FT's Wolf: U.S. Too "Politically Frightened" to Admit Truth About Banks, Part I

Posted Feb 09, 2009 04:10pm EST by Aaron Task in Investing, Recession, Banking

One, policymakers have better information than private economists and really believe the big banks aren’t insolvent, i.e. they continue to view the crisis as a “liquidity problem,” and believe so-called toxic assets will return from their currently “artificially low” levels once confidence is restored.

Two, policymakers "are not prepared to admit the truth" because it means existing shareholders and bank managements will be wiped out. It also means "admitting total failure" of efforts to date to stem the crisis, says the author of Fixing Global Finance.

Arguing today’s toxic assets are "fundamentally worthless" - and there’s lots more losses coming - Wolf says the lack of political will (or outright cowardice) to admit to reality means "we're really in trouble." Why? Because confidence in policymakers will continue to deteriorate as their ill-conceived solutions continue to fail.

Once policymakers (ultimately) agree insolvency is really the underlying problem, there are two options for dealing with the banks:

- Nationalize them, and then inject government capital as the U.K. government has started to do with RBS and Lloyds. (a.k.a. The Swedish Solution)
- Put them into FDIC receivership or force them into bankruptcy, whereby common stock and preferred debt shareholders get wiped out and “senior” debt holders end up owning the banks.

Editor’s note: Stay tuned for part 2 of this discussion and check out these other segments with Wolf:

- Economy at a Crossroads: We’ll Be Lucky If Downturn Only As Bad As Japan’s
- “Terrible Year Baked In:" Govt. Stimulus Needed, But Not This Bill

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We made two big mistakes in the fall of 2008, TARP and the election of Obama. If the Banks are insolvent let them go Bankrupt. Stop the Bailouts.

This Govt. stimulus is needed, let's get the name of every congress person that is making a big stink and remind him/Her that the voters will vote Him/Her out in the next election. P.S call your rep. now

As is always the case with Government never admit to a problem of this scale, allow lies and misinformation to flourish until such time that the damage done can not be easily repaired. It took almost a whole year to admit the we were in a recession, anoth year will go by along with TRILLIONS of dollars before they admit we are in a DEPRESSION. Then its back to fear tactics to achieve another TRILLION dollar stimulus, bail out package.

OK. STOP ALREADY. YES, most banks are insolvent. But so what. Most major banks were insolvent in the early 90s. FORBEARANCE was the operative word. The regulators simply looked the other way UNTIL (and it took as many as five years) these institutions worked there way out of their problems. Just STOP talking about nationalization.

Holy Crap! I've known this since July 08, but good luck making money off that trade, with all the bailouts. What we have in banking is excess capacity. Fewer banks can handle more banking, thanks to modern technology. We can get rid of two thirds of the banking system's corporate structures, which means two thirds less CEOs, board members, presidents and vice presidents and all the other management suits. All those type A personalities can go make money somewhere else, the banks are not profitable enough to support them.
michael.arya - Monday February 09, 2009 04:35PM EST

Why can't these pundits and the public admit they are also the problem. They borrowed money from the banks, in many cases by misinforming the banks or in some cases fabricating scenarios to justify getting the money. The gov't is also responsible for conniving in this fraud by looking the other way. Now everyone wants to punish the banks, the very entities that provided the funds to the Public and Gov't to keep the economy functioning and growing for the latter decade. Take Responsibility!!!!!!!

Kurt R - Monday February 09, 2009 04:35PM EST

Dollars or Ameros, they'll both be worthless.

Ronny - Monday February 09, 2009 04:37PM EST

Fear, fear, fear!!!

Ronny - Monday February 09, 2009 04:39PM EST

Mr. Wolf. Fear. Get it?

moore1191 - Monday February 09, 2009 04:40PM EST

It's so terribly reassuring that FDIC now insures accounts to $250K when it's so terribly undercapitalized itself... Anyone care to see what happens if there is a run on banks??? We think the government is running a deficit now...

madmiker - Monday February 09, 2009 04:40PM EST

well, it don't take a dang Rocket Scientist to tell you if you buy all foreign made items and your dang dollar goes to a foreign bank...America will jus run out of dollars...duh! http://www.worldthinktank.net/pdfs/TheFlowofTrade.pdf these damn ivy league brats have to all be one sandwich short of a picnic if they don't know dat...

RSK - Monday February 09, 2009 04:41PM EST

Obama, Bush, or McCain it is irrelevant who got elected since they all favor bailouts and government stepping as the savior of the nation for the problems that they created. There is no way out of this downward cycle until we achieve a total market and dollar collapse. It gauls me that our system conveys to the public two worthless parties that are indistinguishable from each other. It is a mono-communist party with two factions contained with and the only difference is the spin or the amount of money they will piss away their own particular projects. When the collapse happens that will
be the first sign that change can happen, because then we(they) will have no choice but to do the right things. Right now they are in the denial or cowardly phase and nothing will change. Hollywood, the media, and company are loving Obama because he is black, but it means nothing.

bleaders1 - Monday February 09, 2009 04:42PM EST

We made two critical errors. One electing numb nuts (George W. Bush) and two spending 12 billion a month in Iraq for 8 years. This is the perfect example of what happens when you elect a daddy's little rich boy, that has never earned a dollar, to the most powerful office in the world. The republicans caused the first depression and looks like they have caused the second depression too.

Yahoo! Finance User - Monday February 09, 2009 04:42PM EST

I see a big 'short' guy talking. If the big banks go bankrupt and bring down all financial stocks, the short guys will make a killing. If the big banks go bankrupt, all stocks go down with it. We'll see DOW at 3000. Stop exploiting the hype and spreading fear...

Yahoo! Finance User - Monday February 09, 2009 04:42PM EST

Bread and circuses, it's all about staying in office and getting those lifetime benefits and untouchable pension.

bleskers1 - Monday February 09, 2009 04:46PM EST

These talking heads have no clue! I am placing my bets on a starting recovery in the 3rd quarter

sirdon2 - Monday February 09, 2009 04:49PM EST

michael.arya - Monday February 09, 2009 04:35PM EST OK, some folks did deceive banks, but a lot of banking, loan specialist did the same by looking the other way when someone's credit was less than worthy, just to make the sale. Who is to blame, the consumer who took the loan, or the banker who knew better to the risk?

wobatus - Monday February 09, 2009 04:50PM EST

Jesus, what hacks. The idea that these assets are worthless because the market says so is poppycock. The market, you will recall, over-priced them for years. So someone would have swooped in already if they were worth something? Wrong again. There are plenty of stocks trading below their net cash level, some significantly, and they still don't catch a bid. In Ben Graham's day during the Depression, that was true of
tons of stocks. Assets don't always catch the bid they "should" Plus there is a ton of money that is just as interested in people believing these assets, and the debt of various financials, and their common, is worthless. Fear is a huge discounter of stocks. The belief in fear has caused a lot of the discount. Oh, and citibank et al have been "insolvent" before, and it didn't cause this level of panic. I like to read Martin Wolf, but he hasn't the vaguest idea if those assets are worthless or really are worth more than the "market" says. And I for one think it would be idiotic for the feds to go around proclaiming that these banks are all insolvent. I could not imagine a policy more geared to making it so than that. And the amount of penny-ante moralizing from the self-promoters at the mis-named "tech ticker" is risible.

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