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Could the truth about Citicorp finally emerge?

by William Engdahl

On Friday afternoon, Aug. 14, some minutes after 5:30, safely after close of business, the chairman of the largest bank in the United States, Citicorp chairman John Reed, revealed to friendly journalists that his bank had signed a "Memorandum of Understanding" with government regulators of the Office of the Comptroller of Currency and with the New York Federal Reserve. In his brief comments, Reed played the news down by claiming it had been signed last February and that the bank's worst problems were over. Most financial press took his words at face value.

But according to detailed reports from sources familiar with the actual state of the $214 billion Citicorp, the bank is far from healthy. Citicorp has been allowed to "get away with murder" by regulators and officials in the New York Federal Reserve, they say. The average ratio for all U.S. banks of reserve cover to total loans is 75%. Citicorp is allowed an alarmingly low 43%. By latest published figures, Citicorp has $15.2 billion in non-performing loans as of June—but only $3.62 billion as reserves set aside against these. This includes all Third World, real estate and other commercial, and consumer loans. The bank is desperately gambling, with help of apparently blind-eyed regulators, that the world real estate markets will stage an astonishing rebound.

Instead, the selloff of seized real estate from thrift institutions and foreign lenders is about to accelerate. Olympia & York's June bankruptcy filing in Toronto unleashed a deadly new wave of real estate failures and price falls across North America and Britain.

"Clearly certain U.S. banking regulators were getting nervous that Citicorp was refusing to make public its Memorandum of Understanding status," noted City of London economist Stephen J. Lewis to *EIR*. "We will see more of this in the runup to U.S. elections. Regulators remember what happened after the S&L crisis erupted in December 1988 after that election. Regulators were threatened with jail in some cases. I think some people in the civil service bureaucracy are getting nervous about continuing the coverup of some rather blatant bank regulatory practice of the past months."

Frantic coverup

Since Reed's "revelation," the Citicorp affair has disappeared from sight. It might be embarrassing for a full-scale banking crisis to erupt during the Republican convention or shortly after.

That Citicorp faced life-threatening problems, along with such other giants as Chase Manhattan and Chemical Bank, is not news. On Dec. 7, 1990, according to reports given to *EIR* then, a secret Washington meeting took place reportedly involving the highest officials of the Treasury and Federal Reserve. The subject was the insolvency (read bankruptcy) of six of the nation's largest banks. They were reported to have been: Bank of New England (since bankrupt), Manufacturers Hanover (since forced by regulators into a marriage with Chemical Bank), Chemical Bank, Security Pacific (forced to merge with Bank of America), Chase Manhattan, and Citicorp. According to banking insiders in Europe, who were made privy to some of the details of that 1990 strategy session, the administration was told that it "must act," that the federal bank deposit insurance fund had no money to bail out such combined banks, and that everything must be done to avoid word leaking out, for fear of starting a panic.

Since then, Citicorp has engaged in a dazzling array of maneuvers. A "friendly" Saudi prince, Waleed, poured almost $600 million into buying stock in the troubled bank. No doubt the U.S. troops in their country during Operation Desert Storm helped convince the Saudi royal family. But that money was a drop of water on a hot stone. On Aug. 2, 1991, Rep.

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John Dingell (D-Mich.), chairman of the House Energy and Commerce Committee, stated that Citicorp was "technically insolvent" and engaged in a "painful retrenchment, struggling to survive and, I suspect, a major recipient of the largesse of the borrowing window at the Federal Reserve."

"The problem goes back to Paul Volcker and the early 1980s when the Federal Reserve embraced the foolish idea there were banks which were 'too big to fail,' that is that if certain large banks went under it could unravel the world credit system," noted one European banker. In August 1984, the Federal Reserve rescued Continental Illinois Bank, which had a panic outflow of short-term deposits from abroad due to rumors of heavy losses in oil loans and other risks, and the notion of "too big to fail" was invented. Bankers describe it as a federal blank check that big banks could indulge in high risks, trusting that "the American taxpayer in the end will bail us out."

Caution in banking—the hallmark of the original National City Bank—was gone. Citicorp, to make up its huge losses from Ibero-American petrodollar recycling loans of the late 1970s, turned to real estate speculation and other high-risk operations to earn "fast bucks."

Excessive forbearance

"Citicorp is one giant Ponzi scheme," noted a European banker. "They have proven that it is possible for a bank to build a loan portfolio which is all bad." From California to New York, to Toronto's collapsed $25 billion Reichmann Olympia & York real estate empire, Citicorp is time and again in the middle of the biggest real estate fiascos. But what is key, is John Reed's admission that the Memorandum of Understanding had existed since February. If the bank is on the path to recovery, as Reed insisted Aug. 14, why keep such a thing secret? Would not prompt disclosure have reassured shareholders that all necessary steps were being taken?

The February timing is revealing. According to a comment by retired Federal Deposit Insurance Corp. chairman William Seidman to the *American Banker* of Aug. 18, when Citicorp signed the memorandum, it was added to the FDIC list of "problem banks." Normally the FDIC never reveals names of problem banks, but it does publish a total of assets of all banks on its problem bank list. Last February the size of such problem bank assets jumped by $200 billion to $613 billion—by more or less the size of Citicorp's assets.

Also in February, New York Federal Reserve chief Gerald Corrigan called the governor of the Bank of Japan, Yasushi Mieno, to an unpublicized meeting in New York. According to reliable London sources, Corrigan urged Mieno to take steps to prevent Japanese banks from liquidating their considerable holdings in U.S. real estate, stocks, and bonds. Corrigan knows well that given the alarming and continuing fall in Japanese real estate and stock prices, a liquidation of an estimated $80 billion in loans to U.S. real estate projects as well as added tens of billions in holdings of U.S. Treasury bonds and stocks would pull the plug on the fragile U.S. banking system. Corrigan's staff had just completed a study of foreign bank lending to U.S. corporations which confirmed the extent of Japanese involvement. Among the first to be hit in any Japanese selloff, Corrigan no doubt calculated, would be Citicorp and Chase. FDIC resources would be unable to deal with the crisis.

When Mieno returned to Tokyo, the Nikkei Dow stock index stood at some 23,000 yen. Today it is barely above 14,000 yen. Japanese banks are estimated to be sitting on $220 billion of bad real estate loans, six months or more in arrears. Yet, according to reliable Tokyo reports, Japanese banks and insurance companies have not sold U.S. assets to raise badly needed cash at home.

According to a recent statement by Charles Bowsher, head of the Congressional General Accounting Office, the FDIC—the agency created in the wake of the 1933 bank holiday—is too shaky to withstand the shock of *one* large bank failure. So long as depositors knew their deposits were guaranteed by the U.S. government up to $100,000 per account should a bank fail, panic runs were contained. But what if the government's own FDIC Bank Insurance Fund were insolvent because of record numbers of bailouts?

On June 10, in testimony dutifully buried by the media, FDIC chairman William Taylor told the Senate Banking Committee that the Bank Insurance Fund "ended 1991 with a deficit of approximately $7 billion." Its only present source of money is increased assessments of member banks—or emergency loans from the Treasury. The FDIC fund paid out $7.4 billion in 1991 alone for failed banks. The $613 billion in assets of FDIC-rated "problem banks" is 50% higher than only 12 months ago. It comprises almost 20% of the total assets of the almost 12,000 banks in the U.S. commercial banking system.

According to the cited *American Banker* report, Citicorp did not convene its after-hours press briefing because it wanted to set a standard of truthfulness. It was forced. Reportedly, a behind-the-scenes battle pits Corrigan's New York Federal Reserve and those who want to cover up the gravity of the Citicorp crisis, against regulators in the office of the Comptroller of the Currency who insist that the legal requirements must be faced openly. Some Washington bureaucrats are getting nervous that a new administration could be elected, and that they may face criminal action if they do not act.

Since March, say banking sources, congressional Democrats and the Republican White House have tacitly agreed to keep the banking crisis out of the elections. Both parties allegedly know the system is on the brink; neither wants to be blamed for a blowout before the November elections. This has led some Senate staffers to refer to a "December Surprise" for the next President, like what FDR faced in early 1933. But unlike 1932, the very solvency of the U.S. government is in doubt. Official federal debt nears $4 trillion; annual deficits add $400 billion yearly to this. These sums could double after November, when the postponed crisis will hit the unwitting American citizen.