Permanent or temporary?

Banks get part ownership of Chrysler under the new de facto bankruptcy reorganization.

Chrysler Corporation was put through a second limited bankruptcy reorganization Jan. 14. The reorganization was worked out at a meeting of the three-member U.S. Chrysler Loan Guarantee Board, the United Autoworkers (UAW), Chrysler Corporation, and Chrysler's creditors, and cleared the grounds for Chrysler's merger with other companies. It is not yet clear whether this new agreement will be sufficient to salvage Chrysler from full-scale bankruptcy and liquidation.

The terms of the agreement include:

1) The $72 million in "sacrifices" by Chrysler's suppliers:

2) Very harsh sacrifices from the Chrysler labor force. The UAW has agreed to forego for the next 21 months' cost-of-living adjustments and wage increases totaling $622 million. UAW President Doug Fraser called the agreement "the worst economic settlement" he had ever negotiated.

Another $161 million in wage cuts was applied to Chrysler's non-union workers.

3) The settlement of $1 billion in debt owed by Chrysler to a consortium of 200 banks and insurance companies. One-half of this debt was paid to the Chrysler creditors at the rate of 30 cents on the dollar. The other half was converted into preferred stock issued to this consortium of banks.

It is this second part of the debt settlement that is the key to the Chrysler bankruptcy reorganization and will help explain what may be happening to Chrysler in the days ahead.

By the terms of the debt-to-stock conversion plan, Chrysler will issue approximately 20 million shares to this consortium of banks, led by Manufacturer's Hanover, Chase Manhattan, and Citibank at $25 per share. This would make the consortium the largest holder of preferred stock in Chrysler Corporation, giving them one-fifth ownership of all Chrysler shares outstanding, common and preferred, which (including the new issuance of preferred) will total about 90 million shares.

Bank ownership of Chrysler would be in violation of the Glass-Steagal Act that specifically prohibits banks from owning any industrial corporation. In this aspect alone, the Chrysler reorganization constitutes a dangerous precedent.

There is more. While the 20 million shares of Chrysler preferred stock that the banks will hold (if Congress approves the agreement) are not known immediately to carry voting rights, that may be a moot point.

The preferred stock will apparently carry the equivalent of voting rights in the form of management controls, written into specific covenants. In particular, the preferred stock issue stipulates, it is believed, definite accrued dividend levels, as well as retained earnings levels, working capital levels, and other performance levels that Chrysler must maintain.

According to one source close to the Department of Transportation, "If Chrysler defaults on these performance levels then it is possible this banks' consortium may be able to have two people on the board of directors."

Such preferred stock gives banks like Manufacturers Hanover, Citibank, and others a clear shot at some of the valuable assets in the event of Chrysler's liquidation, while the arrangement gives Chrysler some breathing room.

Currently, Chrysler has all 40 of its production, assembly, and other plants on the North American continent shut down. Chrysler shut down most of these plants in the first week of December and halted its remaining K and J car output on Dec. 21-23.

Chrysler is now living off its car inventories. This keeps costs to a minimum and brings in new cash flow. But Chrysler still owes its suppliers $300 million, and this amount is growing by $50 million per week.

The elimination of a large amount of Chrysler senior debt may clear the way toward a merger. It it easier to sell a company which has a lot of equity outstanding than it is to sell a company with a lot of debt that must be paid off soon by the prospective buyer.

Such a merger could conceivably work. If the Reagan administration reduces interest rates, overrides the tendency that New York banks would have for asset-stripping Chrysler, and gets the economy going, Chrysler will have a slim chance of survival.