buyouts, are a combination of stock-market speculation and tax wingding. If the equity appreciates, the operation is doubly profitable, since the additional interest paid against debt issued to buy the equity is simply written off the corporation's tax bill. If the operation fails, and corporate cash flow declines, the operation becomes a disaster, for lenders in particular.

The disaster in the oil patch, which threatens to topple $200 billion of Texas banking assets, among other things, appears to have caused an epidemic of sobriety among bankers and their regulators. The deadpan statements of the bank regulators have a clear message: "Head for high ground, boys, the dam's a-bust!" As noted, short-term credit lines to non-financial corporations have dried up,
the orgy of leveraged buyouts, corporate equity repurchases, and so forth, has quieted a bit. Net stock repurchases were at $23 billion in the third quarter of 1985 and $25.3 billion in the fourth quarter, but fell to $11.7 billion in the first quarter of 1986.

Not merely oil patch banks, but larger, troubled institutions like Bank of America, are in no position to finance the additional $100 billion per year or so that America will need to buy the same amount of foreign goods with cheaper dollars.

The disappearance of commercial banking in the international markets is now repeating itself in the domestic markets. In 1981, international bank lending reached a peak of $500 billion. By 1985, international bank lending had fallen to less than $80 billion. What replaced the banks was the Eurobond market, funded by international dirty money. From barely $20 billion a year in 1981, the Eurobond market grew to $140 billion at present rates. Now, the domestic bond markets have virtually replaced domestic lending; but the bond markets have financed nothing better than 1928-style stock market speculation.

The result is evident from the international trade data, which show that the undeflated dollar volume of international trade was lower in 1985 than in 1980. At home, the first signs of downturn will create a new category of problem loan: the "leveraged buyout loan." Regulators will tear their hair out over corporate over indebtedness, at the same time that oil banks, farm banks, and major international lenders slide further over the edge.

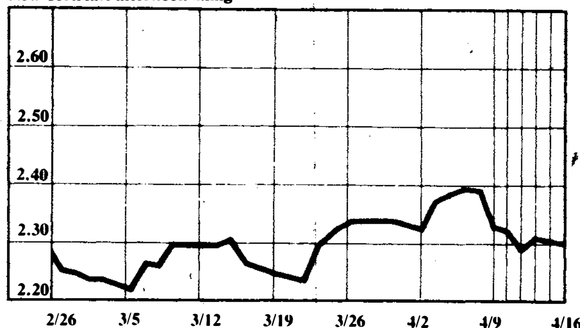
The financial consequences of the current downturn are unpredictable, particularly since $1.26 trillion of "off-balance-sheet" liabilities on the part of the 15 largest U.S. commercial banks may turn sour very quickly. These include loan guarantees, currency and interest-rate swap agreements which depend on the solvency of the participants, standby letters of credit (guaranteed loan facilities), and other risks.

Without drawing on metaphoric language from the vocabulary of nuclear explosive devices, we can state clearly that the phony stability of the past three years is over, and reiterate our year-end 1985 forecast: a 15-25% downturn of U.S. physical output during 1986.

Currency Rates

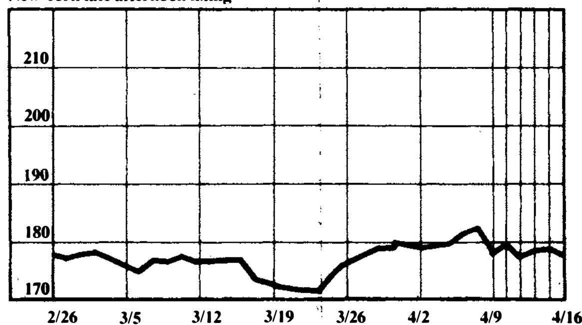
The dollar in deutschemarks

New York late afternoon fixing



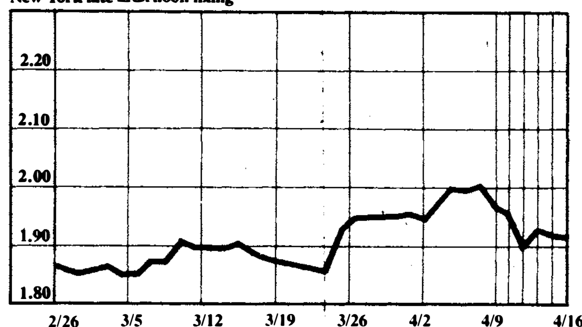
The dollar in yen

New York late afternoon fixing



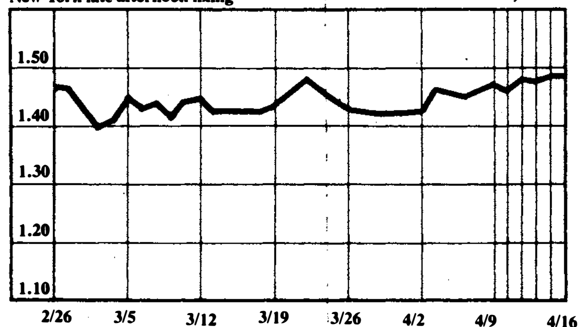
The dollar in Swiss francs

New York late afternoon fixing



The British pound in dollars

New York late afternoon fixing



© 1986 EIR News Service Inc. All Rights Reserved. Reproduction in whole or in part without permission strictly prohibited.