

Too big to resist: Wall Street's comeback



Edward Luce

There will be another crisis. No law can stop it, no regulator can foresee it

When Washington is on the brink, who has the clout to persuade legislators to keep government open? The obvious answer is the US president. A better one is [Jamie Dimon](#), chief executive of JPMorgan Chase. With last week's vote in doubt, Mr Dimon helped to arm-twist Congress to [pass a bill](#) to keep the Federal government running for most of next year. What a splendid public service, I hear you say. In fact, his motive was more specific. The bill included an unrelated item allowing banks to resume derivatives trading from their taxpayer-insured arms. That ban is now history. Who other than a Wall Street titan could demand — and receive — such a service?

More than six years have passed since the collapse of Lehman Brothers triggered a global meltdown. Never again would Wall Street be allowed to write the rule book for itself, said Washington. To some degree, its wings were clipped. Big banks lobbied fiercely against parts of the 2010 Dodd-Frank reform act. In many cases they failed. Thus, Washington now has a consumer financial protection agency. The [Federal Reserve](#) has imposed a ceiling on Wall Street's leverage ratios. Banks must put many types of derivatives through a central clearing house. Under the Volcker rule they must keep proprietary trading separate from their deposit taking mother ship.

Many of these reforms count as progress — particularly the leverage limits. Moreover, in some cases Wall Street has reason to complain about over-reach. Banks are not special pleading when they point to the escalation in regulatory costs since 2010. Washington has more financial regulators than sense. Often they are penny wise and pound-foolish. Banks' compliance departments have swollen to keep pace with an avalanche of micro-regulations that few believe will do anything to reduce overall risk. The aftermath of 2008 is by no means a simple tale of Wall Street running rings around Washington. Yet — as Mr Dimon's intervention showed — high finance is recapturing whatever sway it lost.

The problem originated with the crisis. When the system was collapsing in 2008, Washington did whatever it took to prop it up. Timothy Geithner, Barack Obama's first Treasury secretary, ignored those he called the Old Testament fundamentalists who demanded big banks be liquidated and their chief executives put on trial. Such medicine would have been worse than the disease. Mr Geithner and his colleagues made up the rules as they went along to prevent a collapse that would have plunged the world into depression. Their forbearance was pragmatic. Unfortunately, they retained it long after the crisis receded. It was right to let Citigroup stay in business in

2009, even though it was effectively bankrupt. But should it be so much larger than it was six years ago? Is it healthy that Citi lobbyists wrote the clause, almost word for word, that was tucked into last week's spending bill?

The question answers itself. It also points to two glaring deficiencies that will come back to haunt Washington when the next crisis strikes. The first is that the "too big to fail" banks are considerably larger than when they were bailed out. The US financial system is far more concentrated than it was in 2008. The big four, JPMorgan, Citi, Bank of America and Wells Fargo, account for 68 per cent of US deposits and an even higher share of US derivatives trading. Apologists say the crisis began with investment rather than commercial banks. That is technically true. It nonetheless engulfed Citi, Chase Manhattan and others. Even the most blue-chip investment banks, such as Goldman Sachs, came perilously close to disaster. Can any regulator be sure they know what is on Goldman Sachs' books?

Second, there has been no improvement in Wall Street's culture — or in Washington's revolving door habits. Bankers dismiss Elizabeth Warren, the Democratic senator from Massachusetts, as a populist. Perhaps they should listen to Bill Dudley, president of the New York Federal Reserve and a former Goldman Sachs partner. In a speech last month, Mr Dudley said banks must either change their unethical culture or face being broken into smaller entities. Remember the Goldman trader who revealed the bank refers to clients as "muppets"? Though frequently observed in the breach, even journalists have a code of conduct. No code applies to Wall Street. The problem stems from the "barrel makers" themselves, said Mr Dudley — not a few bad apples. "The pattern of bad behaviour did not end with the financial crisis," he said.

At some point there will be another Wall Street crisis. It could be a decade away, or maybe next year. Markets run in psychological cycles in which fear gives way to greed and then hangover. Greed is once more in the ascendant. No law can stop the next bomb from detonating. No regulator can foresee it. But they could do much more to be ready for it when it comes. Here Mr Geithner's moral fundamentalists have a point. Last week's spending bill contained another item that had nothing to do with keeping government open. This one upped the limit on how much an individual can give to a political party — it now exceeds \$700,000. No prizes for guessing which sector of the US economy is the largest electoral donor. None, either, for which is most able to mould regulations to its taste.