Banking by EIR Staff

Coming unstuck

The chewing-gum arrangements for the U.S. banking system are not working.

During the week of Aug. 16,

1) The supposedly solvent Federal Deposit Insurance Corporation was supposed to stand by the bankrupt Federal Savings and Loan Insurance Corporation, if needed. Now analysts warn that FDIC may run out of money. With $18.4 billion in assets, FDIC is holding $10.8 billion of assets from failed banks, now being liquidated at a fraction of book value. The fund earned only $167 million in the first half of 1987, against $1.4 billion in 1985. Meanwhile, bank failures are eating away at its funds. Combined assets of failed banks doubled to $8.1 billion in 1986 compared to 1985.

2) One of the nation's biggest and worst-off thrifts, Finance Corp. of America, announced that it is much worse off than it previously said.

3) A renewed outflow of deposits hit the savings and loans in June, raising the prospect that the "government-organized Ponzi scheme" holding them together may not last until October, when their insurance agency is supposed to borrow some new money to bail some of them out.

4) Citibank's $3 billion write-down of bad foreign debt was supposed to be a salutory house-cleaning. The moment (Aug. 18) Citibank announced that it needed to raise $1 billion in new capital, the market for bank stocks turned sour.

5) Bank regulators ignored the Aug. 20 deadline for banks to set aside about $20 billion in reserves against their non-paying Brazilian loans, hoping that the Brazilians will cough up some interest before the loans stink.

6) Amidst all of this, the Criminal Division of the U.S. Department of Justice is running a turkey-shoot against bankrupt Texas savings-and-loan operators and real-estate developers, who happen to be habitual contributors to the Democratic Party.

All of this casts considerable doubt as to whether the administration's measly $11 billion re-funding program for the bankrupt FSLIC will ever take place. First, investors are supposed to lend money to a fund which is $50 billion or more in the hole, on the presumption that the S&Ls, which collectively run a loss, will pay the interest. If the investors' accountants follow the guidelines of the Financial Accounting Standards Board (FASB), they will buy Czarist bonds before touching FSLIC paper.

The S&Ls cannot even treat their shares in the FSLIC as an asset. Four California thrifts have been forced by the Financial Accounting Standards Board to write-off $80 million they had invested in FSLIC. A handful of big institutions, led by Great Western Savings, had protested that the write off was, in effect, an unprecedented default by a federal agency on its obligations. Wall Street did not agree. "I don't think the whole thing should be restored at once," Peter Treadway, a thrift analyst with Smith Barney, Harris Upham & Co, told the *Wall Street Journal*. "I put the FSLIC in the same category as Bolivia."

As *EIR* has reported, the 500 or more "brain-dead" thrifts have been kept alive by an FSLIC bucket-brigade, which provides lists of desperate thrifts to deposit-brokers, who then place institutional money with the thrifts in amounts of less than the $100,000 the FSLIC supposedly guarantees. But the latest data from the Federal Home Loan Board Bank show a $3 billion net outflow from thrifts during June, against a $1.4 billion inflow in May, possibly indicating a dead end for these desperate efforts to keep deposits going into "braindead" institutions.

One of the biggest and worst-off S&Ls, Finance Corporation of America, reported $1.38 billion of problem loans as of June 30, but admitted in an SEC filing that new bank examinations "would have increased significantly" the number, already several times larger than the bank's net worth. The loan problems derive from oil-producing areas, and hotel and motel loans. Ford Motor has offered to take it over, and put in $1 billion in capital, if the government guarantees it against some future losses.

The worst of it all is that Washington appears to be preparing its cover-story for a collapse of the thrifts, by arguing that fraud, rather than economic and regulatory disasters, account for the tidal-wave of bankruptcies. Twenty Texas savings and loans are the subject of the biggest FBI investigation of bank fraud ever mounted, including 50 FBI agents, among others. The investigation, expected to last two to five years, attacks the heart of political funding in Texas.

Bank regulators say the Department of Justice routinely ignored bank fraud around the country for years, but suddenly became interested when Democratic funders were involved.