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Banking by John Hoefle

Failing banks and Bushspeak

Bush's banking bill goes to Congress, the tab goes to the taxpayers, and worry grows that the patch won't hold.

The Bush administration's alleged solution to the U.S. banking crisis is about to be presented to Congress as we go to press, amidst signs of growing opposition to key components of the plan.

The most pressing measure is the recapitalization of the Federal Deposit Insurance Corp.'s Bank Insurance Fund, which stood at a mere $8.4 billion at the end of 1990, or 43¢ in coverage for every $100 in insured deposits. The FDIC projects that coverage will drop to 19¢ per $100 in deposits by the end of this year. Regulators consider $1.25 in coverage for every $100 in deposits to be a safe level.

Under the administration's plan, as disclosed in a March 15 letter from Treasury Undersecretary Robert Glauber to FDIC chairman William Seidman, the administration has decided to replenish the BIF by allowing the FDIC to borrow up to $25 billion from the Federal Reserve. The FDIC already has the authority to borrow up to $5 billion from the Treasury, and under a formula based upon its net worth, another $65 billion from the Federal Financing Bank. If Congress approves this plan, it would allow the FDIC to borrow up to $95 billion.

The administration, in its Orwellian Bushspeak, is presenting this plan as an alternative to a taxpayer bailout of the banks. In theory, the loans from the Fed will be repaid by raising the deposit insurance premiums the banks pay to the FDIC, but everybody knows the bankrupt banks can't fund their own bailout. Once the money is borrowed, the government will issue its usual "who could have known this would happen?" statement, and the taxpayers will cover the bad loan. Under the guise of protecting the taxpayer, the Bush administration plans to stick the public with another $95 billion. And, as the ongoing savings and loan fiasco demonstrates, that's just the down payment.

How Congress will react to this proposal remains to be seen. The narrow passage of the $78 billion for phase two of the S&L bailout shows the growing uneasiness in Congress for voting for taxpayer bailouts.

The Fed is not happy about aspects of the Bush banking plan either. Federal Reserve Board governor John LaWare recently publicly reiterated the Fed's opposition to the provision that would remove the Fed's authority to regulate the biggest U.S. banks.

While the administration fiddles with its smoke and mirrors bank policy, the banking system continues to hemorrhage. The banks claimed an aggregate profit of $1.4 billion for the fourth quarter of 1990, the fourth consecutive quarterly drop in earnings and 65% below the earnings for the third quarter. For the year, the banks claimed a profit of $16.6 billion, or $1 billion more than they earned in 1989.

The domestic operations of the U.S. banks earned a net $1.1 billion in the fourth quarter, the lowest level since the FDIC began keeping statistics in 1983, and about half of the profit of the previous worst quarter. For the year, domestic operations netted $14.8 billion in 1990, down $6.7 billion from 1989.

While profits were dropping, nonperforming loans were on the rise, hitting a record 2.9% of all loans. The biggest losses were from real estate loans, and net losses nearly tripled during 1990 at banks in the Northeast, and nearly doubled at banks in the Southeast and Central regions. At year's end, $36 billion in real estate loans were reported as delinquent, compared to $22.5 billion in 1989.

To cover these rapidly deteriorating loans, the banks wrote off $8.3 billion in loans in the fourth quarter. For the year, the banks wrote off $29 billion, up 27% from $23 billion in 1989. Despite the higher writeoffs, the banks ended the year with $19.8 billion in repossessed real estate, compared to $12.5 billion in 1989.

The banks also added a record $11.5 billion to loan loss reserves during the fourth quarter, bringing the yearly loan loss reserve addition to $31.7 billion. While that figure just slightly exceeds the $31 billion added to reserves in 1989, a much higher percentage of those reserves were devoted to domestic losses. In 1990, the banks set aside $1.5 billion to cover losses on their loans to the less-developed countries, compared to $10 billion in additions in 1989.

FDIC chairman Seidman characterized the condition of the banking system as "bleak," and described the fourth-quarter bank profits as "severely depressed."

"I don't find much in here that says the first quarter of 1991 will be characterized as anything but bleak, but perhaps not as bleak as the last quarter—if you can have degrees of bleakness," Seidman said. "I want to emphasize, so people don't think that the whole system is in a state of collapse, that the banks made $16.6 billion. . . . The problems that we're seeing are clearly not comparable to the S&L industry."

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