

U.S., Japan, Germany Bank Systems Melting

by Richard Freeman

The United States' bank regulatory agencies' annual review of syndicated loans in the country, called the "2002 Shared National Credit Review," has opened eyes about the true state of America's banking system. The report, released Oct. 8, shows that between 2000 and 2002, the percentage of loans that are classified as "adversely rated or troubled" has more than doubled. Exemplifying the crisis, the next day Moody's Investor Services downgraded, once again, the long-term debt of America's second-largest bank, J.P. Morgan Chase.

This crisis is clearly not confined to the United States. Japan's government has announced its third major bank "reorganization/bailout" program since 1998. Japanese banks have more than \$1 trillion in non-performing loans. In Germany, Commerzbank—once a titan of that nation's banking sector—is melting away, having lost, since January 2000, 88% of its stock value, and rumored suffering major derivatives losses.

Never in post-World War II memory, have the banking-financial systems of the three major economic powers—the United States, Japan, and Germany—experienced such crises simultaneously. Combined, these banking systems possess between two-fifths and two-thirds of the assets of the world's banking system. The breakdown conjuncture of these nations' interconnected bank systems defines a crisis point of the world financial system.

More and More Troubled Loans

The Shared National Credit Review (SNCR) is compiled once each year by the three major American bank regulatory agencies—the Federal Reserve Board of Governors, the Office of the Comptroller of the Currency (OCC), and the Federal Deposit Insurance Corporation (FDIC).

The SNCR reports on two broad categories of what it calls "adversely rated," or in common parlance, troubled loans. The first category is defined as "classified loan commitments," or "loans that have well-defined weaknesses." This includes loans that are a) substandard; b) doubtful; or c) in default/loss. The second type of adversely rated loans is that of "special mention loans," which are loans that "exhibit potential weaknesses, which may result in further deterioration if left uncorrected." These are not yet "classified," but are headed in that direction.

Table 1 shows the story. What is stunning is the increase in the volume of troubled "classified loan commitments," from \$22 billion in 1997, to \$157 billion in 2002, a sevenfold increase (within this category, the loans in default leapt from \$0.9 billion in 1997, to \$19.6 billion in 2002). Moreover, just between 2000 and 2002, "adversely rated loans" as a portion of total loan syndication commitments more than doubled, from 5.1% to 12.6%.

The telecom sector represents a problem spot: 44% of the syndicated loans to that sector are "adversely rated."

Compounding the problem is the high rate of indebtedness: David Gibbons, who is the OCC's deputy comptroller for risk, told the Oct. 9 *New York Times*, "We still have a lot of leverage in the system." The average corporation has debt that is 6.1 times its cash flow, based on an analysis of Federal Reserve data. That is a greater debt burden than corporations carried during the last two recessions, according to Gibbons.

Exemplifying the American banking system's overall crisis is the giant J.P. Morgan Chase Bank's evaporation. On Oct. 9, Moody's Investor Services cut its rating on Morgan Chase's long-term debt, by one notch, down to "A1," which is its fifth-highest grade. This affects the rating on \$42 billion

TABLE 1

Loans Commitments That Are Troubled in the United States

(\$ Billions)

| Year | Classified Loan Commitments | Special Loans | Total Adversely Rated Loans | Total Loan Commitments | Adversely Rated as % of Total Commitments |
|------|-----------------------------|---------------|-----------------------------|------------------------|---|
| 1997 | \$22 | \$20 | \$42 | \$1,435 | 2.9% |
| 1998 | 22 | 23 | 45 | 1,759 | 2.6% |
| 1999 | 37 | 31 | 68 | 1,829 | 3.7% |
| 2000 | 63 | 36 | 100 | 1,951 | 5.1% |
| 2001 | 118 | 75 | 193 | 2,050 | 9.4% |
| 2002 | 157 | 79 | 236 | 1,871 | 12.6% |

Source: 2002 Shared National Credit Review.

of Morgan Chase's long-term debt. J.P. Morgan Chase, with \$713 billion in assets, is the world's leading derivatives bank, with \$26 trillion in such highly leveraged bets. Since the start of 2001, Morgan Chase's market capitalization has gone down from \$106.5 billion to \$33 billion. Morgan Chase is undergoing a death seizure which mirrors that which Enron experienced during 2001, where each month, it shrinks further.

Morgan Chase Chairman William Harrison has announced that he plans to fire 20% of the bank's investment banking division, which employs 20,000 people. (This would bring the number of workers fired at all divisions of Morgan Chase to 14,000 since the merger of J.P. Morgan and Chase Manhattan banks in December 2000.) On Oct. 9 the *Financial Times* reported a joke making the rounds on Wall Street, to the effect that a newspaper headline will soon appear, reading, "J.P. Morgan To Cut Workforce 120%." The same day, *Financial Times* "Lex Column" called Morgan's firings "haircuts [that] are getting close to the scalp—which may be in line with prevailing fashion, but makes each round harder to handle without damaging the franchise."

Japan and Germany

Bank of Japan (BOJ) Governor Masaru Hayami announced on Oct. 11, "The strength of [Japan's] banks has declined and the market's trust has been damaged. If there is a crisis, we will serve as lender of last resort." There will be the third banking system "reorganization/bailout" since 1998. The BOJ will attempt a very delicate operation in which Hayami will try to facilitate the purchase and write-off of bank bad paper, while continuing the functioning of Japan's heavy industrial enterprises.

In Germany, Commerzbank was hurt further by an early-October memo from Merrill Lynch, reporting that Commerzbank has sustained credit derivatives losses. Commerzbank's stock fell from 44 euros in 2000, to 5.3 euros on Oct. 8. Moreover, the market share price of other financial institutions which make up Germany's main stock index, the Dax-30, have also experienced huge losses: Bayerische HypoVereinsbank, -84%; Deutsche Bank, -64%; Allianz/Dresdner Bank, -83%; Münchner Ruck, -75%; and MLP, -96%. The entire market capitalization of these six banking firms plummeted from a combined 330 billion euros in 2000, to just 71 billion euros in early 2002, a fall of 78%.

The collapse of the physical economies of these three nations is accelerating the banking-financial crisis.

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South African Strike Exposes False Choices

by David Cherry

At the ruling African National Congress's policy conference in Johannesburg in late September, with the national trade union strike in prospect, South African President Thabo Mbeki angrily declared that the ANC was "under attack from domestic and foreign left sectarian factions" who accuse the party of turning its back on the poor. He was absolutely right. The jackals are gathering to feed on the discontent and misery partly unavoidable in the immediate post-apartheid years, but which are increasingly the consequence of the globalization and privatization policy into which President Mbeki himself has been steered by his Anglo-American self-declared "friends." South Africa can be brought to its intended end as a "failed state" by the policies of the left, or by Mbeki's own policies, or by the two in competition. But it need not happen.

Africans have difficulty believing that the Anglo-American powers contributed to the ending of apartheid for the purpose of imposing on the entire continent a combination of policies of differing political stripes that is even worse. It is a replay of the British use of its drive against the African slave trade in the 19th Century to seize much of the continent—but now with much greater human suffering in prospect. These are the policies of principalities and powers that are imposed by polite, friendly, and apparently well-intentioned people who are, nonetheless, the walking dead.

Trade Unions Offer No Alternative

The occasion for President Mbeki's attack on "domestic and foreign left sectarian factions" was the approach of the national strike of Oct. 1-2 led by the Congress of South African Trade Unions (COSATU), a member—along with the ANC and the South African Communist Party (SACP)—of the now strained tripartite governing alliance. Statements by Mbeki indicate that he blames COSATU for being guided by these "factions." We are confronted with a picture of President Mbeki and the ANC leadership on one side, and COSATU and the SACP on the other, playing out their scripted parts in a variation of what has already happened in other countries such as Peru, Mexico, and Colombia, leading to the destruction of national sovereignty and potential for development.

For his part, Mbeki supposes that a global financial system that is collapsing will fulfill its promises to inject capital to help develop the country, so long as free trade and privatization inducements are provided. In Mbeki's reckoning, a social