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B'nai B'rith implicated in killing of Lincoln
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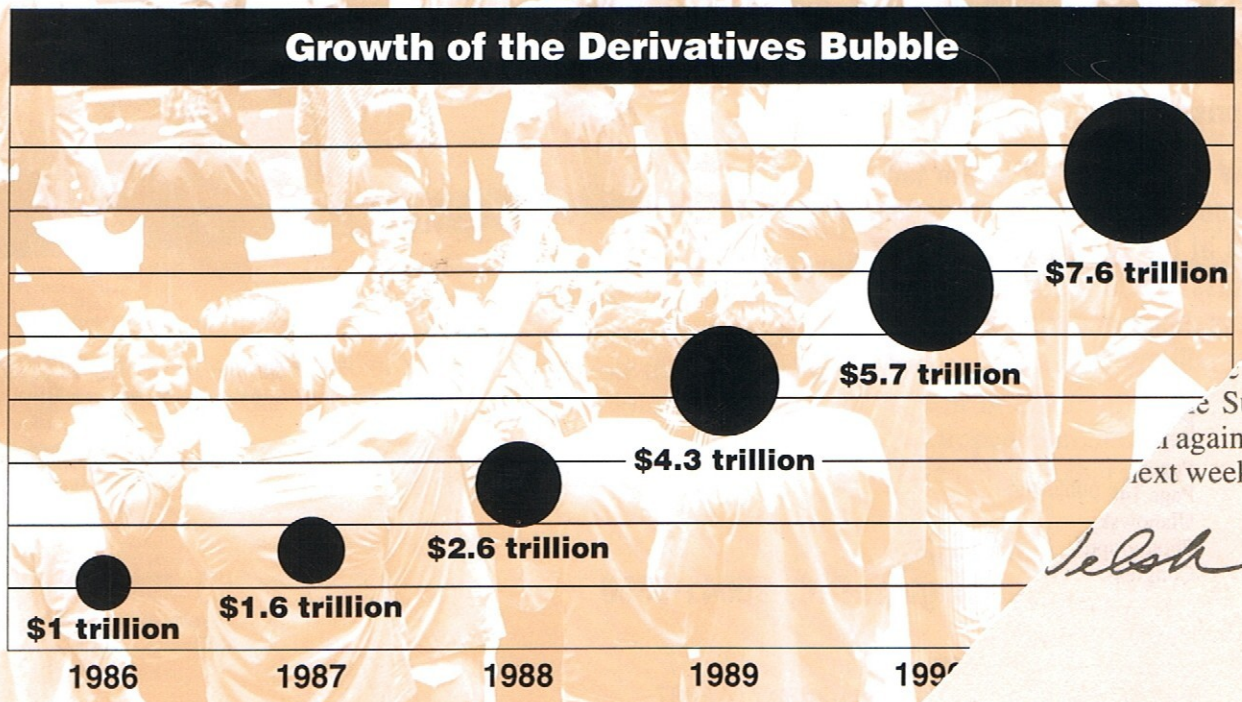


Finding a cure for derivatives, the market cancer

by Chris White

This *Feature* presents some materials related to the background of so-called financial derivatives, and to jailed economist Lyndon LaRouche's proposed 0.1% sales tax on each such transaction (see page 34).

For clarity's sake at the outset, the following ought to be understood, as background to our assessments of current and recent volume of trading in derivatives, and the effect of the proposed tax. This, because in addition to the revenue-raising potentials of the tax, LaRouche also insisted that the imposition of such a tax would contribute to bringing out-of-control, speculation-driven markets under proper executive control. The imposition of the tax would help reveal the problems to be encountered in doing such a cleanup. Here are some of the problems, and thus some of what has to be brought under control:

1) The bulk of such trading, as is profiled below, the so-called "over-the-counter" segment, is blatantly illegal under present U.S. law. Under standing provisions of the Commodity Exchange Act, it is illegal for banks, or anyone else, to deal in futures contracts outside of commodity exchanges. This is never mentioned publicly by any of the partisans of derivatives. "Over-the-counter" derivatives are only traded safely at this time because of the work of the former chairman of the Commodity Futures Trading Commission, Wendy Gramm (wife of the loud-mouthed priest of financial orthodoxy Texas Sen. Phil Gramm), who was given the right to "waive" existing law.

2) All treatments of derivatives, generated from within the financial and regulatory communities, distinguish between exchange-based and "over-the-counter" trading between banks, as if they were completely separate activities. The distinction is fraudulent. "Over-the-counter" derivatives—for example, a swap between a floating-rate Swiss franc-denominated instrument and a fixed-rate dollar instrument—are consummated and put into effect through exchange-based trading of currency, bond, and interest rate futures and options. The degree to which the growth of the $1 trillion per day foreign exchange market, or the $300 billion per

America's vast, rotted-out industrial and transportation infrastructure surrounds the great financial centers, such as New York's Lower Manhattan here, where it's considered cheaper to ruin the economy, than it would be to save it.

day market in U.S. government securities, is conditioned by trading generated as a result of illegal inter-bank "swaps," is unknown.

For these reasons, it is impossible to estimate, to any acceptable degree of accuracy, what the size of the legal market is which would be subject to the tax. And obviously, one would not want to legitimize what is already outside the law, by subjecting such crimes to a tax.

3) Leaving the matter of crime aside, trading volumes, and the rate of turnover of the contracts traded—i.e., the actual, not the notional maturity of the instruments traded—are likewise unknown. This makes *EIR's* previously relatively high estimates of the effect of the proposed tax, and our presently relatively low estimates, equally suspect. They should be understood as hypothetical extremes. The more so, given the fact that the bulk of such trading is flatly illegal. For example:

- No reporting of derivative exposure by banks includes instruments with maturities of 14 days or less; yet the purpose of bank swap arrangements, for example, is to transform nominal medium- and long-term maturity instruments into short-term instruments, such that daily trading subserves a contract which is renegotiated every three months.
- No consolidated accounting exists of activities by bank holding companies and all their subsidiaries, or by so-called non-bank financial companies—e.g., GE Capital Corp. and General Motors Acceptance Corp (GMAC). Volume estimates are based either on particular banks' activities, or on activities of holding companies as such. The reports for both cover different time-frames. They are neither complete, nor are they compatible. Non-deposit-taking lending institutions (non-bank banks in the present parlance) are not covered at all, because they are not regulated.

Without considering the provisos stated above, the derivatives market, or series of markets, is estimated at some undetermined part of $16 trillion—the same order as the total financial and tangible assets in the U.S. economy as a whole, according to the Federal Reserve's balance sheet of the U.S. economy. How could such an immense market have come into existence in defiance of existing law?

How does Jack Kervokian continue to get away with murder in the name of "assisted suicide"? The two questions are not so different. With trillions of dollars of liabilities accumulated illegally, it would not be credible to simply say that someone must have been asleep at the switch.

Investigate the Federal Reserve

To find out the truth, it would be sufficient to mount a real investigation of what the Federal Reserve has been doing since 1978, and, specifically, what the Federal Reserve Bank of New York has been doing. The Federal Reserve is supposedly responsible for monetary policy, and through its discount window operations helps set the interest rates which govern the yields sought by the derivatives operators.

Such an investigation ought to focus on three areas:

1) Narrowly, how has the Federal Reserve has interpreted its regulatory mandate over stock index futures markets, and

how and why was the Federal Reserve given such a mandate in the first place?

2) More broadly, what does the Payment and Settlement Committee of the Federal Reserve Bank of New York actually do, and what role does the Federal Reserve play in its work?

3) What is the effect of Federal Reserve involvement in derivative-driven markets on credit generation, the banking system, and the economy as a whole?

4) What is the extent of criminal collusion between the Federal Reserve Bank of New York and the eight commercial banks which account for 90% of the activity in "over-the-counter" derivative transactions? The Federal Reserve Bank of New York is owned by the same banks which have systematically been violating the Commodity Exchange Act.

The broader purpose of a cleanup to reimpose order is straightforward:

1) So long as present methods of organizing credit flows within the economy and financial system are continued, there will be no prospect of economic recovery, nor a feasible job creation program, nor any capital- and technology-intensive renewal of the economy.

2) Derivative markets—options, futures options, options indexes, swaps, strips—whether on or off exchange, given the rate of growth in their international volume and turnover, especially in currencies and bonds, have become key in setting financially "acceptable" rates of return, thus interest rates, and thus overall credit flows.

3) Bush administration policy and Alan Greenspan's Federal Reserve commitments to avoid at all costs the spillover of the savings and loan banking crisis into the nation's commercial banks, by increasing spreads between bank lending and borrowing, made the problem much worse than it would otherwise have been. Returns from commercial and industrial loans cannot match the derivative-enhanced yield on the tax-free 4-5% spread they have been given in recent years.

4) To organize a recovery is to create *new wealth*. New wealth can only be created by putting Americans back to work in modern infrastructure construction projects, necessary to support expansion in employment and economic activity, and in technologically progressive capital goods industries, to increase productivity. This increases the tax base without increasing tax rates, and thereby reduces the deficit. Every 1 million jobs created at $30-40,000 per year gross will add between $5 and $6 billion to the Treasury's personal taxation revenue stream directly, and will obviously have quite dramatic additional indirect effects.

5) Unfortunately, the time-frame for achieving project viability, and the discounted present cash value of the returns on such investments, cannot compete with the derivative money-go-round. Therefore, either derivatives and their users submit to an exercise of national will, or the country submits to the continued rule of those who employ derivatives, in violation of its very laws.

Derivatives: What are they?

by Anthony K. Wikrent and Chris White

The textbook definition of a financial derivative is a financial instrument, the value of which is based on the value or values of one or more underlying assets or indexes of assets. Derivatives can be based on equities (stocks), debt (bonds, bills, and notes), currencies, and even indexes of these various things, such as the Dow Jones Industrial Average. Derivatives can be sold and traded either on a regulated exchange, such as the Chicago Board of Trade, or off the exchanges, directly between the different counterparties, which is known as "over-the-counter" (OTC). The textbook explanation of the purpose of derivatives is that they serve to reduce the risk inherent in fluctuations of foreign exchange rates, interest rates, and market prices. Derivatives traded on exchanges also are said to serve as a "price discovery" mechanism.

According to the Bank for International Settlements' October 1992 report, *Recent Developments in International Interbank Relations,* "swaps" are the largest type of derivatives, as measured by the *notional prinicpal amount* outstanding (**Table 1**).

A generation or so ago, the matter of what derivatives are might have been adequately summarized by contrasting the difference between investment, on the one hand, and gambling or speculation, on the other.

The instruments which "underlie" derivatives—stocks, bonds, commodities, money—represent a claim, usually through ownership, on wealth produced in the economy. Such claims can be purchased. Thus, shares in a company can be bought, as can bonds issued by governments or corporations, or hard commodities produced by agriculture, forest industries, or minerals extractors and refiners.

The instrument so purchased provides a means by which the wealth produced may be turned into money. In the case of stock, this may take the form of the company's dividend payment, the part of after-tax profits distributed to shareholders, or it might take the form of capital gains realized through the appreciation of the stock's value. Formerly, such monetization, or potential for monetization, would have been more or less directly related to the economic performance of the company, in contributing to an increasing overall rate of wealth generation through productivity-enhancing increases in the powers of labor. So too are bonds directly related to

economic activity, though where stocks represent equity ownership, bonds represent indebtedness. The interest paid corresponds, more or less, to the dividend yield of a stock. Moreover, like stocks, bonds can provide capital appreciation.

A generation ago, such financial instruments were the means for transforming economic surplus into monetized net profit. "Hard" commodities are different, because they are part of the materials-flow needed to sustain production and consumption, which ought to be bought and sold so that production might proceed—outputs of production on the one side, are also the inputs for the next level of productive transformation on the other: Wheat becomes flour, flour becomes bread; iron ore becomes steel, steel becomes machinery, buildings, automobiles, and household appliances. Such activities used to contribute to generation of surplus, but their monetization is not part of after-tax profits.

Purchases of stocks and bonds would once have been seen as investment for the long haul. Trade in commodities would have been seen not as investment, but as purchases and sales.

With what are now called derivatives, we move from investment, and purchases and sales of hard commodities, to speculating on the future price or yield performance of what were once investments, and relatively simple, economically necessary transactions.

All derivatives are actually variations on futures trading, and, much as some insist to the contrary, all futures trading is inherently speculation or gambling. Thus until late in 1989, all futures trading, of any sort, was outlawed in Germany, under the country's gambling laws. Such activities were not treated as a legitimate part of business activity. And, who will contend against the observation, that Germany did quite well without them?

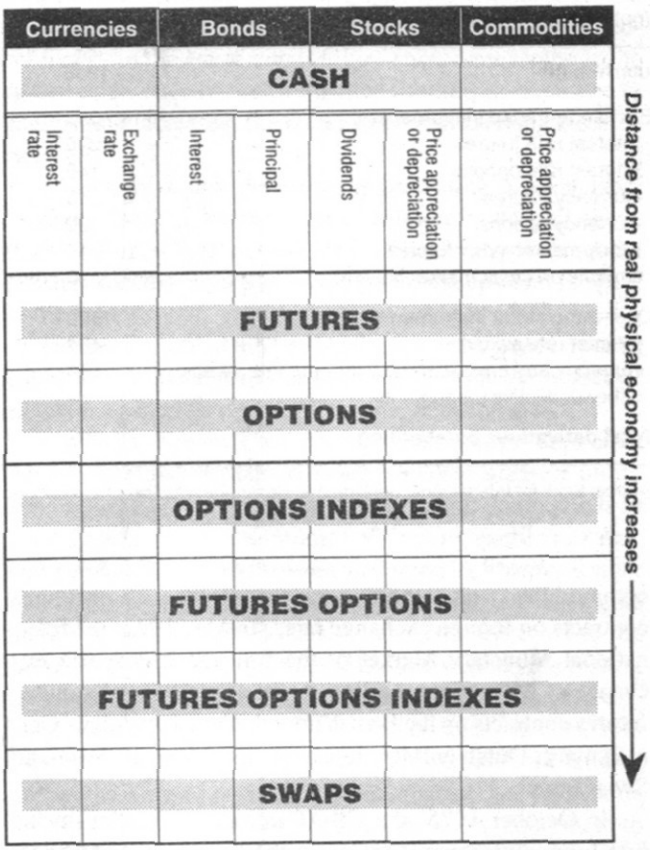
There are two types of futures trading; each can be applied to each of the instruments, like stocks and bonds, which, bought directly for cash, monetize what used to be after-tax profits. The first type is, as it were, a second step removed from economic activity as such. This is futures trading per se: contracting to buy or sell at a future date, at a previously negotiated price. Here the presumption used to hold, that commodities, for example, would actually change hands for money, as the agreed-on contracts fell due.

The other kind of futures contract, called an option, moves another step further away from economic activity as such. Now what is bought or sold is the right, but not the obligation, to buy or sell a commodity, stock, bond, or money, at a future price on an agreed-on date.

Where the futures contract speculates on what the price that would have to be paid against delivery will be, the option simply speculates on the price.

At yet another remove from economic activity per se is an index. An index is not the right to buy a commodity or stock in the future which is traded, but the future movement of an index based on a basket of stocks, commodities, bonds, or whatever.

Hierarchy of financial transactions



As one proceeds downward in the chart, transactions have increasingly less bearing on processes in the real physical economy.

Futures contracts

In the U.S., futures contracts on corn, oats, and wheat began to be traded on an organized exchange, the Chicago Board of Trade (CBOT), in 1859. "Notional principal amount" refers to the value of the underlying assets in a futures contract. For example, in a corn futures contract to take future delivery of 5,000 bushels three months hence, the notional principal amount of the contract would be the price of a bushel of corn times 5,000. If the price of corn were, for example, $2.00, the notional principal value of the corn futures contract would be $10,000. But the actual price of the contract, however, is the *margin* set by the exchange; the CBOT, for example, requires $270 be paid to purchase a futures contract that on May 15 had a notional value of $11,637.50.

Since financial deregulation in the 1970s, futures contracts have been developed for things that are not assets or

TABLE 1

Derivatives markets exploded in late 1980s

(notional principal amount outstanding at year end, billions $)

Instrument	1986	1987	1988	1989	1990	1991
Exchange-traded instruments	$ 583	$ 725	$1,300	$1,762	$2,284	$3,518
Interest rate futures	370	488	895	1,201	1,454	2,159
Interest rate options	146	122	279	387	600	1,072
Currency futures	10	14	12	16	16	18
Currency options	39	60	48	50	56	59
Stock market index futures	15	18	28	42	70	77
Options on stock market indexes	3	23	38	66	88	132
Over-the-counter instruments	500	867	1,330	2,402	3,451	4,080
Interest rate swaps	400	683	1,010	1,503	2,312	2,750
Currency and cross-currency interest rate swaps	100	184	320	449	578	807
Other derivative instruments	–	–	–	450	561	577
Total derivatives outstanding	**1,083**	**1,592**	**2,630**	**4,264**	**5,735**	**7,598**

Source: Bank for International Settlements, *Recent Developments in International Interbank Relations,* Basle, Switzerland, October 1992.

commodities. The first move was the introduction of futures contracts on foreign exchange rates. In May 1972, the International Monetary Market of the Chicago Mercantile Exchange (CME) began trading in the first financial futures: futures contracts on the British pound, Canadian dollar, German mark, Dutch guilder, Japanese yen, Mexican peso, and Swiss franc.

In October 1975, the CBOT introduced trading in the first futures on interest rates, on the Government National Mortgage Association's (GNMA) mortgage-backed certificates. In January 1976, the CME began futures trading in 90-day U.S. Treasury Bills. Trading in futures contracts on 15-year U.S. Treasury Bonds began on the CBOT in August 1977. Trading in such interest rate futures, as they are called, quickly grew to become the most heavily traded futures contracts in the world. On the CBOT, trading in Treasury bond futures and options has risen from 28.3% of total volume in 1981, to 64.4% of total volume in 1991.

In February 1982, futures contracts for *indexes* of asset values began trading, with the introduction of futures contracts based on the Value Line Average Stock Index, on the Kansas City Board of Trade. Two months later, the CME began trading in the Standard and Poor's 500 Stock Price Index, which is now one of the most heavily traded futures contracts at the CME. Trading in this contract is considered so important, that the CME set up a special room in a different building to allow continued trading in the S&P 500, when the CME was forced out of its building by the flooding waters of the Chicago River in May 1992, closing trading in all other futures contracts. Not coincidentally, the S&P 500 Stock Price Index futures contracts is one of the instruments the U.S. Federal Reserve has reportedly used since October 1987 to reverse collapses on the New York Stock Exchange.

Other derivatives

There are other types of derivatives which are not traded on exchanges but are negotiated between contracting parties, usually large banks. These are called "over-the-counter" instruments. "Swaps" are designed to transform a nominally long or medium-term contract into a succession of shorter-term maturities.

For example, swapping a floating rate Swiss franc-denominated obligation for a fixed-rate dollar instrument between banks, involves the Euromarket, the currency markets, the swap market, and perhaps also the interest rate futures and/or options markets. The intrepid might want to try to calculate how far we now have moved from the first level of cash purchases of stocks and bonds.

An *interest rate swap* is a transaction in which two counterparties agree to exchange two different types of interest payment streams based on an underlying notional principal amount. For example, assume that a bank with a portfolio full of adjustable rate mortgages (ARMs) wished to receive an income stream of fixed-rate interest payments. The bank would package together, say, $10 million of such mortgages, all paying interest currently at 6.5%, and exchange the ownership of the interest payment stream from that package of ARMs with a corporation that would give the bank in return the ownership of an interest payment stream fixed at, say, 8%. The notional principal amount of the swap would be $10 million, but the actual amount of money that exchanges hands would be limited to the interest payments each counterparty owed to the other over the life of the swap.

Swapping of interest rates is said to have begun in connection with the Eurobond market in the early 1980s, when high interest rates dictated that only the highest quality borrowers could qualify for long-term, fixed-rate financing.

Borrowers of lesser quality, who were excluded from such financing, were able to obtain it indirectly through swaps.

However it was not until the U.S. Student Loan Marketing Association (Sallie Mae), began using swaps in 1982, that they began to be widespread. Sallie Mae was seeking a way to avoid having to borrow longer-term, higher-priced funds, to lend out for shorter terms at lower rates. The swaps used by borrowers in the Eurobond markets proved to be the perfect vehicle for Sallie Mae, which, as a quasi-government agency, is perceived by the markets to be an extremely high-grade borrower. The first swap for Sallie Mae was arranged through an investment bank in the summer of 1982, with ITT as a counterparty. ITT reportedly saved 17 basis points (17/100 of 1%) in borrowing costs in the deal.

Currency swaps

Currency swaps have been used by central banks for decades. The Bank of England, for example, would receive a set amount of dollars from the U.S. Federal Reserve in exchange for a set amount of pounds, in order to have dollars to use on the foreign exchange markets. After a period of time, the Bank of England would return the dollars to the U.S. Federal Reserve, and receive back its pounds. The accepted definition of a currency swap is a transaction in which one counterparty exchanges its principal and cash flows denominated in one currency, for the differently denominated principal and cash flows of another counterparty. At an agreed upon future date, the two counterparties close out the transaction by reversing the swap of the principal.

In the 1970s, a small number of currency swaps were arranged that were not related to central bank activity. A U.S. dollar/French franc swap, for example, was arranged for the Republic of Venezuela to help meet payment obligations arising from the construction of a commuter rail system in Caracas. The details of these swaps were largely kept from the public view, for fear of disclosing proprietary operating information.

After the debt bomb exploded when Mexico threatened a debt moratorium in 1981, however, the World Bank widely publicized a swap arranged by Salomon Brothers between itself and IBM. The motivations of the World Bank and IBM to conclude the transaction made the swap exceptional at the time. The World Bank was seeking to maximize the rate of interest on its debt, and IBM was seeking to hedge its Swiss franc and German mark debt, while at the same time capturing a paper profit from the appreciation of the dollar against both currencies. As Michael Wood, senior manager of International Financial Markets at Dresdner Bank in Frankfurt, noted in the 1992 textbook *Cross Currency Swaps*, by Lehigh University professor Carl Beidleman, it was "the first time that a currency swap was used to arbitrage between capital markets, that is, where a capital market issue was done solely for the purpose of swapping into another currency."

And then there are caps, floors, and collars, options on the anticipated interest rate movements which make up the swap:

Caps, in which the buyer will receive from the seller the difference between current interest rates, and some agreed-upon rate, in the event interest rates should move above the agreed upon rate. In return for thus limiting its exposure to interest rate increases, the buyer pays to the seller a onetime fee.

Floors, in which the buyer is protecting himself from decreases in interest rates. That is, if interest rates fall below an agreed-upon level, the seller is obligated to make up the difference to the buyer, in exchange for the up-front fee paid by the buyer.

Collars, in which the buyer of a cap simultaneously sells a floor at the same time, or vice versa, with the object of maintaining interest rates within some defined band.

Currency forwards are perhaps the simplest derivative instruments, and perhaps the one with the greatest utility for companies involved in producing and shipping goods in foreign trade, given the insanity of floating exchange rates. Assume that Boeing has sold an airliner to Lufthansa. Rather than go through the trouble of converting the deutschemarks paid by Lufthansa into dollars—and being subjected to the risk of changing exchange rates if Lufthansa is paying Boeing back over a period of time—Boeing pays a fee to an intermediary (a swap dealer) to find a German company that has sold something in the United States that is of comparable value to the Boeing airliner purchased by Lufthansa. Let us assume that Siemens has sold some power-generating equipment to a U.S. utility. Under a currency forward, the utility that had bought equipment from Siemens, will pay dollars to Boeing instead of Siemens, and Lufthansa will pay deutschemarks to Siemens instead of Boeing. In other words, Boeing gets Siemens's U.S. income stream in the United States, in exchange for which Siemens gets Boeing's deutschemark income stream in Germany.

Thus, the definition of a currency forward is a contract in which two counterparties agree to exchange differently denominated income streams at an agreed upon exchange rate at some point in the future. There is no swapping of principal involved.

Within the United States, the entire "over-the-counter market" is quite illegal, since by the current version of the Commodity Exchange Act, banks and related agencies are prohibited from engaging in off-exchange futures contracts. Thanks to Sen. Phil Gramm's wife Wendy, former head of the Commodity Futures Trading Commission, regulatory agencies have successively undermined that exclusion through so-called interpretation and exemption, just as the earlier prohibition of options was undermined, or just as the 1930s Glass-Steagall Act, which divided U.S. banks into two, mutually exclusive types—commercial banks and investment banks—is now being disregarded, even though it remains on the books.

How financial derivatives became the world's fastest-growing market

by Anthony K. Wikrent, Richard Freeman, and John Hoefle

According to the October 1992 report of the Bank for International Settlements, *Recent Developments in International Interbank Relations*, "since the mid-1980s, the growth of turnover and of volumes outstanding in markets for derivatives instruments, including over-the-counter (OTC) markets that offer more customized products, has outpaced the growth of most other financial activity." As seen in **Figure 1,** by 1988, the "notional principal amount" (referring to the value of underlying assets) of derivatives outstanding had exceeded the total market capitalization of the New York Stock Exchange. By 1989, the notional value of derivatives outstanding was almost one-third larger than the total market value of all publicly listed companies in the United States. By the end of 1991, the notional value of derivatives was soaring toward being double the market capitalization of all U.S. publicly listed companies.

In other words, if the phenomenal growth rate derivatives exhibited from 1986 to 1991 has continued in the past two years, *the amount of derivative paper outstanding*—none *of which is carried on corporate balance sheets—is now somewhere around twice the total market value of all publicly listed companies in the United States.*

That financial derivatives have grown to such an extent is all the more amazing, considering that these instruments simply did not exist 25 years ago. The largest single type of derivatives, interest rate swaps, did not get off the ground until the summer of 1982. Futures on currencies did not come into use until May 1972. Interest rate futures first came into being in October 1975.

Oddly enough, there are no official figures available for the *dollar volume* of futures trading in the United States. Not even the Commodities Futures Trading Commission, the federal government agency charged with regulating the futures markets, has figures for the dollar volume of futures trading. Neither do the Chicago Board of Trade or the Chicago Mercantile Exchange, the two largest futures exchanges. The only figures available are for the number of contracts traded (**Figure 2**).

By multiplying the number of contracts traded of a certain basic type—agricuultural commodities, precious metals, energy products, currencies, and financial products—by an average price for each basic type, *EIR* has estimated that the U.S. futures markets have an annual turnover of around $25 trillion. This is a major revision from *EIR*'s original estimate of $152 trillion, published in December 1992. Still, it demonstrates that the futures markets dwarf the New York Stock Exchange, which had a market capitalization of $3.713 trillion, and total value of shares traded of $1.520 trillion in 1991.

The futures markets are also some five times larger than the U.S. Gross National Product, which was $5.519 trillion in 1991.

These gigantic markets are highly concentrated, with a mere handful of firms completely dominant. A report by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corp., and Office of the Comptroller of the Currency, *Derivative Product Activities of Commercial Banks*, issued on Jan. 27, 1993, revealed that the ten largest commercial banks in the U.S. control 95.2% of all derivatives activities by U.S. commercial banks (**Figure 3**).

The same situation probably exists on the investment bank side. In a listing of the 40 largest institutions in the futures markets, ranked by customer equity (the futures markets define equity as the residual dollar value of a futures account, assuming it were liquidated at prevailing market prices), in the March 1993 issue of *Futures* magazine, the five largest were investment banks: 1) Merrill Lynch Futures, Inc. ($2,176.9 million); 2) Goldman Sachs and Co. ($1,581.3 million); 3) Shearson Lehman Brothers, Inc. ($1,527.7 million); 4) Dean Witter Reynolds, Inc. ($1,120.1 million); and 5) Prudential Securities, Inc. ($1,106.1 million).

These were followed by 6) Refco, Inc. ($1,071.3 million); 7) Morgan Stanley and Co. ($844.7 million); 8) Cargill Investors Service, Inc. ($804.5 million); 9) Daiwa Securities America, Inc. ($588.5 million); 10) PaineWebber Inc. ($576.2 million); 11) Bear Stearns Securities Corp. ($539.4 million); and 12) Salomon Brothers, Inc. ($488.6 million).

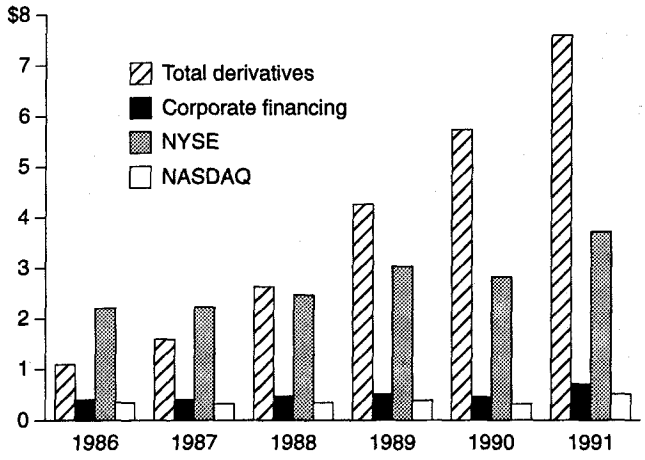
Of these firms, the three with the largest net adjusted capital (the amount of liquid capital established by Commodities Futures Trading Commission capital requirements) were Salomon Brothers ($999.6 million), Goldman Sachs ($963.6 million), and Shearson Lehman ($859.4 million).

EIR's revision of its estimate of the size of the futures markets means that the largest market in the world remains the foreign exchange, or currency, markets. In March, the Bank

FIGURE 1

Derivatives compared to U.S. corporate financing and stock market capitalizations

(trillions $)

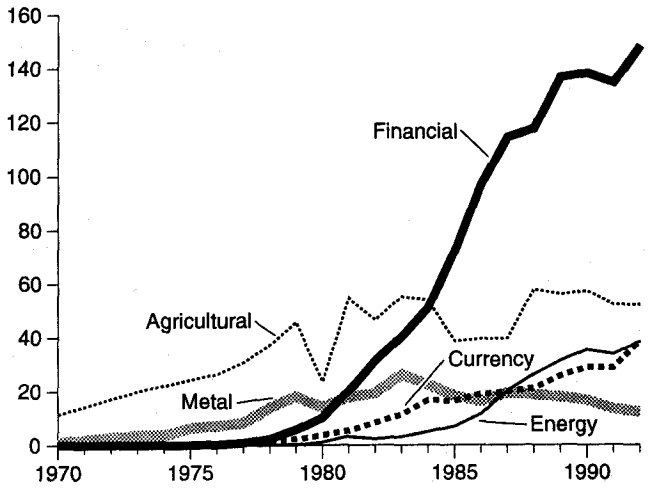


Sources: Bank for International Settlements; Securities Industries Association.

FIGURE 2

Number of futures contracts traded

(millions of contracts)



Sources: Commodities Futures Trading Commission; Futures Industries Association.

for International Settlements (BIS) issued a new report, *Central Bank Survey of Foreign Exchange Market Activity in April 1992*, which states that foreign exchange trading increased 42% from 1989 to 1992, to an estimated $880 billion per business day. This figure includes derivatives trading in currencies (i.e., futures contracts on currencies, swaps, and options), but also excludes offsetting positions. The actual total gross turnover reported by the 26 central banks which conducted the surveys, was $1.354 trillion *a day*.

According to the BIS report, London now trades more dollars and deutschemarks than the United States or Germany does. London has increased its share of world trading, from 25% or $187 billion in 1989, to over 40% or $300 billion in 1992. Trading in London is also increasingly concentrated, with the 10 most active banks in the City of London accounting for 43% of trading in 1991, compared to 36% in 1986, according to a report issued last year by the Bank of England. That means 10 London banks accounted for 18% of all world currency trading in April 1992 (**Figure 4**).

The second largest currency market was the United States, reporting a daily volume of $129 billion in 1989, and $192 billion in 1993. Japan was the third largest, with daily volume in April 1989 of $115 billion, and $126 billion in 1993.

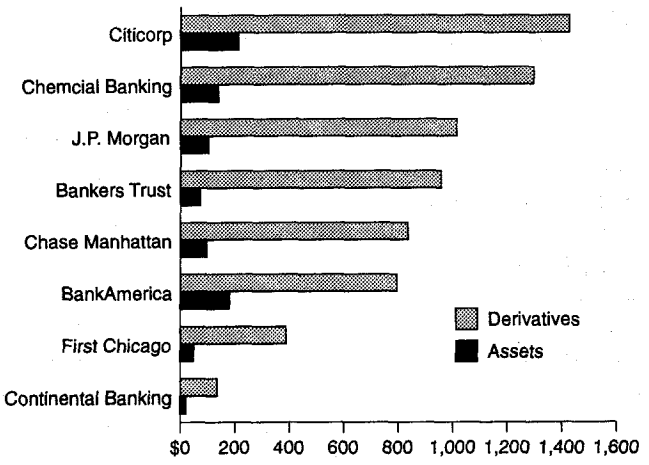
The fifth and sixth largest markets were two key members of the British Commonwealth: Singapore and Hong Kong, with $76 billion and $61 billion in daily trading in April 1992, respectively. If the figures for Britain, Singapore, and Hong Kong are added together, it will be seen that the British Empire controlled almost exactly half of the $880 billion in foreign exchange trading that took place *every day* in April 1992.

In December 1992, for the occasion of the meeting of the finance and bank ministers of the Group of Seven, the BIS issued a new estimate of daily world currency trading, of $1 trillion a day.

FIGURE 3

Derivatives activities compared to balance sheet assets at big U.S. banks

(billions $)

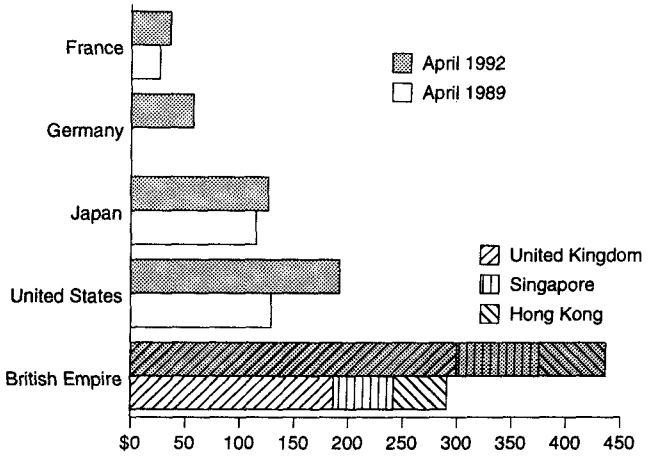


Source: Salomon Brothers.

FIGURE 4

The City of London dominates world currency trading

(daily currency market trading in billions $)



Source: Bank for International Settlements.

Two case studies

Derivatives and agricultural commodity trading

How much does the trading activity on the futures markets contribute to "making the economy more efficient?" Just how many grain futures contracts—covering corn, wheat, oats, soybeans, barley, and sorghum—that are traded on the futures markets, are real, representing the movement of agricultural produce, and how many are purely speculative trades?

Most American farmers will tell you that the agricultural futures markets, whether for grain, livestock products, oilseed products, orange juice, coffee, or sugar, are the farmers' worst opponents, forcing the price of grain products down below production cost. Only 5-15% of farmers even bother to use the futures market to sell their products.

Normally, in theory, the agricultural futures market would work in the following way. A wheat farmer, at planting time in the spring, might see that the price of wheat is but $2.25 per bushel. He might buy a September or December wheat futures contract (a "put") that will pay him $2.75 for his wheat at the month at which the contract expires. This way the farmer has guaranteed himself a minimum price for his wheat when it comes time to sell.

However, most farmers know that the theory does not work out that way in practice. The eighth largest futures trading firm in America, for futures trading of all kinds, is Cargill Investor Services, Inc., run by the Cargill grain cartel. The 34th largest futures trading firm is ADM Investor Services, Inc., of Archer Daniels Midland. They directly manipulate prices against the farmer.

Consulting the statistics provided by the Commodity Futures Trading Commission, which regulates the futures and options industry, in 1992, there were 17,552,356 grain futures contracts traded. Of that total, only 64,200 were settled by delivery/cash settlement, meaning that the actual grain produce of the contract was taken for physical delivery. That is but 0.36% of all contracts traded.

However, at the level of the farmer selling his grain to an elevator, for each sale of real grain—called a hedge—there has to be an offsetting speculative trade to make the market. So, on that first level, there are 128,400 legitimate trades. Then, the local elevator usually sells the grain to the sub-terminal or terminal, such as in Omaha, Nebraska or Kansas City, Missouri, and sale by the local elevator operator must be offset by a speculative sale. Plus, the sub-terminal or terminal might have to sell the grain one more time. So, there are three times 128,400 contracts which can be considered legitimate. That is 2.2% of all trades; so 97.8% of all trades are purely speculative, having no connection to the real process involving the farmer and his produce. They involve speculators, often linked to the grain cartels, moving paper back and forth, attempting to capture spreads, or drive down the grain price for farmers.

The Bank of New England blowout

The January 1991, failure of the Bank of New England (BNE), which had until its collapse been one of the 10 largest bank holding companies in the United States, provides a good example of the way federal regulators have propped up the banking system, and of the risks faced by banks which play in the world derivatives markets.

The collapse of the speculative real estate market, which virtually wiped out the Texas banking system in the late 1980s, spread to New England by the end of the decade, bringing to a close the speculative bubble known as the "Massachusetts miracle." Boston-based BNE, which had lent heavily in the regional real estate market, suddenly found itself with overwhelming losses on its real estate portfolio. The bank, which had grown rapidly thanks to the real estate bubble, was dying with the collapse of that bubble.

In October 1989, BNE, which then had $31.4 billion in assets, announced plans to dramatically downsize the bank through massive asset sales and employee cutbacks. The plans included selling some 10% of its branches, closing loan production offices in Chicago, New York, and Philadelphia, and reducing its work force by more than 20%.

In late December 1989, BNE took the extraordinary step of rescinding a previously announced 34¢ quarterly stockholder dividend. The step was forced by federal regulators, who were already making preparations for the inevitable fail-

ure of the insolvent bank. Federal regulators also threw out the chairman of the bank, and replaced him with an interim chairman, H. Ridgely Bullock.

In early February 1990, in an attempt to calm public fears and prevent depositor runs, Bullock declared that the bank was "off the critical list and getting better. . . . We're in a fix-it mode. We're not going to be as big, but we're going to be better."

BNE was not "off the critical list," however; the only thing keeping its doors open was a massive covert bailout from the Federal Reserve. By the time Bullock made his statement, the bank had already received nearly $1 billion from the Fed.

Beginning in mid-January, the Fed had begun pumping vast amounts of money into BNE via loans from the Boston Federal Reserve. Federal Reserve statistics show that the Boston Fed lent banks in its region $478 million the week ended Jan. 24, compared to just $3 million the week before. While the Fed does not reveal to which banks the money was lent, it is clear that most, if not virtually all, went to prop up BNE.

The weekly bank lending by the Boston Fed rose dramatically in the following weeks: $440 million the week ended Jan. 31, then $723 million the next week, then $930 million, and $1,280 million the week ended Feb. 21. During each of the next seven weeks, the Fed pumped between $1.5 billion and $1.85 billion into the bank; by April 11, the Boston Fed had lent $15.6 billion to its regional banks, the vast majority going to the Bank of New England.

By March, after some $5 billion of bailout funds had already been injected into the bank, the Office of the Comptroller of the Currency and the Fed issued formal cease-and-desist orders to the bank. The Fed order stipulated that the bank could not pay stock dividends without permission from the Fed—a requirement that had already been in effect for more than three months!

Even more comical was the bank's admission in its second quarter 1990 report to the Securities and Exchange Commission, that it may need government assistance to survive. This, after some $18 billion had already been funnelled into the bankrupt bank!

The end for the Bank of New England came on Jan. 4, 1991, when Chairman Lawrence Fish told federal regulators that the $450 million loss the bank suffered in the fourth quarter of 1990, had wiped out its $225 million in equity, making the bank officially insolvent. At this point, the bank had just $23 billion in assets, and had fallen from 10th place on the list of largest U.S. banks, to 33rd place.

Not surprisingly, the announcement triggered massive depositor runs at the banks, with long lines forming at its corporate offices. Two days later, on Sunday, Jan. 6, 1991, federal regulators officially closed the bank. Federal Deposit Insurance Corp. Chairman William Seidman estimated the ultimate cost to the agency of the failures at $2.3 billion, at the time the second most costly bank failure in U.S. history, after the 1988 failure of First RepublicBank Corp. of Dallas.

Why did federal regulators pump more than $18 billion into the Bank of New England, and then close it? If they were going to close it anyway, why did the regulators keep the bank open for a year after it was insolvent?

The answer is: derivatives.

The *Wall Street Journal,* in a June 18, 1991, article by Craig Torres, revealed that regulators had propped the bank up for a year in order to unwind its portfolio of "off-balance sheet" derivatives transactions.

"Everybody knew we had $30 billion in assets" on the balance sheet, BNE head of treasury operations Arthur Meehan told the *Journal.* "But nobody but a small cadre of regulators and analysts knew we hand $36 billion in off-balance sheet activity."

During November and December 1989, before BNE publicly revealed the size of its fourth-quarter losses, BNE chief currency and derivatives trader David Pettit was able to trim his off-balance sheet exposure by $6 billion; getting rid of the remaining $30 billion was not so easy.

The bank, under the close supervision of federal bank regulators, began attempting in January to cash out thousands of derivative transactions. However, as word of its financial troubles spread in financial circles, banks all over the world denied BNE credit, and demanded cash up front. Not surprisingly, this is when the Boston Fed began pumping money into BNE.

Having become a pariah on world financial markets, BNE enlisted the help of Shearson Lehman and Prudential Securities to help it unwind its currency swaps on the Chicago Mercantile Exchange's International Monetary Market. By doing so, Meehan acknowledged, "we moved the risk out of the interbank system into the exchanges;" but had we not, he said, regulators would have been forced to take over BNE's trading positions.

By the end of 1990, BNE had reduced its derivatives portfolio to $6.7 billion. A week later, the bank was closed.

The collapse of the BNE nearly sent the global banking system into "gridlock," the *Journal* warned, adding, "It all sounds far-fetched. But that's just what nearly happened, federal regulators say, in the months before they seized the Bank of New England."

If BNE, with its $36 billion in derivatives, nearly sent the global banking system into gridlock, imagine what would happen were Citicorp, with its $1.4 trillion in derivatives, to fail.

"For certain banks there is a lot of exposure" in the derivatives market, a senior examiner at the Office of the Comptroller of the Currency told reporter Torres. "If we had a real problem with one of the larger banks, a meltdown scenario would be a possibility."

That meltdown scenario is not just a possibility. It is, in fact, well under way.

LaRouche's proposed derivatives tax would solve budget crisis

by Richard Freeman

On March 9, Lyndon LaRouche intervened in the economic crisis to propose a plan that is as exquisitely simple and direct, as it is potentially effective in its execution: a sales or transaction tax on the turnover of "financial derivative" securities or financial instruments. Each time such a security or instrument is traded, he said, it should be taxed at 0.1% of its face value, or, as it is called in the derivatives trade, its notional principal amount.

No more than that simple "least action" step is needed.

The tax will raise between $60 and $80 billion in federal tax revenues in its first year of application. That is a very handsome sum for the U.S. government.

Although bankers will catalogue why the explosion in financial derivatives since 1986-87 is absolutely essential—"they hedge risk," "they make the markets more efficient" and so forth—their rationalization is *post hoc* nonsense. A financial derivative is a speculative, highly leveraged instrument, capturing interest rate or currency-related spreads. Rates of return on financial derivatives can vary from 10-15%, up to 2,000%, and even higher.

Taken as a whole, the financial derivatives market, orchestrated by financiers, operates with the vortical properties of a powerful hurricane. It is so huge and packs such a large momentum, that it sucks up the overwhelming majority of the capital and cash that enters or already exists in the economy. It makes a mockery of the idea that a nation exercises sovereign control over its credit policy. What good is a U.S. government policy to inject a few billion or even hundreds of billions of dollars of credit into the economy for jobs or other programs, when the financial derivatives market can overwhelm and counteract the effects? One hundred billion dollars is but one one-thousandth the size of the financial derivatives market. It is the financial derivatives market that organizes the overall geometry of, and thus significantly determines, how the U.S. credit system functions.

In his weekly "*EIR* Talks with Lyndon LaRouche" radio program on April 28, LaRouche told interviewer Melvin Klenetsky:

"This is *sucking the lifeblood*, in the same way that Michael Milken and his raiders were doing, who were stealing from people's pensions and so forth with junk bonds and these acquisitions. It's sucking the lifeblood out of industries, out of pensions, out of households—out of everything—out of our businesses, out of our farms. These people are thieves."

This vast market in the tens of trillions of dollars is international in scope, although 65% of financial derivatives trading occurs in the United States. But lawfully this international market must melt down. It will follow the path of every bubble in history since the tax-farming pyramiding schemes of the treasury of ancient Babylon and Imperial Rome up through A.D. 300, to the notorious John Law financial bubble in the eighteenth century. The violent effects of an explosion of the derivatives market bubble will far overshadow, the collapse of the leveraged buy-out bubble combined with the October 1987 stock market crash, liquidating one-third the value of the market within weeks, and the $350 billion expended since 1987 for the bailout of the commercial banks and savings and loan institutions.

Hence, LaRouche proposed that America re-assert sovereign control over its power of credit issuance through the transactions tax. The tax will also introduce transparency: Since each transaction to be taxed will be registered, the tax will act to identify the major players controlling the market. Such tax proposals have been made at earlier periods in the nation's history (see box, p. 36). The financiers fiercely resisted them, and usually prevailed. But this time, the stakes are immensely greater than ever before in history.

How the tax works

To understand how the tax will raise $60 to $80 billion in revenue, and how it will bring the derivatives market under control, let us examine the different kinds of derivatives markets that the tax will encounter, and how the tax will apply in each case. These instances simultaneously provide a useful bird's eye view of the incredible levels of deadly leverage at work. We will conclude by showing how the revenue from the tax is calculated.

Currently, the derivatives markets, and other financial markets, *pay zero percent sales tax on trades*. Most states apply a general sales tax of between 4.5 and 9.0¢ on the dollar; that is, a tax is assessed equal in value to between 4.5 and 9% of the value of the purchase (transaction) made at the store. Under the LaRouche tax proposal, each trade of a financial derivatives market instrument will be assessed a "sales" tax equaling just 0.1% of the value of the purchase, far less than the rate citizens pay every day. It is absurd and

dangerous to continuously raise the tax on Social Security and to apply an energy BTU tax, which will devastate every sector of the economy, while the transactions—as opposed to the realization of profit—of the financial derivatives market, which are harmful to the economy, go untaxed.

With a sense of poetic justice, the LaRouche tax will provide *reverse leverage*. As will be shown, the higher the leverage operating in a particular market, the more the LaRouche tax will bite. The less-leveraged markets, such as the stock-equity and the bond markets, which in normal times are helpful to an economy in supplying equity capital or debt for new capital formation and expansion, will be least affected. The tax will help return these markets to their true function.

Applications of the tax

As a simple example of the transaction tax, consider the case of an application of the tax to a stock. Take the random case of the oil giant, Amoco, which at the close of trading May 14 was worth $55.50 per share. A 0.1% transaction tax would add 5.6¢ to the cost of a share—less than half the value that Amoco stock moves every day in a quiet market. Let us take the case where someone is buying the Amoco stock through a broker. The brokerage commission would be 4 to 8¢ per share traded. The tax adds a small, but real impediment: It roughly doubles the per share cost of purchase to what the brokerage commission fee alone would cost. While the cost is not very large, representing 0.1%, it is important. It makes the purchaser less financially able to rapidly turn over trades in the stock, and makes him hold the stock a longer term for the dividend yield, rather than trading short term for its rapidly changing price.

Next, attention is turned to application of the tax to the futures market. The futures market has exploded, largely through the introduction of trading in financial instruments. All through the 1950s and 1960s, up until 1970, the volume of yearly trading of futures rarely exceeded 10 million contracts. By 1992, however, annual trading volume climbed to 289 million, 29 times the annual level of 1970. The futures market, valued at roughly $25 to $30 trillion, comprises the largest share of the dollar value of the entire U.S. derivatives market.

How the tax will function is illustrated by examining its practical application to two of the most powerfully destabilizing and leveraged of all futures contracts.

U.S. Treasury Bond future

Traded on the Chicago Board of Trade (CBOT), the U.S. Treasury Bond future is the single most widely traded futures contract instrument in the world. In 1992, a whopping 71,099,955 contracts in this future were traded. That figure represents one-quarter of all contracts of all types traded on the CBOT, which is the world's largest exchange. The notional principal value of the underlying bond of the U.S. Treasury Bond contract is $100,000. It is usually a bond of 15 years or longer maturity. The speculator buying this contract does not pay $100,000, but only a fraction of that, which is called the "initial margin requirement." Margin requirements vary from contract to contract, but for this one, the initial margin required is $2,025. The leverage in this contract is the notional principal amount, or $100,000, divided by the margin bond requirement of $2,025. Thus the leverage is a spectacular 49 to 1.

Assume, for a moment, that the bond underlying this contract is a 15-year bond bearing an initial yield of 8%. Assume further that, during the first hour of trading, the interest rate on 15-year Treasury bonds fell marginally to 7.995%. As bond yields are inverse to prices, that would push up the price of the bond to $100,050. The speculator holding a U.S. Treasury Bond contract has made a $50 profit (to realize it, he must either take physical delivery of the bond, or sell the contract to someone). That $50 represents a rate of profit on the investor's original margin investment of $2,205, of 2.47%.

The reader may think that $50 is a very small return. Not at all.

First, speculators in these markets play with very large

The John Law bubble gone mad

From LaRouche's March 9, 1993 proposal for a tax on derivatives:

The derivative bubble, by the very nature of these transactions, is a financial bubble in the tradition of the more primitive, more rudimentary, and far less dangerous bubbles of the eighteenth century such as the John Law bubble in France and the South Sea Island bubble in England in the same period of time. This is the John Law bubble gone mad. The vulnerability to the entire financial system, the chaos and destruction of actual physical processes of production, distribution, employment, and so forth is incalculable in potential, and therefore this thing must be brought under control promptly. . . .

The down side that would be argued from certain sources, apart from the wild free market monetarist maniacs, will be that the number of transactions related to any single initiating trade, can be enormous, can be over 100 individual transactions. Fine! Tax them all! "That's a big amount of paper," they will say. Fine! Tax them all! The burden of doing the paperwork will itself prevent you characters from ballooning this market in that way.

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volumes. A speculator may buy 100 contract units of U.S. Treasury bond futures on the CBOT, meaning that the profit realized in one hour of trading (less commissions, etc.) is $50×100, or $5,000.

Second, the actual rate of return placed on a daily or yearly level is huge. For example, were the speculator to continue to realize this 2.47% hourly rate of profit for a week, his rate of return would be above 85%. Who will invest in steel plants, which return about 5% per year, when spectacular rates of return can be made in the derivatives market in a week's worth of trading?

Now, if LaRouche's 0.1% transaction tax is levied to the $100,000 notional principal amount of the U.S. Treasury Bond contract that has been purchased, the tax would yield $100, and could be collected by the exchange. But, in this example, the tax is a necessary, unbridgeable hurdle: The speculator will pay more in tax ($100) than his profit ($50). The LaRouche tax makes the deal unprofitable. Just to break even to cover the cost of the transaction tax, the speculator would have to make $100 profit, which represents a rate of profit of 5% on this particular transaction. To go over breakeven, the speculator would have to make $150 or so, representing a 7.5% rate of profit on his investment. The chance that a Treasury bond will move up $150 in an hour is slim, although hardly impossible, especially in a manipulated market. But markets can turn very suddenly, as speculators very well know. In markets, in which the time it takes to transact a trade is measured in fractions of a second, a speculator can be severely burned if he is constrained to wait in the market long enough for it to realize a full 5-7.5% rate of return. If it doesn't in that time frame, the market jolts the other way, he is doomed. The threshold level for real or net profitability, introduced by the 0.1% transaction tax, will, like a surgical tool, slash trading in this market instrument by at least one-fifth to one-quarter of its volume, puncturing this market, and begining to dry it out: precisely as the tax is intended.

The stock index future

The other example is the Major Market Index (MMI), which is also traded on the Chicago Board of Trade. The MMI is an average of a basket of 20 leading stocks, such as AT&T, Du Pont, or Mobil, and is the favorite of the program traders. By using the MMI in the Chicago futures market, they can send the Dow Jones Industrial Average gyrating up and down. The MMI was one the chief culprits behind the October 1987 stock market crash. The notional principal of the underlying MMI contract is calculated by a formula, which is 500 times the MMI index's closing price. On May 13, the MMI index closed at $356.40, so the notional princi-

The history of the fight against derivatives

The fight to institute Lyndon LaRouche's proposal for a one-tenth of 1% tax on financial derivatives comes after intense warfare over this issue by many nations that were fighting to preserve their national sovereignty. In the United States, trading in options on agricultural commodities had been banned in 1936, and the ban was not officially lifted until 1983.

Farmers had opposed the highly destructive effect of options, one of the earliest forms of the derivative market, starting in the 1920s, long before they became as large as they are today; even then, farmers still exercised significant influence within the United States. In 1933, an attempt was made to manipulate the wheat futures market using options, which resulted in an opportunity for farmers to force the U.S. government to ban trading in these options. There were attempts to re-introduce trading in agricultural options during the 1970s, but the plan met with only limited success.

It was only in January 1983, when President Ronald Reagan signed the 1982 Futures Trading Act, that the ban was officially lifted. This was a major feature in the disastrous Reagan-era deregulation of the U.S. economy.

Contrary to the "free enterprise" argument that options markets are essential to agriculture, because they make the market more efficient, American agriculture has demonstrated its ability to function and thrive without options trading for the three and a half decades since the ban in 1936 through 1983.

Moreover, America had, for a short time, a small financial transaction tax, and the fight to impose a larger financial transaction tax was very intense in the late 1980s.

Throughout the 1950s and early 1960s, the United States had a low-rate transaction tax—called a stamp tax—on the issuance and transfer of stocks and debt. The tax was repealed in 1965.

Rumblings from Congress

However, in the late 1980s, the fight broke out more intensely for a transaction tax of a greater size. In 1987, Speaker of the House Jim Wright of Texas called for a transaction tax on the financial markets. Wright's proposal called for a 0.5% tax on both the seller and the buyer in the same transaction, thus, effectively, amounting 1%. For six months, there was a heated public debate over Wright's proposal. Wright was soon driven from office in what is generally agreed to be an overblown scandal. The

pal amount of the MMI futures contract was $178,200. The initial margin requirement that a speculator must commit to buy an MMI futures contract is only $5,400. The leverage built into this contract is 32 times.

Assume that the MMI index trades upward for the day by 25¢, which, multiplied by 500, per the formula, makes a profit on the contract of $125. However, the 0.1% transactions tax for the single trade in the Major Market Index will yield $172. Thus, once again, the tax level is higher than the anticipated profit. A trader in the MMI contract would have to make more than 3.2% on his margin investment to go over breakeven. Again, the trading volume of the market in this destructive contract will shrink.

A sizeable revenue

This is how the tax acts to exert reverse leverage. The higher the leverage of the transaction, as in the case of the U.S. Treasury Bond futures contract, the more bite the derivative tax takes, thereby shrinking the markets. In the case of stocks traded on the New York Stock Exchange, the effect is important, but less remarkable. The tax is applied in similar fashion to every section of financial derivatives markets, such as currency and interest-rate swaps held by the banks in the United States.

If one adds up the value of the annual transactions in all the diverse segments of the financial derivatives market—the many and varied derivatives in currencies, stocks, bonds, interst-rate futures, commodities, etc.—the sum of the notional principal value traded is between $80 and $100 trillion. A precise figure does not exist, in part because the different trading exchange and government regulatory bodies have not compiled figures for the different segments of the market—and do not want to—because it would expose how large the markets have become. It can be assumed that the tax will reduce trading volume and, in parallel, a roughly corresponding dollar volume, in all the financial and financial derivative markets by at least one-fifth to one-quarter. This reduction will occur within a matter of weeks of the application of the tax, so that the derivatives market against which the LaRouche tax can be applied will be reduced to a low of $60 trillion or a high of $80 trillion. A tax on this range of 0.1% range will yield $60-$80 billion in annual revenue. After the first year, because the tax is, in part, a "sin" tax, the tax revenue will be smaller. However, as every congressman and senator caught in the budget debate will admit, such a tax produces a very, very large revenue figure.

Most importantly, the tax harms nothing essential in the physical economy, while lancing a growing malignancy. It constitutes a crucial step toward restoring America's sovereignty.

Oct. 16-19, 1987 stock market crash confirmed Wright's warnings of the instability of the financial markets.

Also in the 1989-90 period, during discussion of the 1990 Budget Reconciliation Act, Sen. Lloyd Bentsen, then chairman of the Senate Finance Committee and now secretary of the treasury, raised a proposal for a transaction tax on selected financial instruments on the floor of the Senate.

In February 1990, partly in response to the furor over this issue, the Congressional Budget Office, in its report "Reducing the Deficit: Spending and Revenue Options," had a section on pages 388-89, entitled "Impose a 0.5% Tax on the Transfer of Securities." Its analysis of the tax reported that "the tax would have to be broad-based, applying to stocks, debt, options and trades by Americans on foreign exchanges."

What other nations have done

Various nations have taken action to tax and/or ban some of the instruments traded in the financial derivatives market, in an attempt to assert sovereign control over their national credit and finances.

- In 1986, the government of Sweden doubled its equity transaction tax, which is the tax on trade of stocks on the Swedish stock market. In 1989, Sweden extended the tax to futures and options trades. The effect of this new tax was to substantially reduce the trading of futures on Sweden's Stockholm market. Furthermore, the tax closed the Swedish Option and Future Exchange (SOFE) for two years. But in 1990, apparently under pressure from financiers, Sweden abolished the derivative tax, and trading in the derivatives market exploded, helping to deepen Sweden's financial problems.
- Until as late as 1989, the German government held firm and refused to legalize the trading of some financial derivatives within the country. As a result of pressure from the trading of German government bond futures in the London markets, amendments to Germany's gambling law in 1989 made changes and permitted retail participation in derivative markets, followed by the opening of Germany's first financial exchange, Deutsche Terminbörse in 1990.
- At present, derivative taxes are assessed in Finland, France, Hong Kong, and Japan. These countries assess a transaction tax on various securities at rates 3-6 times larger than the LaRouche-proposed tax. In France, the fee is only used to finance the annual budget for CMT, the French regulatory body for the futures and options markets. Once the CMT's budget requirement is met, the fee is no longer levied.—*Richard Freeman*