

Global reorganization and the cartel of doom

by John Hoefle

When analyzing the activities of the international financial oligarchy, it is useful to compare what they actually do, to what they publicly claim they are doing. From that perspective, we shall examine the wave of mergers and acquisitions sweeping the world. What is occurring is not the “trees” of individual mergers, but rather a “forest” of a global reorganization and cartelization.

The current wave of consolidation dwarfs the leveraged-buyout wave of the “go-go” 1980s, with more mergers announced in 1998, in terms of price, than during the entire period from 1985 through 1990, and more than four times the total for 1989, the year of the infamous “Barbarians at the Gate” buyout of RJR-Nabisco by takeover bandits Kohlberg Kravis Roberts (KKR).

A record \$2.5 trillion in takeover bids were announced during 1998, compared to \$1.6 trillion in 1997 and \$1.1 trillion in 1996—and compared to \$568 billion in 1989, the high-water mark of the 1980s (Figure 1). The pace this year is even higher, with more than \$1.3 trillion in mergers announced as we approach the first half of 1999.

Invariably, these mergers are presented to the public as soap operas: Who wins, and who loses? Which chief executive will get the top spot? Which city will get the headquarters? How many people will lose their jobs? What will Wall Street think? Will the stock go up or down?

This process of consolidation is, in and of itself, bad for the economy, because it destroys the layer of small and medium-sized companies from which so many scientific and technological breakthroughs have come, and throws hundreds of thousands of employees out onto the street. The larger the corporation, and the more focussed it is on the “bottom line,” the more it stifles creativity. As General Electric chairman Jack Welch might say, “We make money, not products.”

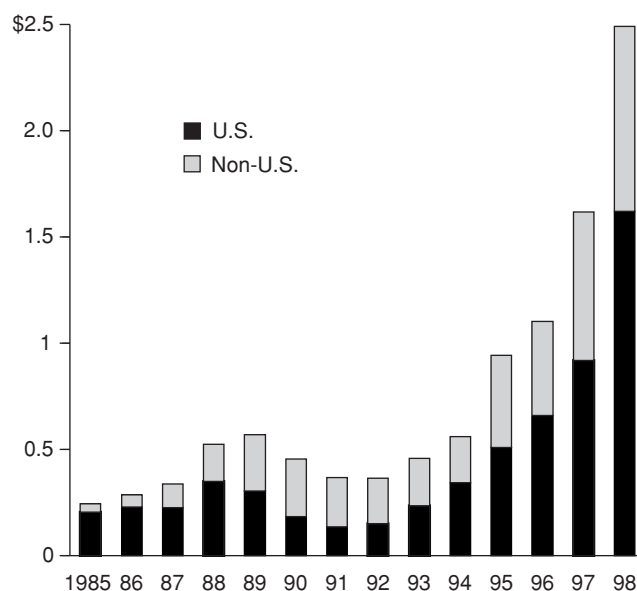
As bad as that is, it gets worse.

Post-crash positioning

Driving this frenzy of consolidation and restructuring, is the knowledge that the present global financial and economic system is doomed. The battle, as the more clever players know, is to shape—and carve out a position of power in—the system which follows.

Many of the institutions which seem so powerful today,

FIGURE 1
Global cartelization escalates: value of announced mergers and acquisitions (trillions \$)



Source: Securities Data Co.

will simply disappear. This is already occurring in the financial sector, where some of the more famous names in history—Barings, for example—have crumbled. The layer of banks and financial services companies which grew up with the bubble, is now threatened with extinction; if the bubble goes, they go with it. The rash of mergers in the financial world reflects the attempt by the financial oligarchy to create institutions so big, and so powerful, that they can dictate the terms of surrender to the nations of the world.

As bad as these bubbleheads are, an even nastier group lurks behind them, moving to seize control over the productive processes and infrastructure necessary for humanity to survive. After a crash, those who survive will still need food,

water and energy, health care, telephone service, and the like, and those who control those necessities will have great power. Those who can pay the cartels might survive; those who can't, will die.

This is what ultimately stands behind the merger mania.

Monopoly money

The merger wave of the 1980s occurred mainly via leveraged buyouts (LBOs), funded by junk bonds. Asset-strippers like KKR and the group known as “Milken’s Monsters” would buy public companies, then have those companies issue junk bonds to cover the purchase price. Later, after some serious looting, these companies would be sold back to the public. The impact of the takeover bandits went far beyond the companies they targeted, though, by creating an environment in which companies, terrified that they might be the next victim, turned to investment bankers for protection. Like cattle, they were herded right into the slaughterhouse.

The LBO mergers were limited by the amount of junk bonds and related paper which could be sold. KKR’s \$26 billion takeover of RJR-Nabisco marked a peak in the merger wave, in large part because it used up much of the available money.

That was, in these days of “Internet time,” a long time ago. Today, with the stock market several times higher than it was back then, a new currency has arisen: stock. Today’s mergers are being financed mainly via stock swaps, the buyer giving its own stock, rather than cash, to the shareholders of the company being acquired. Given the absurdly high valuations of stock these days, companies can seemingly afford to pay incredible prices. The RJR-Nabisco deal, once so large that it was breathtaking, would barely make the top 25 today. Even WorldCom’s shocking \$37 billion bid for MCI Communications in 1997, would be considered a mid-level deal today, compared to Exxon’s \$86 billion takeover of Mobil, and a raft of \$70 billion deals (Travelers-Citicorp, SBC-Ameritech, Bell Atlantic-GTE, and AT&T-TCI).

Through the use of stock swaps, mergers which were once impossible, are now commonplace. But treating this monopoly money as if it were real, has its dangers, as shown by the Travelers-Citicorp merger. At the time of the deal, Travelers agreed to give Citicorp shareholders a specific number of its own shares. The morning the announcement was made, those Travelers shares were worth \$72 billion; by the end of the day, they had zoomed to more than \$80 billion. However, by the time the deal closed and the shares changed hands, Travelers’ stock had fallen to the point that the shares pledged to Citicorp’s owners were worth a mere \$37 billion—or roughly half of the original purchase price.

Banking and finance

Lyndon LaRouche has aptly compared the mergers of the big banks and other financial institutions to two drunks,

leaning on each other in order to keep standing. Most of the big bank mergers have been organized by the central banks, to hide the bankruptcy not only of the individual banks, but of the banking system itself.

In the United States, the Federal Reserve has played a key role in the consolidation, dating back to the merger frenzy of the 1980s—including the “S&L crisis” of the late 1980s, which transferred trillions of dollars in assets to the banks, and billions of dollars of losses to the taxpayers.

During the 1980s, aided by the formation of the Reagan/Bush bubble and significant deregulation of the banking system, mergers among U.S. banks rose sharply (**Figure 2**). While the number of mergers peaked in 1988, the consolidation is actually escalating, with bigger banks now merging. There are now fewer banks in the United States than at any point since the Great Depression, and the dominance of a handful of giant banks is steadily growing.

As of March 31, 1999, there were 8,721 commercial banks in the United States, a decline of 40% from the 14,496 banks at the end of 1994 (**Figure 3**). The number of savings institutions, which peaked at 3,677 in 1986, has fallen to 1,669, a decline of 55%, and the assets held by savings institutions has dropped from \$1.6 trillion in 1988 to \$1.1 trillion today, a decline of 31%.

According to the Federal Deposit Insurance Corp., of the \$5.4 trillion in assets held by all U.S. banks on March 31, 1999, roughly \$3.5 trillion (65%) were held by the 73 banks with assets of more than \$10 billion, compared to \$901 billion in assets held by the 317 banks with assets of \$1-10 billion; \$727 billion in assets were held at the 2,956 banks with assets of \$100 million to \$1 billion; and \$251 billion in assets were held by the 5,375 banks with assets of less than \$100 million.

The concentration is even greater when one looks at the bank holding companies. As of the end of 1998, the 10 largest bank holding companies held 55% of all U.S. bank assets, and the top 25 held 71% of all assets. By comparison, the 10 largest U.S. banks held just 28% of U.S. bank assets at the end of 1985. The two largest U.S. bank holding companies at the end of 1998 (Citicorp, \$689 billion in assets, and BankAmerica, \$618 billion), had one-third more assets than all 8,382 banks with less than \$1 billion in assets combined.

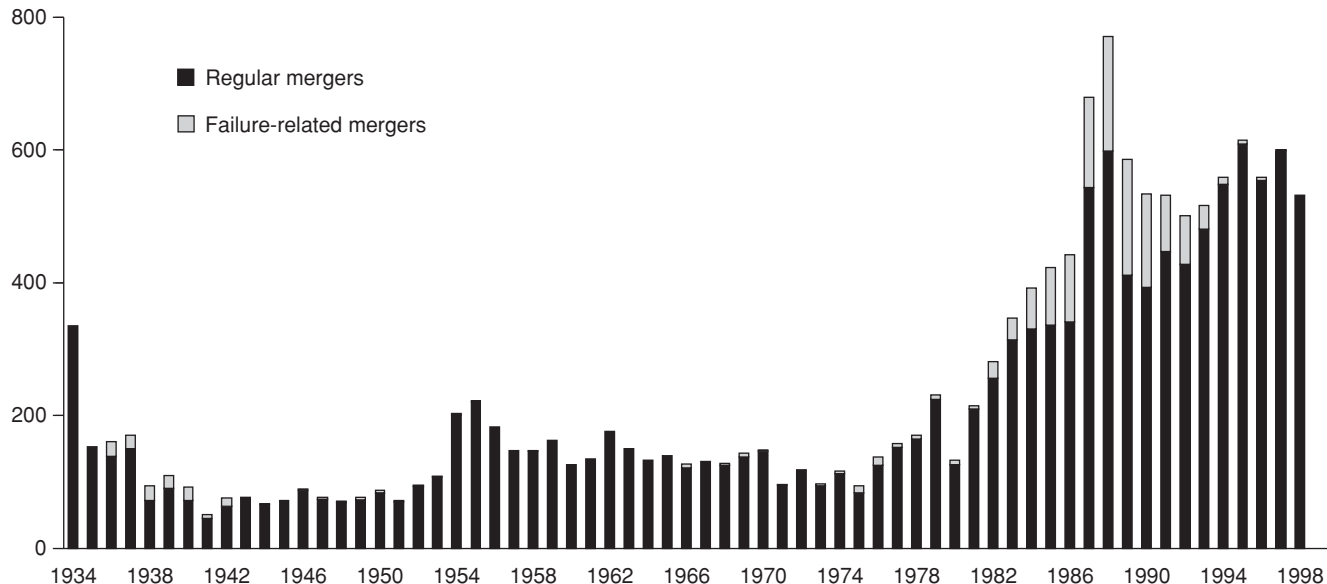
Globally, more than \$360 billion in mergers involving commercial banks were announced in 1998, up from \$158 billion in 1997. The biggest bank in the world, as of this writing, is Germany’s Deutsche Bank, with assets of some \$800 billion, followed by Switzerland’s UBS, at \$750 billion; Citigroup; Japan’s Bank of Tokyo-Mitsubishi, at \$650 billion; and BankAmerica. All of the top 10 had assets well over \$400 billion. Ten years ago, the largest bank in the world was Japan’s Dai-Ichi Kangyo, with \$270 billion in assets.

The investment banks have also been merging. The once-powerful Salomon Brothers was acquired by Travelers for

FIGURE 2

U.S. commercial bank mergers

(number of mergers)



Source: Federal Deposit Insurance Corp.

\$8.9 billion and merged with Smith Barney (and is now part of Citigroup), while the white-shoe Morgan Stanley was bought by the more pedestrian Dean Witter Discover for \$10.6 billion. The investment bank/securities dealer sector was the third most active sector for U.S. M&A deals in 1997, with \$59 billion in deals compared to \$16 billion in 1996. (The 1997 deals represented 38% of all domestic brokerage M&A deals since 1980, according to Securities Data Co.)

Insurance companies are also cashing in on the merger craze. American International Group recently bought SunAmerica, Crédit Suisse bought Winterthur, and Warren Buffett's Berkshire Hathaway bought General Re.

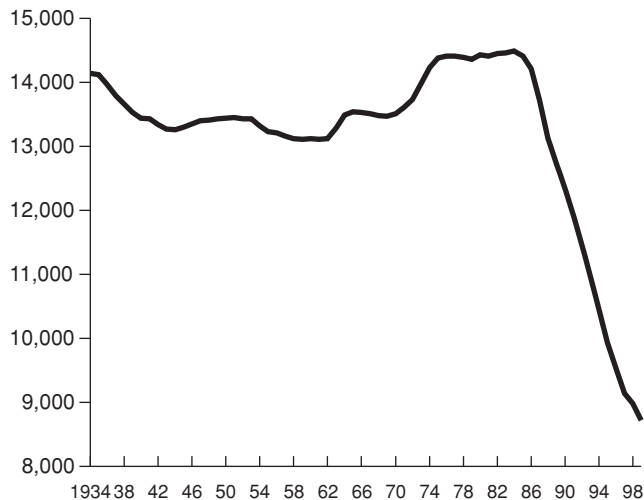
On top of all this, one can add the reorganization under way on the world's stock, commodity, and derivatives exchanges, with their consolidations, alliances, and headlong rush into electronic trading. With more than a quadrillion dollars a year in annual financial turnover, the casinos are having trouble keeping up with all the bets.

Telecommunications

Running neck-and-neck with the commercial banking sector for the lead in mergers over the last few years, has been the telecommunications sector, led by consolidations among existing phone companies, the privatization of state-owned phone companies, and the spread of wireless networks. The

FIGURE 3

The number of U.S. banks is shrinking



Source: Federal Deposit Insurance Corp.

largest merger bid ever announced, Deutsche Telekom's \$92 billion bid for Telecom Italia in April 1999, ultimately failed because of political considerations and a subsequent bid from Olivetti.

TABLE 1

Recent mergers and acquisitions

Buyer	Target	Value (billions \$)	Date Announced
Deutsche Telekom	Telekom Italia	92.3	Apr. 1999
Exxon	Mobil	86.4	Dec. 1998
Travelers Group	Citicorp	72.6	Apr. 1998
SBC Communications	Ameritech	72.4	May 1998
Bell Atlantic	GTE Corp.	70.9	Jul. 1998
AT&T	Tele-Communications Inc.	68.3	June 1998
Vodafone Group plc	AirTouch Communications	65.9	Jan. 1999
AT&T	MediaOne Group	63.1	Apr. 1999
NationsBank	BankAmerica	61.6	Apr. 1998
Comcast Corp.	MediaOne Group	58.2	Mar. 1999
Ing. C Olivetti & Co. SpA	Telecom Italia	56.0	Feb. 1999
British Petroleum plc	Amoco Corp.	54.3	Aug. 1998
Global Crossing Ltd.	US West	51.1	May 1999
Daimler-Benz AG	Chrysler	39.5	May 1998
American Home Products Corp.	Monsanto Corp.	39.1	June 1998
WorldCom Inc.	MCI Communications	34.6	Oct. 1997
Carrefour SA	Comptoirs Modernes SA	34.4	Aug. 1998
Norwest Corp.	Wells Fargo & Co.	34.4	June 1998
BP Amoco	Arco	33.7	Apr. 1999
Zeneca Group	Astra AB	31.8	Dec. 1998
Banc One	First Chicago NBD	29.6	Apr. 1998
GTE Corp.	MCI Communications	29.0	Oct. 1997
Rhone-Poulenc SA	Hoechst AG	26.5	May 1999
Bank of New York	Mellon Bank Corp.	24.2	Apr. 1998
Berkshire Hathaway	General Re Corp.	23.3	June 1998
Union Bank of Switzerland	Schweizerischer Bankverein	23.0	Dec. 1997
Lucent Technologies	Ascend Communications	21.1	Jan. 1999
Banque Nationale de Paris	Paribas	19.0	Mar. 1999
Banque Nationale de Paris	Societe Generale SA	18.7	Mar. 1999
Zurich Versicherungs GmbH	BAT Industries plc-Financial	18.4	Oct. 1997

Source: Securities Data Co.

Much of the telecommunications activity has taken place in the United States, where the seven original Baby Bells have been reduced to four, via mergers (pending and completed). SBC Communications, formerly Southwestern Bell, bought fellow Baby Bell Pacific Telesis in 1997, and in 1998 cut a deal to buy Ameritech, the new name for Illinois Bell. Bell Atlantic, the mid-Atlantic Bell, bought NYNEX, the New York-New England Bell company, in 1997, and reached a deal last year to buy GTE. Besides SBC and Bell Atlantic, only Bell South and US WEST remain, and US WEST is considering a bid from Global Crossing, the investment bank/long-distance carrier, which is also buying Frontier, another long-distance carrier.

AT&T, the largest U.S. long-distance carrier, has also been busy, converting itself into the largest cable-television

company in the nation, with its purchases of Tele-Communications Inc. and MediaOne. Its top U.S. rival, MCI World-Com, has extensive Internet operations through its UUNET subsidiary.

In addition, several of these companies have invested heavily in the former state-run phone systems in Ibero-America, eastern Europe, and Asia, and in wireless phone networks worldwide, as have the major European phone companies.

Oil and raw materials

The oil business has always been dominated by a handful of giant companies, and that control has been concentrated by a recent spate of giant mergers. The original Seven Sisters have been reduced to five, thanks to Exxon's acquisition of Mobil (reuniting the two biggest spinoffs of the old Standard Oil Trust), and Chevron's 1984 acquisition of Gulf. Today, three Sisters dominate: Exxon-Mobil; BP Amoco (formed by British Petroleum's acquisition of Amoco, and its pending takeover of Arco); and Royal Dutch/Shell. The other two Sisters, Chevron and Texaco, recently cancelled their own merger talks. There have also been a large number of mergers among smaller oil- and gas-producing and service companies, chemical companies, and other raw materials companies.

Pharmaceuticals

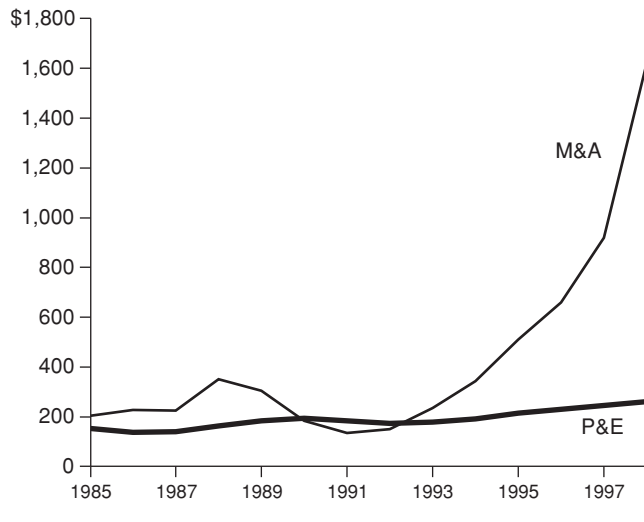
The pharmaceutical industry is another sector where rapid consolidation is taking place. In 1995, British drug companies Glaxo and Wellcome merged to form Glaxo Wellcome, and Pharmacia merged with Upjohn; and in 1996, Swiss giants Ciba-Geigy and Sandoz merged, creating Novartis. Currently, Sweden's Astra and Britain's Zeneca are merging into AstraZeneca, and France's Rhône-Poulenc and Germany's Hoechst (which bought Marion Merrell Dow and Roussel Uclaf in 1995) are creating Aventis. American Home Products bought American Cyanamid in 1996. The result will be five giants with annual sales in the \$10 billion range: AstraZeneca, Aventis, Glaxo Wellcome, Merck & Co. and Novartis. In 1998, the top 10 pharmaceutical companies accounted for \$91 billion—36%—of the industry's \$252 billion in sales, and the top 20 accounted for 57%, according to IMS Health.

There has also been a pattern of drug companies buying

FIGURE 4

Mergers and acquisitions vs. manufacturing expenditures for new plant and equipment

(billions \$)



Source: Securities Data Co., Economic Report of the President, *EIR*.

pharmacy benefit managers, such as Eli Lilly's purchase of PCS (which it recently sold to CVS) and the push by the big drug chains (Walgreen, CVS, RiteAid, and Eckerds) to displace the smaller pharmacies, as part of the overall move to "managed care."

Food and agriculture

The food sector has also seen its share of mergers. Cargill, the world's largest grain trader, bought the grain operations of Continental Grain, and there has been a consolidation among the seed companies, including the purchase by Du Pont of the remainder of Pioneer Hi-Bred that it did not already own. The grocery store sector has also seen a jump in concentration, with Kroger buying Fred Meyer (which bought Food 4 Less and Smith's Food and Drug Centers), and Albertson's buying American Stores. The Netherlands' Royal Ahold recently bought the Washington, D.C.-area Giant supermarket chain from Britain's Sainsbury, making it the fifth-largest grocery chain in the United States—and growing. Meanwhile, the farmers who actually produce the food are rapidly being driven out of business. (See article p. 47 on hog cartel.)

These are just a few examples of the merger mania spreading around the world. On a smaller scale, are the mergers and privatizations in the electric, gas, and water utilities. There are also the mergers which will flow from the drop in commodity prices, as a result of the reduced market demand which follows the decline in physical production and consumption in

areas hit by collapse.

A big part of the problem, is the growing disassociation between industrial companies and the industrial processes upon which they are supposedly based. As the economic collapse deepens, the level of merger activity is rapidly increasing, as the drunks try desperately to prop each other up. The amount of money being spent on mergers and acquisitions in the United States, now dwarfs the amount of money being invested in new manufacturing capacity (Figure 4). These companies are not building for the future; they are looting it.

Take, for example, General Electric, a company which traces its roots back to the research laboratory of Thomas Edison, and was once one of the leaders of the industrial revolution. Once upon a time, GE's identity lay in the products it designed and built. Under its current chairman, Jack Welch, GE has become something much different, a company which earns half of its income from the manipulation of money. Welch has bought and sold hundreds of companies during his tenure, weeding out companies and managers who failed to generate the expected contributions to GE's bottom line. GE's mission of building the world, has been replaced by a determination to produce ever-increasing earnings, and a higher stock price.

For his role in post-industrializing GE, Welch has been lionized as a model for a whole new generation of "bottom line" corporate executives.

Another example of this disassociation is Douglas Yardley, chief executive officer of copper producer Phelps Dodge. Phelps Dodge has stated that it requires a copper price of between 65¢ and 70¢ a pound, in order to break even, and one would think that with copper in the 61¢ range, the company would want the price to rise. But not Yardley. Yardley would prefer a lower price, to run some of his competitors out of business.

"I've said to anyone who would listen that the best thing that could happen to this industry is 55¢ copper for six months to a year," Yardley recently told *Barron's*. "That would clear it out in a hurry. This 70¢ stuff is slow death."

Barron's, published by *Wall Street Journal* publisher Dow Jones, clearly shares this insane view. The weekly has said that lower prices would impose "discipline" on the copper market and "eliminate marginal operators." According to *Barron's*, there is simply too much copper on the market, with a 6.2-week supply, compared to a 3.6-week supply a year earlier.

That these so-called captains of industry prefer cost-cutting and cartelization to launching an emergency effort to rebuild the world's productive sector, is indicative of the utter failure of Western corporate leaders to understand the first thing about real economics. By becoming more interested in making money than in making products, they have sealed their own doom, and face a cartel with far more power than their own—that of the Four Horsemen of the Apocalypse.