

February 23, 2009

OP-ED COLUMNIST

Banking on the Brink

By [PAUL KRUGMAN](#)

Comrade Greenspan wants us to seize the economy's commanding heights.

O.K., not exactly. What Alan Greenspan, the former Federal Reserve chairman — and a staunch defender of free markets — actually said was, “It may be necessary to temporarily nationalize some banks in order to facilitate a swift and orderly restructuring.” I agree.

The case for nationalization rests on three observations.

First, some major banks are dangerously close to the edge — in fact, they would have failed already if investors didn't expect the government to rescue them if necessary.

Second, banks must be rescued. The collapse of Lehman Brothers almost destroyed the world financial system, and we can't risk letting much bigger institutions like Citigroup or Bank of America implode.

Third, while banks must be rescued, the U.S. government can't afford, fiscally or politically, to bestow huge gifts on bank shareholders.

Let's be concrete here. There's a reasonable chance — not a certainty — that Citi and BofA, together, will lose hundreds of billions over the next few years. And their capital, the excess of their assets over their liabilities, isn't remotely large enough to cover those potential losses.

Arguably, the only reason they haven't already failed is that the government is acting as a backstop, implicitly guaranteeing their obligations. But they're zombie banks, unable to supply the credit the economy needs.

To end their zombiehood the banks need more capital. But they can't raise more capital from private investors. So the government has to supply the necessary funds.

But here's the thing: the funds needed to bring these banks fully back to life would greatly exceed what they're currently worth. Citi and BofA have a combined market value of less than \$30 billion, and even that value is mainly if not entirely based on the hope that stockholders will get a piece of a government handout. And if it's basically putting up all the money, the government should get ownership in return.

Still, isn't nationalization un-American? No, it's as American as apple pie.

Lately the Federal Deposit Insurance Corporation has been seizing banks it deems insolvent at the rate of about two a week. When the F.D.I.C. seizes a bank, it takes over the bank's bad assets, pays off some of its

debt, and resells the cleaned-up institution to private investors. And that's exactly what advocates of temporary nationalization want to see happen, not just to the small banks the F.D.I.C. has been seizing, but to major banks that are similarly insolvent.

The real question is why the Obama administration keeps coming up with proposals that sound like possible alternatives to nationalization, but turn out to involve huge handouts to bank stockholders.

For example, the administration initially floated the idea of offering banks guarantees against losses on troubled assets. This would have been a great deal for bank stockholders, not so much for the rest of us: heads they win, tails taxpayers lose.

Now the administration is talking about a "public-private partnership" to buy troubled assets from the banks, with the government lending money to private investors for that purpose. This would offer investors a one-way bet: if the assets rise in price, investors win; if they fall substantially, investors walk away and leave the government holding the bag. Again, heads they win, tails we lose.

Why not just go ahead and nationalize? Remember, the longer we live with zombie banks, the harder it will be to end the economic crisis.

How would nationalization take place? All the administration has to do is take its own planned "stress test" for major banks seriously, and not hide the results when a bank fails the test, making a takeover necessary. Yes, the whole thing would have a Claude Rains feel to it, as a government that has been propping up banks for months declares itself shocked, shocked at the miserable state of their balance sheets. But that's O.K.

And once again, long-term government ownership isn't the goal: like the small banks seized by the F.D.I.C. every week, major banks would be returned to private control as soon as possible. The finance blog Calculated Risk suggests that instead of calling the process nationalization, we should call it "preprivatization."

The Obama administration, says Robert Gibbs, the White House spokesman, believes "that a privately held banking system is the correct way to go." So do we all. But what we have now isn't private enterprise, it's lemon socialism: banks get the upside but taxpayers bear the risks. And it's perpetuating zombie banks, blocking economic recovery.

What we want is a system in which banks own the downs as well as the ups. And the road to that system runs through nationalization.

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