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Amid financial shakeup, a new architecture is coming together

From major powers Brazil, Russia, India, China and South Africa, to rural Australian municipalities, political leaders are challenging the current financial order and rolling out new mechanisms to replace it.

There has been a concerted effort by BRICS nations, with a growing retinue of collaborators, to ramp up functions of a new financial architecture. China has just paid for energy from the United Arab Emirates in yuan for the first time, as did France; Brazil and China have agreed to settle trade in yuan; ASEAN (Association of Southeast Asian Nations) countries will trade in local currencies, and Indonesia is introducing its own domestic payment system. A proposal for a "new currency" to serve a multipolar world will be presented at the BRICS leaders' summit scheduled for August in South Africa.

This has been motivated by the latest example of the dying US-centric banking system, with the collapse of three US banks and contagion spreading to European giants Credit Suisse (out for the count) and Deutsche Bank (long on life support and again showing signs of imminent demise).

The unravelling US dollar order (p. 8) threatens economies and people everywhere. Mechanisms were enacted after the 2008 crash to make *the people* pay for the next one, by stealing their deposits. This is now hitting headlines from the USA to regional Australian towns.

Senator Malcolm Roberts brought the issue of "bail-in" directly to Finance Minister Katy Gallagher, and pointed to the reality that the Deposit Guarantee Scheme is effectively worthless, as *if* invoked it would cover only some 7 per cent of deposits! (p. 3) This parallels the US situation where the federal deposit insurance fund holds only US$128 billion while deposits total some US$17.7 trillion! This is a big topic of debate as authorities were forced to back all deposits in the failed US banks, given their high levels of uninsured deposits, to stem runs on those banks. The real fear, though, was of setting off a run on *all* banks, knowing that nearly 200 others are in the same position as Silicon Valley Bank. After 15 years of quantitative easing, the overinflated assets of the US banking system are worth US$2 trillion less than the book value registered by the banks holding them, said a March report released by the Social Science Research Network. ("Four US banks and one Swiss giant—expect more bank runs", *AAS*, 22 March.)

ASEAN delegates meeting in Bali agreed to trade in local currencies and other measures to insulate themselves from the US dollar order. Photo: AFP/ Sonny Tumbelaka

The danger of councils having deposits seized in a new financial meltdown is very real for Australian shires that saw investments in toxic securities wiped out in 2007-08. The federal legislation allowing for bail-in of deposits to save failing banks, passed in February 2018, was raised at a Wagga Wagga Council meeting on 3 April. A motion to demand the federal government close the loophole that can allow confiscation of deposits, which would include the $196 million held by Wagga council, passed unanimously. The deposit guarantee, even if it did what it professes to do, would obviously not protect these funds, or those of any other Australian council or large organisation.

This unanimous endorsement followed a comprehensive briefing on the subject by Councillor Richard Foley (p. 12), who has been leading the local fight to stop regional banking closures. Numerous councils have taken up that issue—which is shuttering their towns—creating a formidable force that given the extension for submissions to the parliamentary inquiry (p. 3), can be unleashed even more effectively. No doubt more council will take up the fight against bail-in, especially since Wagga has determined to bring the issue to the National General Assembly of Local Government which meets in June. At the earliest opportunity, Malcolm Roberts will again move the One Nation bill to amend the bail-in legislation to explicitly exclude deposits from bail-in.

With these tandem fights we have an extraordinary opportunity to contribute to the international fight for a better economic order!

IN THIS ISSUE

The US dollar reckoning

By *Elisa Barwick*

The current banking turmoil cannot be separated from the fracturing of the US dollar system triggered by geopolitical actions—they are both features of a collapsing global economic framework. US banks are part of a broader platform upon which a massive financial bubble has been constructed, and which a growing portion of the world can see is crumbling. One way or another a new economic order will replace the current one.

Former IMF Deputy Managing Director Zhu Min, interviewed at the annual Boao Leadership Forum, held 28-31 March in Boao, China, addressed the "broad mismatch of assets and liabilities in the US banking system" causing a crisis that is "much more serious than in 2008". "Assets", he said, "are heavily speculative and may be long-term" (and are currently dropping in value due to rising rates), whereas "short-term liabilities are running out of banks because those liabilities (deposits) are earning nothing for depositors." China, however, which has not seen periods of wildly low or high interest rates like many Western nations, does not suffer such a mismatch. Both governments and private companies in China do have high debt, he acknowledged, but there are growing industrial and real assets to show for it. Chinese Premier Li Qiang told the forum that "In this uncertain world, the certainty China offers is an anchor for world peace and development."

Playing into this mismatch, is a combination of a white anting of the US Treasury market itself ("The fall of the hedge funds?", p. 9) and a Treasury bond sell-off by major nations. This is causing a drastic crunch point, for the entire US dollar-dependent world. Once upon a time when the USA issued new debt certificates it was guaranteed that someone, somewhere in the world would buy them. But that "superpower" of the US dollar is waning, wrote columnist Fareed Zakaria, in the 24 March *Washington Post*. Since sanctions were levied on Russia, he wrote, China and Russia are conducting most of their trade in Chinese currency, the yuan, and "making efforts to get other countries to follow suit". Zakaria notes that US public debt has grown *fivefold* in the last 20 years and in the same timeframe the Fed has solved numerous financial crises by expanding its balance sheet *twelvefold*. "All of this only works because of the dollar's unique status. If that wanes, America will face a reckoning like none before."

Departing the dollar

At the instigation of the BRICS+ club (Brazil, Russia, India, China, South Africa), trade is increasingly conducted without using the US dollar for exchange purposes. China has just made its first purchase of energy from the Arab world using the Chinese yuan, and so has France! On 28 March, China National Offshore Oil Corporation and France's TotalEnergies announced their first yuan-settled liquefied natural gas deal, with a purchase from the United Arab Emirates, conducted through the Shanghai Petroleum and Natural Gas Exchange. This follows Chinese President Xi Jinping's December 2022 trip to Riyadh, where China and Saudi Arabia made progress in agreements to settle gas and oil trade in Chinese currency. ("China-Saudi agreements a marker of new economic system", *AAS*, 14 December 2022.)

A new China-Brazil arrangement to trade in local currencies was revealed at the Brazil-China Business Seminar in Beijing on 29 March. Photo: Screenshot

The same topic was discussed during Xi's trip to Russia last month, including trade in local currencies with Asian, African and South American countries. BRICS nations India and South Africa have declared their intention to increase the usage of local currencies for trade settlement. Much trade between Russia, China and India is already conducted without the dollar. A new report from independent European agency, the Centre for Economic Policy Research, shows that trade invoiced in Chinese currency now exceeds that conducted in euros, according to a 31 March article in London's *Financial Times*. The report heralds the emergence of a "multipolar" currency world.

On 28 March ASEAN finance ministers and central bank governors meeting in Indonesia discussed reducing dependence on the US dollar, euro, yen and British pound, by expanding the Local Currency Settlement scheme agreed to in November 2022. According to a report by ASEAN Briefing, Indonesia's banking regulator announced on 27 March that the Bank of Indonesia will be introducing its own domestic payment system. President Joko Widodo is encouraging use of local credit card systems rather than Visa and Mastercard, to shield the country from "possible geopolitical repercussions" in the future.

On 29 March the Brazilian government announced that China and Brazil had reached an agreement to settle trade payments in yuan. "An agreement on settling payments in yuan has been signed with Brazil, which greatly facilitates our trade", China's Vice Minister of Commerce Guo Tingting said 30 March. "We are planning to expand cooperation in the field of food and mineral extraction, and to search for a possibility of exporting goods with high added value from China to Brazil and from Brazil to China", he said. In January an agreement to establish a clearing house was reached, for currency settlements and lending in national currencies. China is Brazil's biggest trading partner.

On the sidelines of the Russia-Indian Business Forum held in New Delhi on 29-30 March, Deputy Chair of Russia's State Duma Alexander Babakov announced that a proposal for a "new currency" to serve a multipolar world will be presented at the BRICS Summit to be held 22-24 August in Durban, South Africa. He described the ongoing transition to settlements in national currencies as the first step in the process, and moves into digital currency as another. "I think that at the BRICS [leaders' summit], the readiness to realise this project will be announced, such works are underway", he said, adding that a new currency would be pegged to gold and "other groups of products".

US Treasury sell-up

Given this transition, and the financial and economic instability of the US economy, nations that have been major buyers of US debt, in the form of securities including US Treasury bonds, are increasingly moving out.

Brazil offloaded a monthly record US$21.5 billion of US Treasury bonds from its foreign currency reserves in March, almost equalling the US$22 billion it sold in 2022—which was close to 10 per cent of its total holdings.

China, which was the largest holder of US debt in 2013 with more than US$1.3 trillion worth of Treasuries, has reduced its total holdings by around 25 per cent. This has occurred via steady month-by-month reductions, amounting to a 17 per cent reduction in 2022, nearly US$175 billion worth. The decline continued in January 2023, for the sixth straight month.

Indicating that it is not only a matter of political allegiance, even the Bank of Japan sold off US$189 billion of its Treasury holdings in 2022, to diversify its foreign exchange reserves.

The fall of the hedge funds?

By Elisa Barwick

The rotten US Treasury market—the world's "single most important market"—is teetering on the brink of collapse.

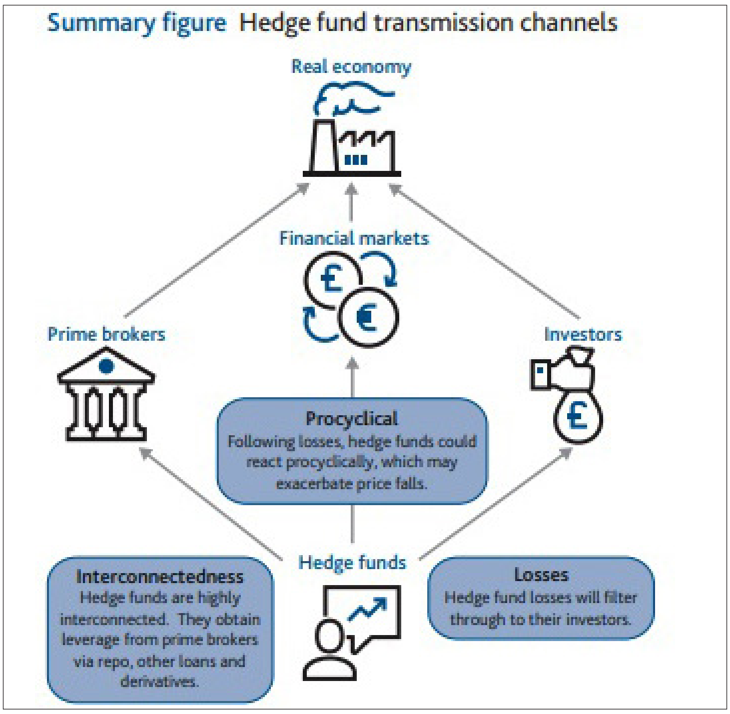
On 18 March, following the collapse of three US banks and amid general turmoil in bond and bond futures markets, big swings in money flows, and disruptions to trading in both the USA and Europe, the London *Financial Times* reported that "the most important market in the world went, to use the technical term, completely bananas. ... This time, the market reaction in Treasuries was nothing short of apocalyptic." Head of fixed income at Union Investment, Christian Kopf, is cited, saying that "the Treasuries market has become a 'hall of mirrors,' packed full of hedge funds trading blows with the Fed.... 'The most important market in the world is being dominated by a bunch of hedge funds,' says Kopf."

The *FT* article, by Katie Martin, was headlined, "The tumult in Treasuries: are hedge funds partly to blame?" The response to the bank collapses, she noted, catalysed "a bigger shock than in March 2020", when Treasury markets almost caved in. Kopf, she noted, "points the finger of blame at the sector he previously worked in: hedge funds." Hedge funds "are displaying far more muscle in the market than more traditional asset managers."

Hedge funds had positioned themselves to win in a high interest rate environment, but, wrote Martin, "When SVB [Silicon Valley Bank] sparked a search for safety in Treasuries, that bet took a hit. When it did, many hedgies were forced to close out their positions, effectively making them buyers of Treasuries. That blew up more negative bets, and forced more buying. It was a classic short squeeze, and a big one at that. It has left a string of big-name macro hedge funds wearing ugly losses. 'The most important market in the world is being dominated by a bunch of hedge funds', says Kopf."

Who put the hedge funds in control?

Since the 2008 global financial crisis the US debt market, which underpins the US dollar-based global financial system, has been completely white-anted. From no later than September 2019 it has been at the point of caving in. The rot started much earlier, however. From 1971 when President Nixon de-linked the dollar from gold, the post-Bretton Woods era saw new debt issuance increasingly dissociated from actual economic activity, which was tanking rapidly.



The potentially destabilising role of hedge funds in crucial financial markets was recognised even in a 2017 Bank of England report, "Hedge funds and their prime brokers: developments since the financial crisis". Photo: BoE

The post-2008 bailout set off changes that would make this dramatically worse, where US Treasuries themselves became the foundation for new speculative bubbles. The size of the Treasury market has increased four-fold since the global financial crash, but this rising debt was not only *not* backed by an equivalent increase in productive capacity, speculators were given free rein to deploy it as a tool to expand liquidity for their gambling activities. As *AAS* documented in "The rise of the hedge funds" (14 July 2021), hedge funds that specialise in trading risky financial derivatives were given a central role providing liquidity to the banking system through "repo" markets. Repo (repurchase) markets consist of short-term lending between financial institutions and "primary dealers" acting on behalf of the Fed, against collateral held in the form of Treasury bonds.

Hedge fund participation increased with regulatory changes in 2017 and further adjustments in early 2019, building up to the September 2019 repo market crunch when the Fed had to step in to provide daily cash injections. In its December 2019 Quarterly Review the Bank for International Settlements (BIS) warned that the big four US banks that dominate repo lending had shifted their reserves into Treasury speculation, holding 50 per cent of the Treasuries in the market. Because they take 1-2 days to settle, this sometimes prevented banks from readily lending into repo markets, hastening the rise of the hedge funds in the market. In turn, hedge funds increased derivatives speculation, noted the BIS, and therefore were themselves demanding more cash in the form of repos. It warned that a "sustained disruption" of the repo market "could quickly ripple through the financial system".

The hedge funds were running a "conveyor belt", wrote American investigative journalist Christopher Leonard in *The Lords of Easy Money: How the Federal Reserve Broke the American Economy*, "magically transforming bonds into cash". (See "Landmines in the graveyard of high finance", *AAS*, 16 Feb. 2022.) But they ended up losing big in March 2020 when betting on the difference between current Treasury bond prices and "futures contracts" on Treasuries. *AAS* reported: "As their bets on Treasuries went bad, hedge funds were desperate for cash and sold close to 20 per cent of their Treasury holdings, worsening the Treasury market dislocation. The impact flowed through other capitals markets, which seized up. The Fed had to intervene, purchasing billions of dollars of Treasury paper itself."

The US Federal Reserve issued a report in April 2021 on "Hedge Fund Treasury Trading and Funding Fragility", which reported on this market dysfunction. The Fed noted "the speed and scale at which extreme moves occurred and in its impact on otherwise safe and liquid markets such as the UST [US Treasury bond] market." The Fed admitted that a big part of the problem was allowing hedge funds to act as players in the repo markets, increasing the opaqueness of a market vital to financial stability. Hedge funds are less regulated than other money market dealers, said the report, employ substantial leverage, and deploy less liquid investment strategies. But the Fed was essentially admitting it had to intervene to save hedge funds, *to save the system*, given their interconnection.

The same month, independent Treasury bureau the Office of Financial Research (OFR) released "Hedge funds and the Treasury cash-futures disconnect", also pointing to the risks created by "non-bank actors in the current structure of the Treasury market". As Fed Chairman Jerome Powell made clear in a 28 April 2021 press conference, "the US Treasury market is probably the single most important market in the economy and the world. It needs to be liquid." Nevertheless, the Fed was still considering letting hedge funds borrow from the Fed's repo clearing house *directly* rather than via middlemen as they currently did. The *Wall Street Journal* admitted that this would amount to the Fed "backstopping their bets".

Despite all this turmoil, crunch time didn't really hit until the Fed started raising interest rates in March 2022. Then, the Treasuries piled on the banks' books became increasingly worthless (the market value of a bond moves in the opposite direction to rates). As deposits on their books shrank (drawn down by squeezed businesses for capital or by savers who weren't earning enough), banks like SVB were forced to sell Treasuries at a loss, leaving big holes in their balance sheets.

Numerous other reports from the BIS, IMF, World Bank and Fed warned of the impact of Fed policy tightening, including a loss of liquidity in US Treasury markets and the impact it would have on emerging market economies with large US dollar-denominated debts. But they didn't take seriously their own advice, and neglected to fully realise how it would impact the USA itself.

Even at this late stage the worst can be avoided by excising this speculative cancer.

Global majority follow China, Russia to exit neoliberalism

By Elisa Barwick

The neoliberal horror show being experienced by nations across the world, stands in stark contrast with the prospects of nations working closely with Russia and China on high-technology infrastructure development.

Take one current example of the destruction wreaked by neoliberal economic policy, in Greece. Commonly presented as a case of an overblown, overspending bureaucracy, the truth is becoming clear as that "bureaucracy" has been dismantled under the post-2008 global financial crisis era of austerity. The financial crisis was not the fault of the state but of the banking sector, which continues to wreak havoc on the nation. (Mark Blyth proves this in *Austerity: The History of a Dangerous Idea*, reviewed in articles in *AAS*, 1 and 15 Feb. and 15 March, available on our Economic Warfare webpage.) The horrific accident on 28 February, where at least 57 people were killed when two trains crashed head on outside Tempi, has brought the outrage of the population to the surface. Tens of thousands of people are showing up at protests sweeping the nation, demanding an end to *all* privatisation. The people must "break the government's narrative about 'human error'" being the cause of this tragedy, said rally organiser Panagiotis Bouros.

A train collision in Greece has sparked nationwide strikes and protests against privatisation. Photo: Screenshot

The actual cause is economic policy. As American Economist James K. Galbraith wrote in "The Austerity Train Wreck", published by Project Syndicate on 10 March, the private company that bought up Greece's railway operator for a song did "just what the profit motive demanded", cutting costs and shedding staff. In 2010 the operator had 6,000 staff; today there are only 800. No automated system existed to prevent two trains running towards each other on the same line, because of its cost. Extensive privatisations and budget cutbacks originated with the 2010 austerity program demanded as a condition of bailout loans. "To ensure that such safeguards are in place, the firm hand of regulation must override the profit motive", wrote Galbraith. The human error here lies not with the stationmaster, who faces a lengthy prison term, but "with those who devised, defended, and promoted the economic doctrines that have ravaged Greece."

Sophia McClennen, Professor of International Affairs and Comparative Literature at Pennsylvania State University, skewered the same issue, affecting even the most advanced nations, in an article published by *Salon* on 8 March. McClennan cited the 3 February train derailment in Ohio, and near-crashes between American airliners, remarking: "Today, like then, we are witnessing a form of collapse caused by neoliberalism. Collapsed buildings, collapsed bridges, collapsed railways. First neoliberalism made us broke. Now it's killing us."

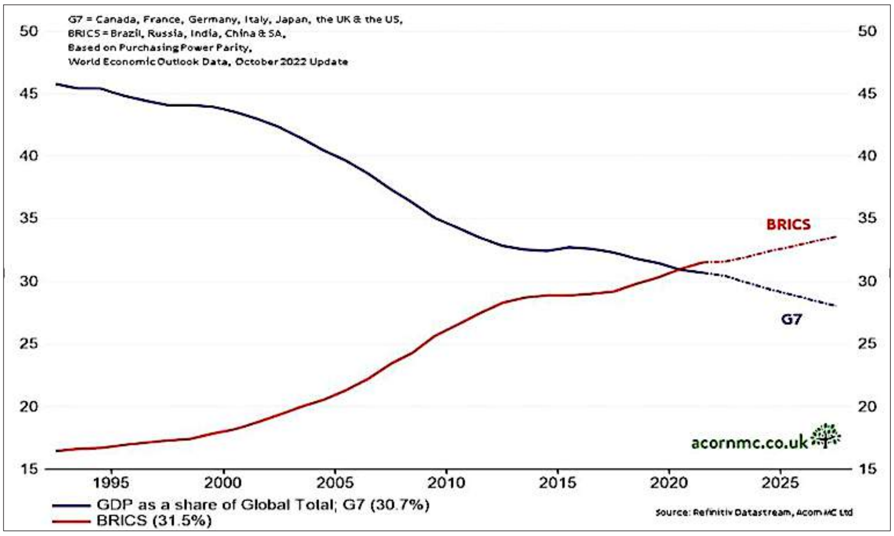
On the other hand, China is leading the way by example, showing how investment in infrastructure does not weaken a nation's finances, but rather is the only way to advance. IMF head Kristalina Georgieva, speaking at the 2023 China Development Forum in Beijing on 26 March, noted that the Chinese economy will "account for around one third of global growth in 2023—giving a welcome lift to the world economy". According to Turkish state-run news agency Anadolu, IMF research also indicates that China's "productivity enhancing reforms" equates to "higher quality and more inclusive" growth. Those that have worked closely with China, through the BRICS forum (Brazil, Russia, India, China, South Africa, and collaborating nations) or the Belt and Road Initiative (BRI), have seen the benefits of this too. The roster of nations wanting in is growing steadily. For many, it is the only sign of hope on the horizon.

In a 22 March *Consortium News* article, "G7 vs BRICS—Off to the Races", former UN weapons inspector Scott Ritter reported on the findings of founder of Richard Dias, of Acorn Macro Consulting, showing that BRICS has now surpassed the G7 nations in the portion of global GDP it produces, using figures adjusted to reflect the "purchasing power parity" of national currencies. (Graph, p. 8.) "BRICS was responsible for 31.5 percent of the PPP-adjusted global GDP, while the G7 provided 30.7 percent." BRICS is expected to surpass the G7 in absolute terms in coming years, wrote Ritter. (For more on PPP, see "Real economic metric shows no excluding Russia and China!", *AAS*, 27 July 2022.)

Xi in Moscow: replace war with development

Three days of talks between Chinese President Xi Jinping and Russian President Vladimir Putin, held in Moscow 20-22 March, put the foot on the "accelerator" in the call for all nations to work together to establish peace, said Chinese Foreign Minister Qin Gang. The two leaders announced a fruitful strengthening of their bilateral relationship, signing a Joint Statement on "Deepening Comprehensive Strategic Partnership for Coordination for the New Era." The Ukraine peace plan drawn up by China was discussed. Russia was supportive and expressed its commitment to resuming peace talks as soon as possible, but insists demilitarisation must be completed and that Ukraine agree to be a neutral, non-NATO state. The leaders called for the international community to recognise "the legitimate security concerns of all countries" in order to "to settle the Ukraine crisis". It is necessary, they said, to "update and improve the international security architecture", calling for urgent consideration of China's 12-point peace proposal for Ukraine. Referencing the grave danger of nuclear war, the leaders called on all other states possessing nuclear weapons to reiterate the inadmissibility of nuclear war.

US National Security Council spokesman John Kirby, on



BRICS overtaking G7 economies. Photo: Consortium News

19 March, revealed the intractability of the Anglo-American war party, however, declaring that "if coming out of this meeting, there's some sort of call for a ceasefire, well, that's just going to be unacceptable because all that's going to do … is ratify Russian's conquest to date."

An extensive development agenda was discussed, with energy security and new technologies central components. Progress was made for an early 2024 commencement of construction of the new Power of Siberia II gas pipeline connecting Russia and China via Mongolia. Agreements were signed for joint work on new nuclear power technology, including fast breeder reactor construction. Other high technology development focused on space research, transport and logistics corridors, new ports, and entirely new industrial chains. Increasing use of local currencies for trade and progression to a US-dollar alternative reserve currency framework was discussed.

Speaking to the media, Putin noted that "As of the end of the first three quarters of 2022, the share of the rouble and yuan in mutual commercial transactions reached 65 per cent and continues to grow, which allows us to protect mutual trade from the influence of third countries and negative trends on global currency markets." Andrei Kortunov, Director-General of the Russian International Affairs Council, told Chinese TV station CGTN that the leaders were signalling to agencies in both nations "that it's high time to roll up their sleeves and to convert the general political agreements reached at the highest level into specific plans and deeds".

Xi was in town on the tail of a Russia-Africa parliamentary forum on 19-20 March, "Russia-Africa in a Multipolar World", to discuss promising areas for economic cooperation in preparation for the second Russia-Africa summit to be held in St. Petersburg in July. At this conference Putin noted that Russia had forgiven over US$20 billion of African debt and said that "Africa will become one of the leaders in the emerging new multipolar world order".

Russia's initiative, like recent diplomatic manoeuvres by China, is not part of some hidden agenda but part of a vision for global cooperation, including by uplifting regions that are engulfed in war or poverty. In February, China unveiled its Global Security Initiative, then released its 12-point Ukraine peace proposal. It brokered a Saudi Arabia-Iran accord on 10 March, based on the mutual recognition of the need for economic development, since which time a spate of activity has ensued in the region. Already the Saudi and Iranian foreign ministers have spoken on the phone and Saudi King Salman has invited Iranian President Ebrahim Raisi to a meeting in Riyadh. The Saudi foreign ministry is reportedly now in talks with Syria about resuming diplomatic relations, after 11 years. Just days after the Iran-Saudi agreement, Syrian President Bashar al-Assad travelled to Moscow to discuss deals for reconstruction of the country, going on to visit the United Arab Emirates, the largest provider of humanitarian and relief aid to Syria since the earthquakes of early February, with discussions focused on economic cooperation and Syria's reintegration into the Arab community. Russia is working on rapprochement between Syria and Turkey.

On 19 March Iran's Supreme National Security Council Secretary, Ali Shamkhani, travelled to Baghdad to meet his counterpart, Iraqi National Security Advisor Qasim al-Araji, where a joint security agreement on border security was signed. According to reports, Iraqi Prime Minister Mohammed Shia' al-Sudani said that Iranian and Iraqi officials view their two countries as "united as one". Additionally, Russia appears to have brokered a peace treaty between Armenia and Azerbaijan. In an invitation to nations for the first China-Central Asia Summit to be held in May with Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan, President Xi presented a "grand plan" to match BRI programs with specific development visions for each nation. For example, the Turkmenistan development plan is called "Revival of the Great Silk Road."

On 22 March it was announced that Egypt has joined the New Development Bank founded by the BRICS in 2014. The Suez Canal Authority announced a US$2 billion deal the same day, for a Chinese firm to establish an iron and steel manufacturing complex in the Suez Development Zone.

Outside the scope of this article, South American countries are likewise clamouring for cooperation with China.

One way or another, "There's no turning back on the demolition of the remnants of Pax Americana", geopolitical analyst Pepe Escobar wrote on 22 March. Expressing well the intention of the two partners, and unnerving many political commentators, Xi told Putin at the conclusion of their Moscow summit that "there are changes that haven't happened in 100 years. When we are together, we drive these changes." Likewise Russian Foreign Minister Sergei Lavrov, in a 24 March article for *Razvedchik* ("Intelligence Officer") magazine, said, "We live at a time of historic geopolitical shifts." He cited Putin's words, that "A future world arrangement is taking shape before our eyes."


This photo with Xi's comment about "changes not seen for 100 years", sparked a furore. Photo: AFP/Sputnik/Pavel Byrkin