# Time runs out for a challenge to Eurodollar takeover of the U.S.

by Kathy Burdman

Shifts in the way the U.S. banking system clears funds will bring the entire national banking network "online" with the international Eurodollar markets by early next year. When this happens, according to plans proposed by Citibank, Prudential Life Insurance, and other financial giants, the assets of the nation's 20,000 commercial and thrift institutions will become inextricably tied to the Eurodollar markets.

In this situation, then, any potential default on the Eurodollar market, where the big New York and California banks get into trouble for bad Third World loans, will now become the problem of the entire U.S. banking system. The shifts include:

- The May 1, 1981 shift of the Federal Reserve System to full, simultaneous national electronic funds transfer (EFT), creating a national bank clearing system.
- The Oct. 1, 1981 shift of the New York banks' Clearing House International Payments System (CHIPS) to an EFT settlement between New York and Europe, creating a same-day international clearing system.
- The planned startup early next year of International Banking Facilities (IBFs) in the United States, which would allow Eurodollar-style reserve-free deposits across the country, creating large new speculative deposits and loans domestically.
- Expansion of the life insurance sector into takeovers of major brokerages—exemplified by the Prudential takeover of Wall Street's Bache, Halsey Stuart—an expansion that is rapidly leading to total deregulation of U.S. banking.

## Closing the time gap

As of May 1, the Federal Reserve consolidates the basis for an interstate banking system in the United States that could make the nation's 14,000 regional commercial banks and 5,000 savings and loan institutions obsolete in a matter of days. On that day, the Fed's nationwide internal EFT system, Fedwire, extends its clearing day, which now ends at 3:30 p.m. Eastern Standard Time, to 6:30 p.m. EST. This is designed to bring the major money-center banks of California, led by Bank of America, and others in the Pacific and Mountain time zones onto the same basic clearing schedule as the New York and Boston banks.

Until May 1, Fedwire's closing at 3:30 p.m. EST has meant that California banks had to scramble to close out federal funds and other trading positions by noon Pacific time, and to clear many positions the next day. This put them at a competitive disadvantage vis-à-vis New York in many transactions, and made direct clearing with the London Eurodollar market, in particular, much more difficult.

Extending the Fedwire closing means that the big California banks, as well as the major Chicago and Texas banks, who are an hour behind New York, conduct transactions, and in particular loan fed funds during broadly the same time as the major East Coast banks. This will considerably enlarge the nationwide market for federal funds.

The new Fedwire system is not in itself a bad thing; it is in fact a potentially welcome streamlining of the system, which in an evironment of economic growth could facilitate capital flows and productive investment. The problem is that the Fed's intended use for the system has nothing to do with such a potential.

The new Fedwire system, Fed sources say, is in fact designed expressly to go with the other elements of the international EFT system now being put into place. Extending Fedwire is a prerequisite for the New York banks' Clearing House International Payments System computer to move to same-day settlement beginning Oct. 1. CHIPS is the large computer system operated by the 12 leading New York banks. It currently clears some $180 billion per day between the New York majors and their foreign branches in the London Eurodollar market, as well as in the Nassau-Cayman Islands, Hong Kong, Singapore, ad other offshore dollar markets.

Currently, CHIPS calculates at the end of the day the size of the global imbalance among New York banks, and who owes how much to whom. But the banks do not actually settle with each other by buying and selling federal funds on Fedwire until the next morning. When CHIPS moves to same-day settlement, these banks will all be in the market for fed funds, creating a potentially huge new daily demand for up to $10 billion in net funds.

Without the extended Fedwire hours, this would cause a major disruption in the fed funds rates and the financial markets generally. Fed sources say that the lengthening of Fedwire's hours is not geared to this problem per se but is "really designed basically to deal with the new CHIPS program." "With Fedwire extending its hours, there will be so many more banks in the fed funds market during the time that CHIPS members are clearing that the CHIPS clearing will be able to take place smoothly, since more funds will be available," said a source.

## The beneficiaries

This does not merely represent increased banking efficiency. The bottom line of the innovations is the plan to link the streamlined EFT system directly into the Eurodollar market through the establishment of International Banking Facilities based in the United States. Federal Reserve sources confirm that the major beneficiary of this new international EFT system will be IBFs.

International Banking Facilities, as we have reported in depth (*EIR*, Oct. 21, 1980), would be branches of U.S. banks authorized to take Euromarket-type deposits in major cities across the nation. By Eurodollar deposits, we mean deposits free of reserve requirements; free of regulations on interest rates; and free of all U.S. federal and local taxes.

This plan, when linked up to the new Fedwire and CHIPS systems, would create an integrated Euromarket banking deposit network dominating the nation's credit base.

The very existence of the fast-clearing mechanism between Fedwire and CHIPS, Fed sources say, will mean that IBFs in Chicago and San Francisco banks, for example, will be able to hook directly into Europe via Fedwire and CHIPS virtually simultaneously. This will encourage a far greater volume of deposits to be created in a Chicago IBF, for example, than a normal Chicago bank now deposits in the London Euromarket.

The reason is that reserve-free deposits are cheaper for banks to maintain, since holding reserves at the Fed costs them money. Therefore Euromarket banks today may offer higher returns to depositors and still profit, as they do. With such marginally higher-rate deposits available at IBFs across the United States, all linked into the local Fedwire, any bank or corporation in the country with excess funds to lend will have an incentive to move its funds into IBFs.

Technically, IBFs are only allowed to take deposits from outside the United States, but banking experts agree that by appearing to book IBF deposits from foreign branches, many American banks and corporations will be able to take advantage of the new deposit facilities.

In particular, local banks and savings and loans, who would never have bothered to sell deposits to London with the complicated telex procedures involved, will now do so, hope the Fed and the New York banks, and hence find it much easier to entangle themselves in IBFs.

## What the mergers mean

The final factor in the major shift now going on is the overt move to legalize interstate banking and merge banking with the life insurance and brokerage companies. Financial giants such as Citibank, Prudential Insurance, and Merrill Lynch will "go national" and bankrupt local commercial and savings banks through cutthroat competition. And the new EFT moves will most benefit these giant institutions.

April alone has already seen two takeovers of major Wall Street brokerages by nationally based finance companies. After Prudential Insurance bought the Bache Group, Inc. for $385 million, American Express announced its $915 million purchase of Shearson Loeb Rhoades. The idea, say Wall Street analysts, is to use the ability of the insurance, finance, and brokerage companies to go interstate—since banking prohibitions don't apply to these "nonbanks"—and set up "financial supermarkets" conducting all sorts of transactions, including taking deposits and making loans, that banks currently perform.

Already, the two brokerages offer banking services called "cash management accounts," whereby a customer can keep deposits and write checks on his stock investment account. With an American Express card, a Shearson customer will soon be able to write these checks and make deposits across the country. "By the end of the decade," says Amex chairman James D. Robinson III, "a typical consumer may have a stockbroker in California, a banker in New York, insurance agent in Maryland . . . all on the American Express card, of course."

Not only will these giants be able to go interstate, making mincemeat of laws against interstate banking. They will obliterate the distinction between banking and brokerages established by the 1939 Glass-Steagall Act. The Amex-Shearson plan "makes a total mockery out of Glass-Steagall," says deregulation sponsor Walter Wriston, the Citicorp chairman who himself is on record pressing banks in turn to go interstate and move into other financial industries. The merger "has driven the final nail into the coffin of bank holding-company regulation," he says.

If that happens, the nation's regional banking system will be next in line.