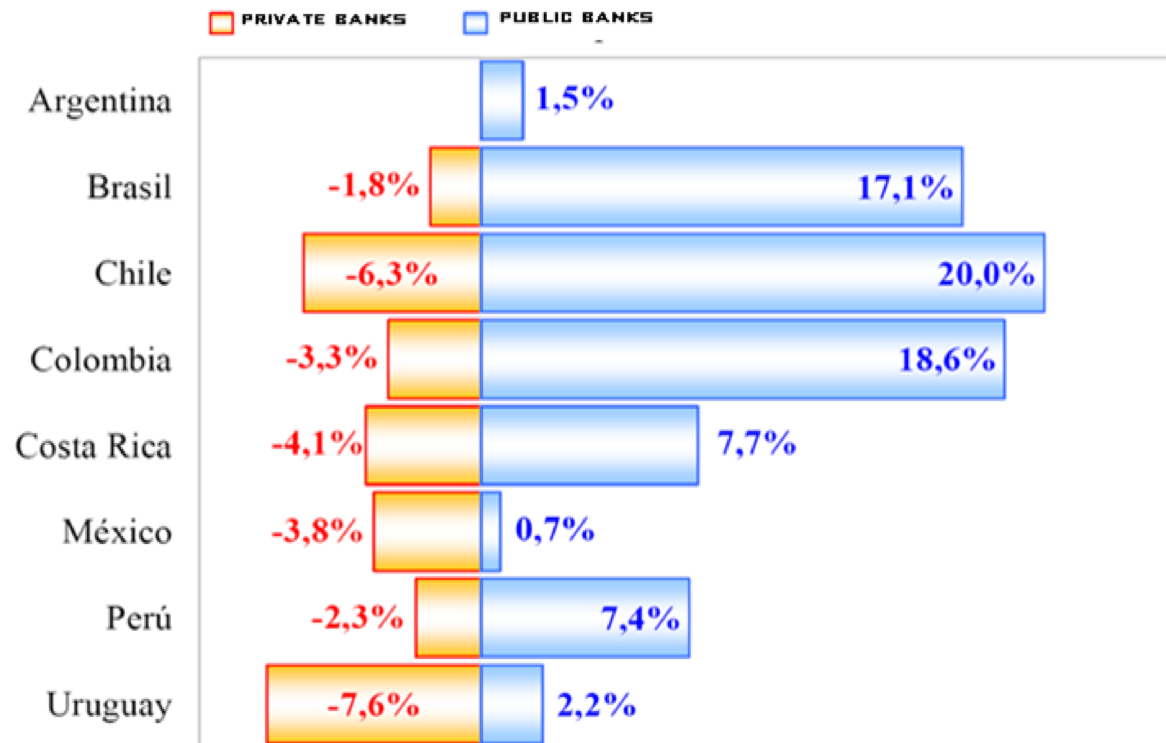
China:
global leader in rapid development



Economist Ha Joon Chang: “Korea’s progress is as if Haiti had turned into Switzerland.”

- Per capita income increased 14-fold in 40 years, something Britain took 2 centuries and the U.S. took 1-1/2 centuries to do.
- How? Chang says, “The government owned all the banks, so it could direct the life blood of business – credit.”

Public banks lend counter-cyclically, aiming at sectors most in need.



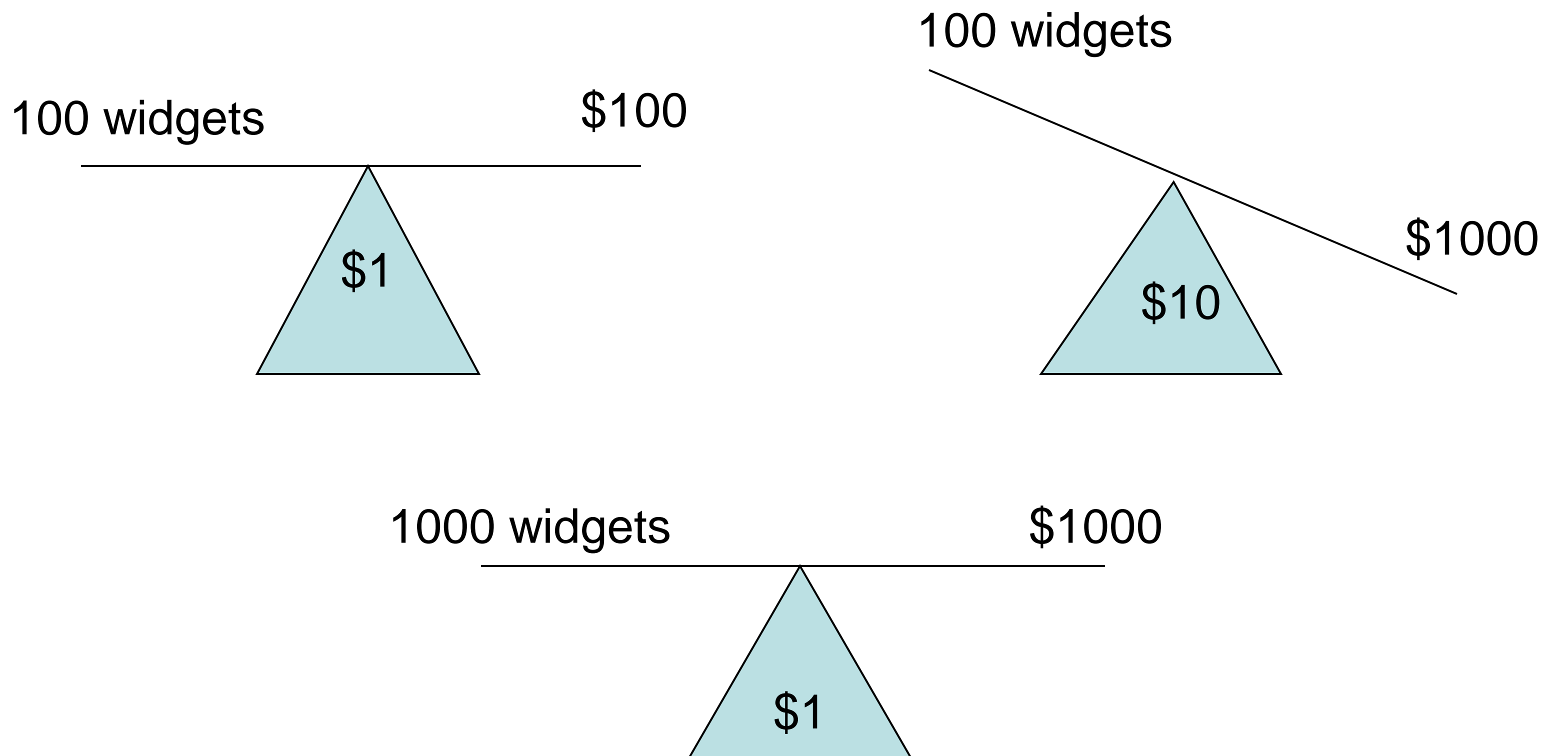
Some alternatives for the EZ and Ireland

1. The ECB could issue more Euros, not to banks, but directly into economies.
2. The money supply could be expanded with private currencies.
3. EZ governments could issue their own national currencies for internal use in tandem with Euros.
4. EZ governments could borrow from their own publicly-owned banks, leveraging public capital and deposits into credit for the local economy.
5. EZ governments could create domestic “development banks” or infrastructure banks, funded by issuing bonds.
6. Ireland could repudiate “odious” debt, exit the EU, and issue its own debt-free currency.

1. Have the ECB issue more Euros.

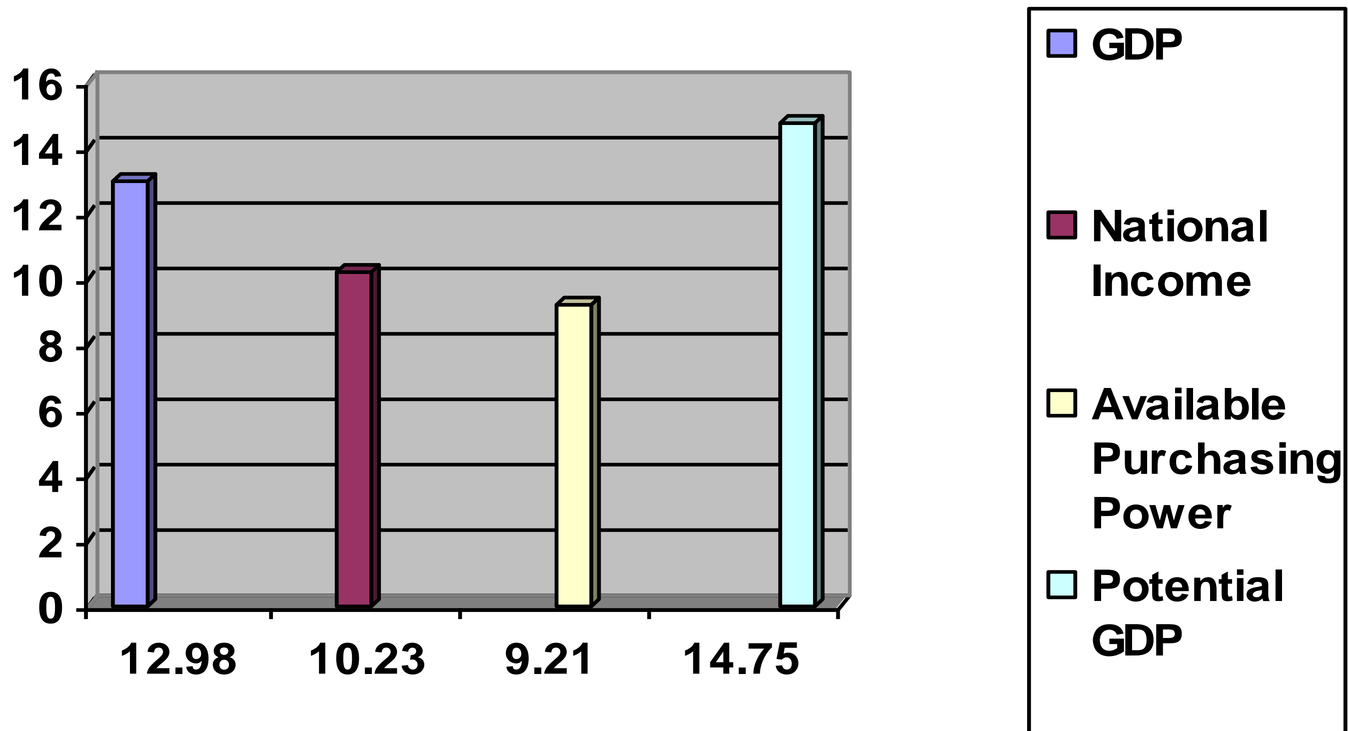
- Distribute in proportion to populations, in an amount sufficient to make up the difference between incomes and GDP.
- Why isn't this happening? Bad economics – the "sound money" fallacy says it would be inflationary.

But price inflation results only when demand (money) exceeds supply (widgets). When supply and demand increase together, prices remain stable.



Euros could be added up to the point of full employment.

U.S. 2006 Figures in Trillions of Dollars



Difference between GDP and potential GDP at full employment: $1.77 trillion
Difference between GDP and available purchasing power: $3.77 trillion
Difference between GDP and available purchasing power at full employment: $5.5 trillion
[Figures supplied by Richard Cook]

2. Expand the money supply with private currencies

- Example: Bangla Pesa—increased GDP by 20%. Showed there was no shortage of demand, just a shortage of currency.
- Example: Swiss WIR (electronic currency traded among member businesses)
- Limitation: not universally accepted.

3. Issue a national or local government currency in a dual-currency system. Call them Irish pounds or IOUs or bonds or frequent flyer miles—whatever works politically.

- Example: Uruguay's "charrua" or "liquidity network"
- Example: Argentinian "debt-cancelling bonds" (2001)
- Example: California warrants (IOUs)

4. Form publicly-owned banks

- Even if the government can't issue its own currency, it can own a bank that leverages public capital and revenues into "bank credit" (money).
- Example: Bank of North Dakota.
- *The Lisbon Treaty permits public banks to join the bankers' club and borrow from the ECB at 1%.*

- Lisbon Treaty, Article 123, forbids direct borrowing by member governments but excepts "publicly-owned credit institutions."
  - 2. "Paragraph 1 shall not apply to publicly owned credit institutions which . . . shall be given the same treatment by national central banks and the European Central Bank as private credit institutions."

A publicly-owned bank can raise government revenues without raising taxes, by:

- Returning a hefty dividend to the government.
- Increasing the tax base by partnering with local banks to increase their loan capacity, fostering local business.
- Reducing government borrowing costs by providing low- or no-interest loans to state and local government.

5. Create a national infrastructure bank or domestic development bank.

- Example: Japan Post Bank, funding Japan's "second budget." Debt to GDP ratio of 225% is no problem.
- Example: Brazil's BNDES.
- Example: Roosevelt's Reconstruction Finance Corporation (RFC).

The RFC sidestepped Congress to fund the New Deal and World War II, using self-liquidating loans – loans that paid for themselves.

- The RFC advanced $10.5 billion, rebuilt the economy, funded World War II, and *returned $500 million in profits to the government.*
- The money came from bonds sold to the Treasury and the public.

6. Exit the Eurozone

- Declare the Irish bank guarantee fraudulent and void.
- Declare the debt “odious” and illegal. .
  - Example: Ecuador
- Issue debt-free national currency.
  - Create jobs
  - Rebuild infrastructure
  - Fund pensions and welfare
  - Not inflationary up to full employment

- Establish a national central bank.
  - Deposit public monies into it.
  - Leverage public funds into low-cost credit for the economy.
- Restore to Ireland the abundance that is its birthright.

For more information –
PublicBankingInstitute.org
WebofDebt.com