Banking by John Hoefle

The off-balance-sheet blowout

A new study by Weiss Research, Inc. shows that bank liabilities are far higher than officially reported.

The classic definition of bankruptcy is when liabilities exceed assets. By that definition, even using their current lying balance sheets, the U.S. banks are bankrupt. That point was driven home by the statistics on the off-balance-sheet liabilities of the top U.S. banks recently released by Weiss Research, Inc. of West Palm Beach, Florida. These statistics were as of the third quarter of 1991.

According to Weiss, the 20 largest banks in the U.S. had combined off-balance-sheet activities of $6.104 trillion, or 697% of their $899 billion in reported total assets.

These so-called off-balance-sheet activities comprise three broad areas: 1) commitments by banks to provide credit at some point in the future, such as loan commitments and revolving underwriting facilities; 2) guarantees to a third party that a bank customer's obligations will be fulfilled, such as standby letters of credit; and 3) various types of futures and other market trading, including interest rate swaps, currency swaps, and financial futures and options contracts.

Under the current Alice in Wonderland accounting standards, these off-balance-sheet items are counted as neither assets nor liabilities on the banks' books. Nevertheless, they do represent direct liabilities for the banks, since any losses on these items come out of the banks' income and capital.

By maintaining the fiction that these liabilities are not part of the "official" assets and liabilities of the bank, banks are also not required to maintain capital or loss reserves against them. These bookkeeping tricks allow the banks to pretend that they are still solvent.

Consequently, there has been an explosion in off-balance-sheet liabilities, especially among the biggest, weakest banks.

In 1984, according to a 1988 General Accounting Office study, U.S. banks had $1.364 trillion in off-balance-sheet activities. By 1985, that figure had risen to $1.840 trillion, or 67% of all bank assets. Of that amount, $1.507 trillion was held by big banks (over $10 billion in assets), representing 159% of those big bank assets. By the end of 1986, total off-balance-sheet liabilities were equal to 80% of all bank assets, and the big banks had off-balance-sheet liabilities equal to 189% of their assets. By mid-1987, those figures had climbed to 108% and 260%, respectively.

Today, one bank alone, Citibank, has $1.381 trillion in such items—more than the entire banking system had just seven years ago. While Citibank has the largest amount of off-balance-sheet liabilities, several other banks have a higher level of such liabilities in relation to assets.

Leading the pack is Bankers Trust, whose off-balance-sheet liabilities are 1,699% of the bank's total assets. First National Bank of Chicago has off-balance-sheet liabilities of 1,232% of assets, closely followed by Chase Manhattan Bank at 1,116%, Morgan Guaranty Trust at 1,075%, and Continental Bank of Chicago at 977%. Citibank is sixth, with 825%, followed by Security Pacific National Bank at 761%, Republic National Bank of New York at 484%, Bank of America at 482%, First Interstate Bank of California at 395%, the Bank of New York at 324%, and First National Bank of Boston at 250%.

The $6.1 trillion in off-balance-sheet liabilities of the 20 largest U.S. banks alone is nearly twice the $3.4 trillion in assets (and therefore liabilities, since total assets equal total liabilities) of the U.S. banking system as a whole as of the third quarter.

Were the off-balance-sheet liabilities reported by Weiss to be added to the "official" liabilities, the U.S. banking system would have $9.5 trillion in liabilities against $3.4 trillion in assets, making the banking system bankrupt nearly three times over.

Lyndon LaRouche warned in 1982 that the U.S. banking system was bankrupt, and advised bankers to admit their insolvency then, rather than delay it and make the system worse. Bankers, led by then-Citicorp chairman Walter Wriston, ignored LaRouche's advice and embarked on the greatest speculative binge the world has ever seen.

As a result, the U.S. banking system is insolvent beyond repair. Wriston's bankrupt Citicorp has been secretly taken over by the Federal Reserve. Even the blue-blood J.P. Morgan, the cleverest of the U.S. banks, is losing money on its banking operations. While Morgan reported a profit in 1991, the profit came from trading in securities and currencies, not banking.

Meanwhile, Bush and bankers like Wriston are pathetically trying to place the blame on federal bank regulators, in a replay of the age-old game of shooting the messenger. They should have listened to LaRouche.