Banking by John Hoefle

Brady's 'no-bailout' bailout

The administration says no bailout of the banks will be necessary, as long as its bailout package passes.

The Bush administration's aversion to admitting to the public that it plans to stick the taxpayers with the cost of bailing out the bankrupt U.S. banking system, is causing the administration to engage in the kind of verbal contortions of which George Orwell would be proud.

The latest example of this is Treasury Secretary Nicholas Brady's March 26 statement to the *New York Times* that he was "very close to promising" that a taxpayer bailout of the banks would not occur unless the economy performed much worse than expected and "you have a pusillanimous reaction by Congress" to the administration's banking proposal.

Brady's statement is idiocy on several levels. To begin with, the Bush banking proposal *is* a bailout of the banks. The Bush plan would allow the Federal Deposit Insurance Corp. to borrow up to $25 billion from the Federal Reserve to bail out sick banks. On top of that, it would allow the FDIC to count its $5 billion line of credit from the Treasury as if it were equity. Using this accounting gimmick, the FDIC would be able to borrow an additional $45 billion from the Treasury's Federal Financing Bank (FFB).

Under the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989 for the S&Ls, the FDIC already had the authority to borrow up to nine times its net worth from the FFB. That would, as of the beginning of this year, allow the FDIC to borrow an additional $65 billion. That sum, combined with the existing $5 billion Treasury line of credit, the $25 billion from the Fed, and the magical $45 billion, would potentially give the FDIC $140 billion in borrowing authority.

The FDIC insists that the $70 billion in the Bush proposal is not new money, but merely the same $70 billion as before. That would be true if the FDIC were already broke, and thus unable to borrow the original $65 billion.

The FDIC is indeed broke by any rational standard, and may even be broke by the Alice in Wonderland standards of the Bush administration. The FDIC's Bank Insurance Fund started 1991 with $8.4 billion in reserves—that is, with $8.4 billion in Treasury IOUs, since the BIF does not exist as a separate fund. But the bailout of the Bank of New England is expected to require some $6-8 billion in cash up front, with the ultimate cost projected at $2.3 billion after asset sales.

The FDIC's own "pessimistic" projection is that the BIF will fall to zero this year and to negative $5.8 billion in 1992. The White House's Office of Management and Budget projects that the BIF will fall to $22.2 billion in the red by 1996.

So either the $70 billion is new money, meaning that $140 billion taxpayer-backed dollars are being pumped into the banks, or the FDIC is already broke and will receive $70 billion taxpayer-backed dollars. Either way, the administration's proposal amounts to a massive taxpayer bailout of the banks. And either figure is only a downpayment.

The rest of the Bush banking proposal is no better. By cutting back deposit insurance, allowing banks to set up unrestricted nationwide branching systems, sell insurance and securities, and merge with industrial corporations, the Bush plan would drive most of the 12,000 U.S. banks out of existence, leaving the system even more dominated by the money center giants than it is now. It would, in effect, give the giant banks almost total control over the allocation of credit in the United States.

Pass this fascist banking bill, with its taxpayer bailout, the imperious Mr. Brady demanded of Congress, or be labeled cowards.

The stupidity of this approach is demonstrated by the failure of FIRREA. The Resolution Trust Corp., created by FIRREA to dispose of the assets of failed S&Ls, has become the nation's largest financial institution. The 18-month-old RTC has become so bogged down in bureaucracy that many refer to it as "Red Tape Central." By year's end the RTC will have already spent over four times the amount of money the administration said would be needed through 1992. To try to unload its $155 billion in assets, the RTC is cutting prices like mad, offering financing, and selling its own government-backed junk bonds. If that doesn't work, it says, it is prepared to give properties away.

Finally, we come to the case of First City Bancorp. of Texas, the Houston bank that was rescued by Robert Abboud in 1988, with $970 million in FDIC money. When Abboud took over the bankrupt First City, he promised to not only reinvigorate the bank but to restore Texas to its rightful place as a major financial center. On March 28, Abboud was fired as chairman and chief executive officer at First City, and the rapidly collapsing bank is looking for a buyer or even, the rumors say, another federal bailout.