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## Banks Are Likely to Hold Tight to Bailout Money

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Even as the government moves to plug holes in the nation's banks, new gaps keep appearing.

As two financial giants, [Citigroup](#) and [Merrill Lynch](#), reported fresh multibillion-dollar losses on Thursday, the industry passed a grim milestone: All of the combined profits that major banks earned in recent years have vanished.

Since mid-2007, when the [credit crisis](#) erupted, the country's nine largest banks have written down the value of their troubled assets by a combined \$323 billion. With a recession looming, the pain is unlikely to end there. The problems that began with home mortgages, analysts say, are migrating to auto, credit card and commercial real estate loans.

The deepening red ink underscores a crucial question about the government's plan: Will lenders deploy their new-found capital quickly, as the Treasury hopes, and unlock the flow of credit through the economy? Or will they hoard the money to protect themselves?

[John A. Thain](#), the chief executive of Merrill Lynch, said on Thursday that banks were unlikely to act swiftly. Executives at other banks privately expressed a similar view.

"We will have the opportunity to redeploy that," Mr. Thain said of the new capital on a telephone call with analysts. "But at least for the next quarter, it's just going to be a cushion."

Granted, the banks are in a deep hole. For every dollar the banks earned during the industry's most prosperous years, they have now wiped out \$1.06.

Even with the capital from the government, analysts say, the banking industry still needs to raise around \$275 billion in light of the looming losses.

But Treasury Secretary [Henry M. Paulson Jr.](#) is urging them to use their new capital soon. On Monday, Mr. Paulson unveiled plans to provide \$125 billion to nine banks on terms that were more favorable than they would have received in the marketplace. The government, however, has offered no written requirements about how or when the banks must use the money.

"There is no express statutory requirement that says you must make this amount of loans," said John C. Dugan, the comptroller of the currency. "But the economics work so that it is in their interest to do so."

Mr. Dugan added that he would not examine how the banks used the money, but he said their actions would "be open to the court of public opinion."

The banks could use the money from the government for any number of things. Some analysts say the banks may use it to acquire weaker competitors. Others say they might use it to avoid painful cost-cutting. And still others say the banks may sit on the capital.

Lenders have been pulling back on credit lines for businesses, mortgages, home equity loans and credit card offers, and analysts said that trend was unlikely to be reversed by the government's money.

"I don't think that the market wants to see that capital being put to work to leverage the business up again," said Roger Freeman, an analyst at [Barclays](#) Capital, which acquired parts of the now-bankrupt [Lehman Brothers](#) last month. "My expectation is it's quarters off, not months off, before you see that capital being put to work."

Many banks are still plagued by past excesses. Losses on a variety of different types of loans of all sorts are growing and spreading beyond the country's borders. Citigroup and Merrill Lynch have each lost money every quarter in the last year, as deteriorating assets wiped out revenue.

Merrill, which is in the process of merging with [Bank of America](#), reported a \$5.15 billion loss, dragged down by about \$12 billion in write-downs.

Citigroup lost \$2.82 billion, as its \$13.2 billion in charges related to credit losses more than overwhelmed every bit of revenue that the bank generated. And analysts say Citigroup is likely to face several more quarters of loan losses as the global economy slows.

Every corner of the economy goes through cyclical ups and downs. But the banking downturn has acted with ferocious speed to erase past profits.

In the case of the nine-largest commercial banks — Citigroup, Merrill Lynch, Bank of America, [Morgan Stanley](#), [JPMorgan Chase](#), [Goldman Sachs](#), [Wells Fargo](#), [Washington Mutual](#) and [Wachovia](#) — profits from early 2004 until the middle of 2007 were a combined \$305 billion. But since July 2007, those banks have marked down their valuations on loans and other assets by just over that amount.

“The losses now are showing that in some sense the profits reported in earlier years were not real, because they were taking too much risk then,” said Richard Sylla, an economist and financial historian at the Stern School of Business at [New York University](#).

Mr. Sylla said that the average profit of the financial industry in the first decade of this century will be abysmal, despite the fact that there were a handful of record years in the middle.

The ways banks value their investments has already come under scrutiny. Bankers are supposed to be skilled at valuing assets, and many of their sky-high bonuses before the credit crisis were based on the lofty values attached to mortgage securities.

In the future, when Wall Street finds a new profit center, as it surely will, analysts may look back at the losses in this downturn as they question new earnings.

At Citigroup, for instance, the write-downs on mortgages and other loans have eaten away 60 percent of all the profits made by the bank during the boom years. At Morgan Stanley, the cost has reached 70 percent of those profits, and at Merrill Lynch, the tally is 250 percent of the investment bank's record earnings over those three and half years.

It is those same banks that are in some shape benefiting from the government's recent capital infusion. Three of the nine — Merrill Lynch, Washington Mutual and Wachovia — are in the process of mergers with others in the group. Two other banks — State Street and [Bank of New York Mellon](#) — also received capital from the government this week.

Several of the banks, including Wells Fargo, Morgan Stanley, and Goldman Sachs, declined to comment on how they will spend the government funds once they arrive.

Bank of America said in a statement that the money “will add to our capital, which will increase our capacity to expand our balance sheet and make more loans.” It did not say if it was willing to increase its lending.

Indeed, observers point to the growing well of bank losses, deeper by the quarter, as reason to question whether the government funding will be used as a financial Band-Aid, instead of an engine to move forward.

“It is the government's responsibility to set the terms and conditions on this money,” said David M. Walker, the former federal comptroller general and now president of the [Peter G. Peterson](#) Foundation. “This is the people's money. They're giving it out with no rules.”

Bank executives, meanwhile, said on conference calls this week that it was premature to discuss their plans.

[Jamie Dimon](#), the chairman and chief executive of JPMorgan, said his bank was in a stronger position to use the money than

some of its competitors.

“It’s clear that the government would like us to use the capital,” Mr. Dimon said on a conference call with analysts on Wednesday. “If you are a bank that is filling a hole, you obviously can’t do that.”

And Gary L. Crittenden, Citigroup’s chief financial officer, on Thursday called the government’s \$25 billion investment in Citigroup “incremental to our thinking.”

“We now have more capital than we anticipated,” he said in an interview. It will “allow us to opportunistically build what we have not been able to do.”

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