Rites of passage for S&Ls

The FSLIC is almost bankrupt. So are many more thrifts. So are the remedies being proposed in Washington.

The Federal Savings & Loan Insurance Coporation has spent so much money bailing out thrift institutions that it is nearly out of cash, New York commercial bankers say. "The FSLIC is bankrupt," one source stated succinctly. And at the same time, roughly 1,000 of the nation's 4,700 savings and loan institutions are inches from bankruptcy, as a result of the Federal Reserve's high interest rates.

In 1981, 17 out of every 20 S&Ls lost money. And, according to the S&L specialist at the Brookings Institution, Andrew Carron, FSLIC figures show that, whereas in 1975-76 the share of thrifts' lending to the housing sector was 60 percent, by the fourth quarter of 1981, it was minus 9 percent!

This problem could have been solved at any time during the past two and a half years, by ousting Volcker and his policies and providing preferential, cheap credit to the productive sectors of the economy, including home-building. That would have quickly reversed the situation in which thrifts carry old mortgages at 5-7 percent, while paying out an average 11½ percent on savers' deposits, and effective demand for housing is pulverized.

Does Volcker now agree to alter his policy? Not at all. He wants to stampede Congress into bailing out the S&Ls with some $10 to $20 billion in taxpayers' money. The "leak" in mid-April that the FSLIC is close to empty should provoke such congressional response, my usual Treasury source told me, laughing.

Volcker's only problem now is that Congress is balking at a bailout, he said. "Freddie," meaning Representative St. Germain, Chairman of the House Banking Committee, "has backed off. He's counted his votes and for now believes he can't get a bailout through. He can't move the Democrats on it this year, in an election year, without political damage to them. The Republicans have already warned they will cry 'foul' and accuse the Dems of budget-busting if they vote up money for the S&Ls before it is absolutely necessary. So the House Banking Committee won't do it until it is absolutely necessary—and then they will wait until the crisis is upon us, and force the Republicans to do it themselves. The Republicans are not ready to do so yet. Treasury is telling them not to."

My source predicted that the crisis would hit in the fall. Meanwhile, the Fed will paper over the situation. "The major problem is that for now, Congress won't give the S&Ls anything else, so the Fed will have to increase use of the discount window. This will grow gradually, and by the fall, there will be substantial use of the discount window and a substantial amount of discount loans outstanding to S&Ls. But it will take more than the current situation to convince Congress that more is necessary."

Such Fed money-printing could cause a panic, of course. Then Congress would be forced to step in. "If and when people do get upset about the S&Ls, or about Fed lending to S&Ls, then Congress will move," concluded my source.

The Reagan administration's own interim solution has been to hand out cash to relatively healthy S&Ls to enable them to take over failing S&Ls, a ploy that has now reportedly consumed most of its $7.5 billion in insurance funds. As this failed to cover the gap, the FSLIC resorted to two other operations, or, properly speaking, scams.

First, it helped provide huge tax breaks to solvent S&Ls who agree to assume the losses of failing ones. This averted the need for FSLIC outlays in most of the 324 mergers that occurred in 1981. Secondly, the FSLIC gave faltering S&Ls paper credits to boost their net worth, and bolster their books. Those bogus assets will disappear with the first wave of S&L bankruptcies.

Moreover, all the merger policy has done is to make those S&Ls with some income-earning ability spread that income over a greater mass of bad debt. The income-earning ability of the thrifts as a whole is not increased, and won't be until the Volcker question is dealt with. Note that the Hyde Park Savings and Loan of Chicago, which took over two failing S&Ls in 1981, had to be taken over itself this January to keep it above water. And the 20th largest S&L in the country, the Fidelity Financial Corporation, a S&L holding company based in California with $3 billion in assets, was shut down by federal authorities April 13; a new owner is being sought.