

# Business Briefs

## Finance

### Will Greenspan End Up in the Tower?

On Sept. 26, Federal Reserve Chairman Alan Greenspan received the great honor of being turned into a “Knight Commander of the Order of the British Empire” (KBE) due to his “outstanding contribution to global economic stability.” Before the ceremony at the Queen’s Balmoral Castle, Greenspan showed up at various events in the City of London.

A Londoner who met Greenspan at one of these occasions, reported that the Fed chairman actually seemed to be “oblivious and living in his own bubble.” He pointedly asked Greenspan about the corporate scandals that had rocked the U.S. financial system and Greenspan responded by saying: “Oh yes, yes, even some of my best friends were involved.” Greenspan added that he had asked his friends “how they could do that,” and they told him, “they just didn’t know what they were promising, but they will never do it again.”

Greenspan also gave a speech in London on Sept. 27, at the dedication of Britain’s new Treasury building. Somehow, he felt the need to talk about the fate of former financial authorities who failed to prevent speculative bubbles from emerging. After the “South Sea bubble” burst in 1720, Greenspan noted, the British Chancellor of the Exchequer ended up in the Tower of London. *CBS MarketWatch* commented, that if markets would continue to go down for a few more weeks, “the Tower may be the only place he’ll be safe from angry investors.” London’s *Financial Times* proposed that Greenspan’s honor should be labelled the “Order of the Bubble.”

## Banking

### Morgan Stock Cracks, Lays Off 4,000 More

Some are now calling it “J.P. Meltdown Chase” bank. The stock of J.P. Morgan Chase fell to \$16.54 a share on Oct. 4, well below the supposedly critical level of \$20, as the bank continued its death spiral. The

bank’s market capitalization has fallen from a peak of \$106.5 billion in early 2001, to just \$33 billion, a decline of 69%.

With its huge portfolio of derivatives contracts since the merger of Morgan and Chase, this is a casino, not a bank. As of the second quarter, Morgan Chase had \$26 trillion in total derivatives, including \$278 billion in credit derivatives—compared to \$207 billion in loans; its credit derivatives exposure alone is greater than its loan exposure. The bank, which has not reported its third-quarter results, has said that it will write off \$1.4 billion in loans for the quarter, and said overall trading revenue in July and August was just \$100 million, compared with \$1.1 billion in the second quarter.

To help cut expenses, Morgan Chase will fire about 4,000 of its 20,000 investment bankers, Bloomberg reported Oct. 4. With these cuts, the bank will have cut 14,000 people since the merger.

Morgan is not alone in the meltdown sweepstakes among the banks. Charles Schwab is down 82% from peak; Morgan Stanley is down 72%; Merrill Lynch is down 60%; Goldman Sachs, 54%; Citigroup, 50%; Lehman Brothers, 48%; and Bear Stearns, 45%. Merrill Lynch, which has already cut 15,000 jobs, is preparing further cuts, according to Bloomberg.

## United States

### Distressed and Defaulted Debt Grows

Financial press reports on Oct. 4 showed that the total of U.S. corporate debt which is classified either as being in default or “in distress,” has risen nearly \$200 billion during this year, to a total of \$879 billion. This amount is greater than the Gross Domestic Product of all but eight nations in the world.

All of this debt is now classified as in junk bond status, though the bonded debt of some companies did not start out that way, but, as in the cases of WorldCom or Adelphia, was only downgraded to junk bond level shortly before, or at the point that these companies filed for bankruptcy. Debt is considered to be in default when the issuing company stops making interest payments on the debt.

Of the \$879 billion debt figure, \$389 billion represents defaulted debt, and the rest, debt that is “distressed.”

In dollar volume, the 12-month default rate in the U.S. economy—that is, the percent of all U.S. corporate bonded debt that is in default—is 15%. This is the highest rate since the statistics for such debt defaults have been kept. Further, the defaulted bonds are trading at 18¢ on the dollar, which is far less than the historical average of defaulted debt of 42¢ on the dollar.

## Mexico

### Central Bank Sees Global Market Problems

Reality seems to have struck some at the Banco de México, as seen in the “Monetary Policy Report” it produced on the functioning of the economy for the first half of 2002. The report, apparently presented to the recent International Monetary Fund/World Bank annual meeting in Washington, noted that “the risks to which the basic economy is subject for the remainder of 2002 and in 2003, are substantially greater than those envisioned for other quarters . . . primarily due to the great uncertainty which currently exists with regard to the evolution of *the world economy* and the volatility of the financial markets.” Moreover, “the U.S. economy hasn’t recovered in the second half of the year, [contrary] to what was anticipated.”

Banco de México warned of a possible change in the dollar exchange rate with regard to the euro, as well as an “additional contraction of capital flows to emerging markets.”

The Bank’s governor, Guillermo Ortiz, told London’s *Financial Times* on Oct. 1, that “the current situation in international financial markets is particularly dangerous because important pieces of the old [financial] architecture have been weakened, and the new elements are barely in the design phase.” Ortiz, who appeared quite worried, called for increasing IMF resources, “and the quantity that can be loaned to any country, proportional to its size.” He argued that the IMF should also make a larger initial disbursement of funds to a country in crisis than it does now.

Also worried is the Private Sector Eco-

conomic Studies Center, which warned on Oct. 1 of the "semi-stagnation" of Mexico's economy, noting that exports dropped by 7.7% in May and June, while industrial production dropped 1.7% for the same period.

## U.S. Finance

### Wall Street Braces For Big Job Cuts

The sustained bear market means that Wall Street is now facing "the deepest job cuts yet," wrote the *Wall Street Journal* on Oct. 8. Since the end of 2000 the nation's securities firms have laid off 32,287 employees, or 8.8% of their workforce. But that's peanuts compared to what is in the offing, according to the *Journal's* report. The magnitude of cuts coming down the pike were telegraphed by Credit Suisse First Boston's Oct. 7 announcement of 1,700 layoffs, and J.P. Morgan Chase's news that it will make 4,000 job cuts, or 20% of its investment-banking department workforce.

Wall Street executives hoped "to hold on" to employees, "betting that the bear market would lift." But now, after mergers-advisory work is down 43% to \$351 billion, from \$616 billion in 2001, global underwriting volume fell 12.6% to \$774 billion in the third quarter over last year's third quarter, and only seven public offerings were made in the third quarter just concluded—"the fewest since 1980"—the executives are "waving the white flag—and handing out the pink slips."

## Derivatives

### Rumors of Big Losses at Commerzbank

The London *Financial Times* and *Guardian* Oct. 7 reported rumors—based on an e-mail sent out by Merrill Lynch investment bank—of large derivatives losses at Commerzbank. "Again, the market is flooded with rumors that Commerzbank, among all its other problems, has sustained large trading losses in credit derivatives. . . . Apparently, a number of banks have begun to shut

down credit lines," Merrill Lynch Europe's Maria Anastase said in an e-mail to Standard and Poors, which was printed by the Oct. 4 *Financial Times*.

That same week, Merrill issued a research note comparing the weakness of the German banking sector with that of Japan. The note, entitled "Turning Japanese," stated: "In particular, the rapidly eroding unrealized gains on the bank's equity holdings, coupled with higher refinancing costs, raise serious questionmarks about the bank's ability to withstand a protracted difficult economic environment."

Commerzbank denied it was in trouble and hinted it might sue, while Merrill Lynch said the flap was overblown, part of "the nervous frame of mind of the market at the moment."

## Europe

### Central Bank Says No Rate Cut

The president of the European Central Bank, Wim Duisenberg, on Oct. 8 said there will be "no rate cut" and demanded stricter adherence to structural reforms, drawing opposition especially from France. A head-on collision between reality and Maastricht treaty budget parameters is under way.

Duisenberg rejected some countries' demand for an interest rate cut, saying, "The risks to price stability over the medium term are at present balanced. We thus consider the current level of ECB interest rates to be appropriate." Austrian Chancellor Wolfgang Schüssel was not pleased: "It would help to think of possible alternatives . . . to stabilize the European economic situation." But Duisenberg retorted that member countries had failed to implement reforms and curb unemployment. "You could find an answer if governments finally embarked on ambitious structural reform programs all across the euro area."

Meanwhile, French Finance Minister Francis Mer refused to promise that France would reduce its deficit by 0.5% in 2003, remarking that France's ability to pare down its gap depends on how fast the economy grows. "What do you want to have—growth, or to reduce the deficit?" SAID Mer.

**LOAN LOSSES** written off by the major investment banks in Europe and North America will total more than \$130 billion this year, according to the *Financial Times* on Oct. 6. This is the highest level ever recorded, and the magnitude of the losses will trigger another wave of job cuts across the banking sector, said the *Times*, citing research by Oliver, Wyman.

**MERRILL LYNCH**, in another sign of the doom of the "new economy," announced on Oct. 7 that it will stop trading 75% of the NASDAQ stocks it handles. More than one-third of NASDAQ stocks are now below \$5 per share, and volumes fell by 35% in the first half of 2002. The huge brokerage is closing its separate New Jersey office for NASDAQ operations.

**DEUTSCHE TELEKOM** on Oct. 8 announced a worst-case scenario, in which it will lay off 55,000 employees between 2002 and 2005. This is 22% of Europe's biggest phone company's workforce. These layoffs include the 30,000 terminations announced earlier this year. The cost-cutting measure is supposed to save Deutsche Telekom \$978 million annually.

**ISRAELI** Finance Minister Silvan Shalom told the daily *Ha'aretz* on Sept. 27 that an Iraq war could seriously hurt Israel's credit rating, which has already been hit by the downgrading of two of its largest banks by Standard and Poor's. Shalom said that the banks' downgrading "doesn't mean that the credit companies will also lower Israel's sovereign rating. . . . But if there is a catastrophic crisis such as a war with Iraq, then Israel's rating will be in danger."

**U.S. UTILITY** company shares plunged on Oct. 8, after Allegheny Electric defaulted on credit agreements and TXU Corp. said a credit downgrade of one of its European units may trigger an early bond repayment. Standard & Poor's Electric Utilities Index fell to its lowest level in eight years, reflecting the collapse of the energy bubble.