Report from Bonn by Rainer Apel

Some progress on derivatives

Finally, a few politicians are beginning to take notice of the meltdown of the international financial system.

In September 1993, at a time when U.S. Rep. Henry Gonzalez (D-Tex.) began to put the high risk involved in speculative money dealings on the House Banking Committee agenda, this writer tried to talk to German Social Democrats, who were gathering for their national party convention in Wiesbaden, about the danger of derivatives—with little success.

Ingrid Matthäus-Maier, for example, the official Social Democratic Party (SPD) financial and budget policy spokeswoman, said that she did not think the time had come to deal with the derivatives issue. She seemed uninterested in the Gonzalez initiative. Other SPDers gave the same impression. Generally, the opposition SPD, which should have used the volatility of the financial system to challenge incumbent Chancellor Helmut Kohl's alleged economic "success story" during the 1994 elections, did no such thing. No initiative against speculation, no proposal that went beyond calls for some budget cuts here and there. This is how the situation looked until March 1995.

The collapse of Barings Bank has changed the picture significantly. Now, the Social Democrats have launched a "grand motion" that calls for a plenary session of the parliament to discuss the problem of derivatives and other speculation.

The motion is signed by, among others, the same Ingrid Matthäus-Maier who ignored the problem 18 months ago, and by party chairman Rudolf Scharping. It explicitly refers to the Barings case as one that dramatically underlines the urgency of political action.

The motion, which was presented in Bonn on March 19, voices profound doubt concerning statements such as that of Finance Minister Theodor Waigel, that Germany's banks, industry, and public sector entities are safe from Barings-style collapse, that "nothing like that could ever happen here." It states that the insolvencies at the Metallgesellschaft group and the Balsam group that were linked to losses in derivatives, document quite the contrary of what Waigel has said.

In the form of 20 questions, the motion recommends that the government tell what it currently knows about the problem, what actions it plans in order to monitor and contain the risk of derivatives, and what options it sees for making reports on "money at risk" mandatory in banking, industry, and public sector institutions.

As an aide to the SPD in the parliament told this writer, the initiative is aimed at getting a "first overview" of the problem, and it is expected that in late April or early May, the parliament will bring up the issue in a plenary session.

Until then, the financial policy committee passed a resolution on March 20 that calls for upgraded monitoring of the derivatives role in speculative deals, and for debate on the fine-tuning of controls and reserve requirements.

Also on March 20, the Federal Accounting Office (BRH) made it known that it is considering an official probe into public sector involvement in derivatives, after it had received alarming information that not only banks and industrial enterprises, but also municipalities, states, and the federal government have already become deeply engaged in derivatives.

The federal Ministry of Finance admits it is involved in derivatives, but it is trying to play down the issue, explaining that it does so "only for concrete credit projects and only to minimize the interest burden." The BRH intends to convene a special session, to examine the extent of public sector involvement.

The BRH is alarmed over the attitude of several state governments that have informed the supervisory agency that they have derivatives engagements, indeed, but that these are below the level of the state government of Schleswig-Holstein, which is financing 50% of its new borrowings through derivatives transactions.

While there is some transparency on the scope of the exposure on the federal and state levels, the scope of municipal derivatives dealings is murky. In light of the recent Orange County, California disaster in the United States, the BRH wants to look more closely into municipal exposure. It is this area of financial policy that has been neglected by the experts, and "some very bad surprises" can be expected, the aide to the SPD parliamentary group said.

However, most politicians who have finally begun to make the risk of derivatives a public issue, will still not go farther than to suggest that regulations be imposed on the so-called "excesses," and leave the derivatives market as such untouched. So far, while the debate is just beginning, Edgar Meister, a member of the central bank board, has been the only senior banking official to call for harsher measures. In an interview in the weekly *Wirtschaftswoche* on March 17, Meister endorsed "any kind of proposal to restrict purely speculative transactions." He added that one "should not concentrate on excesses, but rather on the causes which are still in the political and economic domain."