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Banking by John Hoefle

Shooting the messenger

While the banks maneuver for a bailout, the public is bailing out of the banks.

Whenever the federal government admits to some bad news, you have to wonder how much worse it really is. So it's quite understandable that all the noise coming out of the government about the "recession" and the problems with the banking system, is making the population nervous indeed.

The Federal Deposit Insurance Corp. (FDIC), which just a few months ago was loudly proclaiming its solvency and attacking those who disputed it, is now talking about needing an additional $10-15 billion this year just to keep the doors open. And that's despite a 60% increase in deposit insurance premiums, which took effect Jan. 1.

To maintain the fiction that the taxpayers will not have to bail out the commercial banks, the regulators and major banking trade associations recently held a series of "summit" meetings in Washington to devise a scheme whereby it would *appear* that the banking system would bail itself out, without forcing the banks to actually pay the tab.

The scheme cooked up by these geniuses does just that. The FDIC will sell $10 billion in new long-term bonds to the banks, giving it (except for the $5 billion the FDIC is considering borrowing from the Treasury) the cash it says it needs to make it through the year. The banks would then turn around and sell these FDIC bonds in the secondary market.

The FDIC would raise the funds to pay off these notes by increasing the amount of money it charges the banks for deposit insurance. However, in order to guarantee their payment and make the FDIC notes viable on the secondary market, the banks want the federal government to guarantee payment of the notes, which the banks themselves are supposed to pay.

Thus what is touted to be a private arrangement between the banks and the FDIC, would in fact be a way of sneaking a taxpayer bailout in through the back door.

Anyone who still believes that the banks will be able to bail out the FDIC should take a look at the preliminary figures for the fourth quarter of 1990 recently released by SNL Securities of Charlottesville, Virginia. According to SNL, profits at the nation's FDIC-insured banks fell to $2.6 billion in the fourth quarter, down from $6.3 billion in the first quarter of 1990.

At the rate of $2.6 billion a quarter, a profit no doubt made possible by some *very* creative bookkeeping, the $10 billion that would be loaned to the FDIC under the bankers' plan represents a full year of bank profits.

The profits of the banks are not going to rise, either. According to SNL, non-performing loans at U.S. banks rose to 3.03% of assets during 1990, from 2.24% a year earlier. Commercial loans, which grew by 6.88% in 1989, grew by only 1.9% in 1990, and actually shrank in the fourth quarter of the year.

The decline in loans was also reflected in the Federal Reserve's latest loan survey. Nearly one in five banks was "somewhat less willing" to make auto, home equity, and other consumer loans, whereas the number of banks reporting such policies in earlier surveys was negligible. About one-third of the banks surveyed, including 90% of the foreign banks, have tightened their standards for business loans, and none of them was making it easier for businesses to get such loans.

The tightening of the credit crunch comes despite the Federal Reserve's effort to ease credit. Since December, the Fed has cut its discount rate a full percentage point to 6%, and reduced the federal funds rate by three-quarters of a percentage point.

Rather than dealing with the problem in any serious way, Federal Reserve Board Chairman Alan Greenspan used the occasion of a Feb. 9 speech to the National Association of Manufacturers meeting in Boca Raton, Florida, to blame the credit crunch on federal bank examiners.

"They [the examiners] are responding inappropriately," Greenspan said. "There is an increasing tendency to look at deposit institutions and say we should mark to market the loan portfolios. . . . This is fundamentally wrong."

While Greenspan plays shoot the messenger and the banks scramble to raid the taxpayers' pockets, a large segment of the population has abandoned the banks. According to data from the Federal Reserve, the amount of currency in circulation has jumped significantly. The amount of currency in circulation was running around $245 billion during the autumn of 1990, but began to rise sharply in late December. By Jan. 28, 1991, the amount of cash in circulation had jumped to $254.3 billion.

"Extraordinary," Hongkong and Shanghai Banking Corp. economist Lacy Hunt told the *Los Angeles Times*. "The surge is so abnormal that it suggests people are withdrawing money from the banks and thrifts and literally putting the cash in mattresses, the back yard, safes in the home or something comparable."

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