

Banking by John Hoefle

A taste of things to come

The impending demise of Chase Manhattan shows that political expediency and a banking crash are dangerous bunkmates.

Chase Manhattan Corp., the nation's second-largest bank, gave the country a taste of things to come Sept. 21, when its problems nearly collapsed the entire banking system.

It is common knowledge among financial insiders that the U.S. banking system, and in particular the very largest money center banks, are bankrupt. Considerable effort, both financial and political, is being expended to prevent that nasty little fact from being widely known. Fortunately, truth has a way of asserting itself.

These days bankers hate the ends of the quarters, when they have to reveal their banks' sad financial condition. If they lie, they can go to jail; if they told the truth, many of their banks would collapse immediately.

Chase took the plunge Sept. 21, revealing that it expected to lose \$625 million in the third quarter, due mainly to massive real estate losses and a drastic restructuring. The bank announced that it would also cut about 5,000 employees from its rolls—12% of its work force.

On top of that, the bank is widely expected to cut its stock dividend in half at its Oct. 17 board meeting. In the quick-buck world of modern speculative finance, such dividends are considered sacrosanct. Insolvency can be overlooked, but cutting dividends is another story.

The news sent Chase's already depressed stock plummeting, forcing the New York Stock Exchange to take the drastic step of temporarily suspending trading in it. The stock fell 7% Sept. 21, to only \$12.75 a share. Since the October 1989 stock market

dive, when it was just under \$45, Chase's stock has collapsed nearly 75%.

Chase is hardly alone. The major New York banks—Citicorp, Chase, Chemical, Manufacturers Hanover, Morgan Guaranty, Bankers Trust, and the Bank of New York—have as a group lost over 50% of their common stock value since that 1989 crash, with half of that loss coming since June, and some 10% in the last two weeks alone.

All of these banks, with the possible exception of Morgan Guaranty, are facing serious liquidity crunches. In order to roll over a mere \$200 million in debt, Chase recently had to raise the interest it paid from 9.66% to more than 13%, putting the bank's debt very nearly in the "junk" category.

Stanford University economist Dan Brumbaugh recently told a Cable News Network audience that the six biggest banks in the country are already insolvent, and that 400 banks have shown net losses since 1986. That means, he said, that the Federal Deposit Insurance Corp. is also insolvent, since its \$13.2 billion in insurance funds could not begin to cope with the losses were the insolvent banks to be closed.

The obvious question one should ask is, why are the banks still open?

The answer is simple: politics. There's an election coming up in November, and it's considered bad form to have a catastrophic financial collapse right before an election.

The secret agenda in Washington is to hide the banking crisis from sight

until after the elections, then implement a massive British-style consolidation and restructuring plan.

According to an article by Christopher Whalen in the Sept. 17 *Barron's* magazine, the Federal Reserve has given a virtual blank check to the Resolution Trust Corp., by treating RTC bonds as de facto Treasury obligations. The Treasury, through the Treasury, Tax & Loan (TT&L) mechanism, is pumping billions of dollars of government money into "deserving banks" in a massive covert support operation. To complete the federal bailout picture, Whalen noted that the Federal Reserve has been buying billions in Treasury notes at Treasury auctions.

For these agencies to squander hundreds, perhaps thousands, of billions of dollars to prop up a hopelessly bankrupt system, thereby risking a hyperinflationary blowout, is a reflection of the desperation gripping the government. After all, the Federal Reserve itself has proclaimed inflation as Public Enemy Number One.

Such political manipulation, of course, is old hat to the Bush administration. The 1988 failure of First Republic Bank Corp. of Dallas—which Whalen identified as the beginning of the TT&L support operation—was postponed until after the Texas primaries, at a cost of several billion dollars, despite its obvious insolvency and financial hemorrhaging. It might have hurt the political aspirations of the state's favorite presidential candidate, George Bush. Federal officials are currently investigating to see why the government waited until after the 1988 presidential election to close the insolvent Silverado S&L, where the President's son Neil Bush had been a director.

When political expediency and financial chaos mix, a crash is not far behind.