Banking by Kathy Burdman

One, two, many Conti Illinois?

Volcker wants a crisis to enforce a banking reorganization; but he may get a banking rout.

The June 15 refusal by Treasury Secretary Donald Regan to renew a minor loan guarantee to Argentina could produce a panic in July dwarfing the deposit run on Continental Illinois bank in May.

Regan's "macho" challenge to Argentina represents a dangerous gamble by Federal Reserve Chairman Paul Volcker and International Monetary Fund Managing Director Jacques de Larosiére, the real powers behind Regan. Volcker and de Larosière, themselves fools, plan to contain losses and use them to reorganize U.S. banks.

At Senate Banking hearings June 14, Volcker bragged that he is willing to have several major U.S. banks take losses in July. "What is at issue here is a fairly limited number of interest payments. . . . In itself, I don't think it's terribly significant," he said.

The IMF's de Larosière also told the bumbling Regan June 14 that a hard line is necessary, as Regan himself informed me. "I have never known this administration to lean on the IMF to make loans which the IMF in its judgment feels they can't live with. The IMF has to make that judgment," Regan said.

But hard reality is that if the banks and IMF do not give in and lend Argentina some $500 million this month, Argentina will be over 90 days past due on $500 million or more in interest payments to foreign banks on June 30. Under Volcker's prodding, bank regulators will bend no rules, U.S. money center banks will have to declare the loans "non-performing," and declare over $300 million in lost income. That would be directly deducted from U.S. banks' second-quarter profits.

Manufacturers Hanover, already subject to a European depositor run May 24, will lose some $20 million, a full 25% of the quarter's income, and Chemical Bank, Bank of America, and Citibank a similar 20-25% of income. Manny Hanny has some $1.3 billion in officially reported Argentine loans, Chase Manhattan $800 million, J.P. Morgan $750 million, and Conti Illinois itself some $400 million.

Chemical Bank, Bank of America, and Citibank don't have to report Argentine loans, since they are officially just barely less than 1% of assets, but I estimate them at $700 million, $1 billion, and $1.3 billion, respectively. Aside from Manufacturers Hanover, Chemical and Bank of America have been most often mentioned in London boardrooms as "in big trouble" if Argentina goes, because of major additional bad domestic loans they hold.

That is, there could easily be a major, 1931-style run on the U.S. banking system. Large European depositors lead by the same Lazard, Safra, and Deutsche Bank group who organized the run on Conti Illinois, will take the opportunity to pull deposits out of all these U.S. banks at once.

Asked June 14 what the government would do faced with "many Continental Illinois bank runs at once," Treasury Secretary Donald Regan had no answer:

Regan: Why should there be a run on their deposits?

Burdman: These banks are weak, there has already been a run on Continental and Manufacturers Hanover.

Regan: What do you mean, Manufacturers Hanover is weak?

Burdman: Manufacturers Hanover stock just dropped from 37 to 26 and if they take a $20 million second-quarter loss on Argentina, and if Chemical takes a similar loss, then foreign depositors will move deposits out of these banks, as they did with Continental and you've got a deposit run on many banks at once. What will you do?

Regan: No comment—too many "ifs."

Volcker and de Larosière, oblivious to this threat, want to use a crisis to force mass of mergers and consolidation of U.S. banks. By weakening banks, this would put investment bankers (see last week's column) such as Henry Kissinger's American Express Shearson Lehman, which are expanding into financial supermarkets, in control of the U.S. credit structure.

The supermarkets and a few large "survivor" banks such as possibly Citibank, which has its technetronic infrastructure in place, would under Volcker's plan control all credit, by taking over most regional banks including large ones. This week, Belgian Rothschild scion Baron Lambert's investment bankers Drexel Burnham announced a prototype plan. Lambert and Armand Hammer's employee A. Robert Abboud proposed that the FDIC, now running Conti Illinois, dismember the bank altogether and sell it off in two pieces. One piece, a "bad bank," would be given all the bum loans and sold off a nickel on the dollar to speculators. A "good bank" with the rest would find kinder buyers.

Working with the Swiss-based BIS, Volcker and de Larosière also expect the ensuing credit crunch to weaken U.S. industry, bash the stock market, and make large U.S. industrial companies cheap for major European buy-ups.