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Casino Banking: Wall Street Mega Banks Traded More in their Federally-Insured Bank than the Total for their Bank Holding Company

By Pam Martens and Russ Martens: October 13, 2022 ~

When something happens for the first time in history at federally-insured banks, Congress and federal regulators need to pull their heads out of the sand and pay attention. We're talking about the fact that in the second quarter of this year, trading revenues at federally-insured commercial banks eclipsed the trading revenues at bank holding companies – which typically include subsidiaries where traders actually *have licenses* to trade.

This latest data on what is happening inside the nation's largest federally-insured banks comes from the Office of the Comptroller of the Currency (OCC), see pages 2 and 3 here. The federally-insured banks generated a total of $10.3 *billion* in trading revenue in the second quarter versus $10.2 billion for the bank holding companies, or 101 percent of the bank holding company revenues. That's never happened before according to the data provided by the OCC.

The report provides the following historical perspective:

> "Before the 2008 financial crisis, trading revenue at banks typically ranged from 60 percent to 80 percent of consolidated BHC [Bank Holding Company] trading revenue. Since the 2008 financial crisis and the adoption of bank charters by the former investment banks [Goldman Sachs and Morgan Stanley], the percentage of bank trading revenue to consolidated BHC trading revenue has decreased and is typically between 30 percent and 50 percent. This decline reflects the significant amount of trading activity by the former investment banks that, while included in BHC results, remains outside insured commercial banks. More generally, insured U.S. commercial banks and savings associations have more limited legal authorities than their holding companies, particularly in the trading of commodity and equity products."

The OCC attempts to assign this unprecedented event to a decrease in trading in equity derivatives at the bank holding company. But Figures 15a and 15b in the Appendix of this report actually show equity derivative trading *moving* to the federally-insured bank in the second quarter. Figures 15a and 15b also show that 100 percent of trading in credit derivatives (the majority of which are credit default swaps) moved to the federally-insured bank in the first and second quarters of this year and out of the bank holding company. Credit default swaps are the most dangerous of the derivatives traded on Wall Street.

Trading does not belong in a federally-insured bank that is backstopped by U.S. taxpayers and that is holding the life savings of average Americans who put their money there because they can't afford to take risks. The banking collapse of the early 1930s grew out of depository banks being allowed to engage in speculative trading on Wall Street. The runs on banks that followed the 1929 stock market crash and its aftermath led to thousands of banks failing.

In 1933 the U.S. Congress brought this form of casino banking to an end with the passage of the Glass-Steagall Act. It banned the combination of Wall Street trading houses with deposit-taking banks and created federal deposit insurance for commercial banks to restore the public's faith in banking and stop the runs on banks. Glass-Steagall served the country well for 66 years until its repeal under the Wall Street-friendly Bill Clinton administration in 1999. It took just nine years after its repeal for Wall Street to collapse in 2008, in a replay of 1929.

The financial crash of 2008 would have ushered in another Great Depression except for the Federal Reserve secretly stepping in with a $29 trillion bailout. The Fed Chairman who just received a Nobel Prize in economics for his work during the 2008 financial crisis, Ben Bernanke, is the same man who battled the media in court for more than two years, rather than come clean with the details of this unprecedented bailout of – not commercial banks that finance the real economy – but Wall Street trading houses such as Citigroup, Morgan Stanley and Merrill Lynch that finance speculators. Bernanke was, in reality, bailing out his and the Fed's failure to competently regulate these casino banks before they blew themselves up. Does that really deserve a Nobel Prize?

But we do not have to go back to the 1930s to understand what can blow up when federally-insured banks take on improper trading risks. In 2013 the Senate's Permanent Subcommittee on Investigations released a 300-page report on JPMorgan Chase's London Whale scandal. That case involved deposits at the federally-insured bank being used to trade exotic derivatives in London and losing $6.2 billion of depositors' money along the way.

The Chair of the Senate Subcommittee at the time was the late Senator Carl Levin. He said this about the matter:

> "JPMorgan's Chief Investment Office rapidly amassed a huge portfolio of synthetic credit derivatives, in part using federally insured depositor funds, in a series of risky, short-term trades, disclosing the extent of the portfolio only after intense media exposure."

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> "This case represents another shameful demonstration of a bank engaged in wildly risky behavior. The 'London Whale' incident matters to the federal government because the traders at JPMorgan were making risky bets using excess deposits, portions of which were federally insured. These excess deposits should have been used to provide loans for main-street businesses. Instead, JPMorgan used the money to bet on catastrophic risk."

If you care about the stability of the U.S. financial system, pick up the phone today and call your Senator and demand hearings on the speculative trading that is taking place in the nation's federally-insured banks.

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