Alan Greenspan Has Lost It

by Lothar Komp and Nancy Spannaus

In the face of 200% to 1,000% increases in the price of energy, the collapse of the U.S. economy, the bursting debt bubble in the international telecommunications sector, and the accelerating shakeout in Japan, Federal Reserve Chairman Alan Greenspan went before the U.S. Senate Banking Committee on February, and babbled. Greenspan, as the saying goes, has "lost it"—even though he didn't have much of it to begin with.

The ostensible purpose of Greenspan's appearance was to try to reassure the Senators, and anyone else gullible enough to heed his prouncements, that, actually, things are under control. He babbled about how wonderfully the markets are doing, about how the Information Economy is continuing to produce (mythical) great productivity increases, and about how the burgeoning layoffs are only a temporary "adjustment."

Most ludicrous were his comments on the energy crisis, which is now threatening to put California into the dark, shut down industry nationally with hyperinflation, and shake the foundations of the world financial system, starting with Bank of America and Wells Fargo banks. Not only did Greenspan claim that the skyrocketting prices were not inflationary, but he characterized the banditry of Bush's friends in the energy cartels as a mere "transfer of income to producers of energy." Therefore, Greenspan concluded, "the effects of the rise in energy costs does not appear to have had broad inflationary effects, in contrast to some previous episodes when inflation expectations were not as well anchored."

Pure gobbledygook! Even as his major cuts in interest rates have proven a failure in reviving the markets, much less the economy, Greenspan is simply spinning his wheels—and, of course, pouring out liquidity in hopes of keeping the speculative game going as long as possible. In the first half of February, the entire "recovery" on the markets from January, was again wiped out. Greenspan's magic is gone.

The Telecom Bomb

The bubble that Greenspan built up over the past 14 years—the $30 trillion debt of state, private households, and companies in the United States, the almost $20 trillion stock market bubble on Wall Street, the off-balance sheet liabilities of the U.S. banks—is in the process of popping. On top of that has come the implosion of another section of the bubble, the telecommunications sector internationally.

At the beginning of February, the "Orange" bomb was thrown into the worldwide telecommunications sector, and pulled the stock prices of the affected companies down to the lowest level for more than two years. The setting for this collapse was this:

In order to finance the numerous takeovers and corporate mergers which have taken place in the wake of the global telecommunications deregulation of the last years, the big companies in the sector had to go into debt over their ears. Then came the auctions in Summer of 2000, for the licenses for the future mobile telephone technology, UMTS, which in Great Britain and Germany amounted to 160 billion deutschemarks ($80 billion) alone. That was enough to make the cup run over. The telecommunications companies, especially those in Europe, were suffocating in debt. And since everyone knows it, it becomes more and more difficult every day, to find new creditors who will refinance their debts.

In the coming year alone, the seven biggest telecommunications companies—British Telecom, France Telecom, Deutsche Telekom, the Dutch KPN, Vodafone in Great Britain, Telecom Italia and Telefonica in Spain—have to pay $80 billion in debt. For the whole sector, worlwide, about $200 billion in debt will come due in 2001.

Naturally, the affected companies are not in a position to cover even a portion of this debt from their profits on current activities. They still have to make enormous investments for

Federal Reserve Board Chairman Alan Greenspan: His magic is gone.

the construction of the UMTS infrastructure, and on top of that, they need immense sums for advertisement and dumping, in order to expand their clientele in mobile phones. As a result, most of them have no profits at all.

A particularly striking example is Mobilcom in Rendsburg-Büdelsdorf, Germany, which until recently was a medium-sized company. In Summer 2000, with the backing of France Telecom, it purchased two licenses for $8.1 billion, at the German UMTS auction. Until now, Mobilcom had calculated, it would close with losses "only" for the next 24 quarters. But now the management has to acknowledge that this goal is not attainable, and that no profit may be made until a rather distant future for the stock markets: after the year 2006. Meanwhile, Mobilcom's stock price, which was at 210 euro in March 2000, collapsed on Feb. 14, to a new low of 25 euro.

The Orange Bomb Explodes

There are various ways in which a big company can come into liquidity in the order of billions of dollars. The traditional way, heretofore, would have been to seek bank credits. But the banks, especially the European banks, are sitting on such high telecom debts, that the banking supervisors and central banks in London, Frankfurt, and elsewhere, have sounded the alarm, and have warned against any further engagement in this sector.

Then there are still the international bond markets. Like a swarm of grasshoppers, the telecommunications companies in the recent past seized on these markets. But in the meantime, even the big rating companies have reacted, by downgrading the ratings of the big telecommunications firms, meaning, in turn, that they had to offer higher yields, in order to sell their bonds. The bond markets have also been terrified by the news of dramatically rising default rates on corporate bonds.

Now, there is yet another way to come into the required billions of dollars: Issue shares. Deutsche Telekom did this in June 2000, and succeeded, with the help of frequent television appearances by a confidence-building TV star, Manfred Krug, to convince one out of every two German households to buy telecom stocks for a price of 63 euros a share. Most people did not succeed in purchasing them, because of the enormous demand—luckily for them. Because, in the second half of 2000, Telekom's share price had fallen to 35 euros (and it was at 105 euros in March!).

The whole thing can also be handled in a somewhat more elegant manner, by separating the mobile phone unit from the mother company, and then putting it, as an independent enterprise, onto the stock market. Deutsche Telekom actually wanted to do that last year, with its daughter firm, T-Mobil. But because of the crash of technology stocks, they thought better of it, deciding to postpone it for at least one year.

France Telecom, on the other hand, could not afford to wait any longer, because it had to pay its debts to Vodafone in London. Its daughter firm, Orange, therefore had to go onto the market in February 2001. When France Telecom bought up Orange from its British competitor Vodafone (which, for its part, had just swallowed Mannesmann), it planned to bring in about $150 billion with Orange's initial public offering (IPO). It was supposed to be by far the biggest IPO of all time in Europe.

However, the Orange IPO fell on its face. France Telecom had to revise its price expectations downward. Just prior to the IPO, the price for Orange shares had to be reduced again by 17%, because otherwise it would have been a debacle. In the end, only $45 billion materialized in the IPO—a substantial sum, but much too little to meet their ambitious financial plans. And then, the shares at the 17% reduced price, fell a further 13% in the first three days of trading.

As a consequence, the rating agencies downgraded those telecommunications companies, such as Deutsche Telekom and KPN, which had planned to soon launch their mobile phone units on the stock markets. A worldwide shock wave was unleashed, pulling the shares of the entire telecommunications sector into the cellar. On Feb. 15, Deutsche Telekom stocks fell to their lowest level since December 1998, to only 27.5 euro, which is only about one-fourth its highest value from last year.

On the day before, rumors had been circulating in Frankfurt, that Germany's top manager Ron Sommer had resigned (or, had "been resigned"), and T-Mobil's debut on the market was postponed again for one year. This was denied as "nonsense." However, what is very real, is the $80 billion debts of the German telecommunications giants. Perhaps soon, Ron Sommer and Manfred Krug will be standing outside their neighbor's houses, ringing the doorbell and asking for a handout. After all, if every German household contributes DM4,000 ($2,000) to Ron Sommer, then everything will be fine and dandy.