Dealing With Savings & Loan Crisis

REMARKS

by

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Good morning. It's a pleasure to be here with the Washington Analysis group this morning.

According to your agenda, the topic of my speech is "Dealing With S&L Crisis".

Personally, I wouldn't have chosen to speak on that particular topic so early in the morning, it's a subject best discussed after at least two martinis. So I'll do my best and try to keep my remarks brief.

How much will the S&L's cost? It breaks down something like this:

* RTC -- $100 to $130 billion (Our best guess is it will be close to the higher number.)
* The 1988 deals -- $50 - 55 billion
* Refunding of the thrift's insurance fund -- $15 billion.

If you add up these estimates, it comes to $165 billion on the low end to over $200 billion. Remember, that's in today's dollars. Add interest over whatever period of time you chose. If it's $200 billion and we pay it off in three years at 5 percent, then it will be about $225 billion. Pay it in 40 years at 12 percent and it's over a trillion.

Incidentally, that's why you hear such a wide range of estimates. They vary with the predicted interest cost and the period of repayment.

The figures I just gave you are the obvious costs. But they're not the total costs -- not by a long shot.

Losses of this magnitude don't exist in a vacuum. They have repercussion in other areas of the economy -- real estate in particular.

The normal real estate cycle is expected to be rigorous -- with fairly deep troughs. But the S&L disaster has made the normal down-swing in the cycle worse than normal. This is a real economy cost in putting billions of dollars on the market in a short period of time.

Let me review for you the real estate situation as reflected in our latest quarterly report.

* During the second quarter, banks in 22 states showed worsening noncurrent rates on their real estate loan portfolios. And this includes every state on the East coast.

* Noncurrent real estate loans increased by $3.2 billion in the second quarter, a 13 percent increase.

* Foreclosed real estate properties - increased by $2.1 billion during the quarter, a 15.5 percent increase.

* Net charge-offs on real estate loans totalled $1.36 billion in the second quarter, 76 percent higher than in the same period of 1989.

There has been a lot of talk in the press recently about a credit crunch -- and a lot of complaints in the real estate and building industries that this crunch is due to increased diligence by bank regulators. Of course it's true, banks have tightened their lending policies. It's the only prudent thing to do when you look at our quarterly figures -- but it does increase the costs of disposing of properties -- since there's better financing available in the private sector.

History will assess the ultimate cost of the S&L debacle. And eventually we may find that the highest cost was our loss of confidence in our political system's ability to deal with a financial crisis of this magnitude.

Edward Gibbon once said that.."Great speakers fill you with despair, the bad ones with terror." I don't want to do either, so let me switch to a more positive theme and tell you what the Resolution Trust Corporation is doing to minimize the costs -- at least the more obvious costs.

During its brief history -- the Resolution Trust Corporation has, I think, achieved a great deal.

Consider that just fourteen months ago the RTC had only one employee ---- me. Now it has 5000. And every one a duplicate of yours truly.

No. Truthfully, the people at the RTC are a remarkable young group. Under the fine leadership of David Cooke, they've done more business -- made more sales than IBM in the same 12 month period.

You know, I've been asked why we didn't hire some high-priced, Wall Street executive type to head-up the RTC.

We needed someone who could operate in a government bureaucracy with the efficiency of a private sector manager. Few people could have handled this start-up as well as David.

Let me list just a few of the RTC's accomplishments.

* As of October 5, the RTC had taken control of 492 thrifts with total assets of about $258 billion. If you think about it for a second, that's a major feat in itself.

* It has sold, or in a few cases paid off, the insured deposits of 286 institutions. It has been averaging nine sales a week since the start of the second quarter. By any standards that's a good pace.

* A total of $60 billion in assets were sold in the RTC's first twelve months.

Unfortunately, there are more troubled thrifts coming our way. OTS has identified 206 more thrifts with about $161 billion in assets likely to need RTC help, and yet another 350 thrifts with about $170 billion in assets that are marginally okay.

The RTC tries to sell these assets, which are mostly real estate related as quickly as it can with the least amount of disruption to the market place. We're structuring large packaged sales, trying auctions, and we've set up a national sales office in Washington. For big buyers we have a sales person to lead them through the maze of Federal rules and bureaucracy.

We're putting the finishing touches on a pilot program to offer hard-to-sell commercial assets in large packages of up to $500 million.

I want to emphasize that most of our real estate assets are <u>not</u> big dollar items.

One recent analysis shows that of 40,000 properties, more than 76 percent had individual values of less than $100,000. In fact, if we concentrated only on the top 7 percent of the items in our portfolio, we would capture 80 percent of the entire portfolio value. And this is true for our delinquent loan portfolio as well.

The RTC is making plans to sell these smaller assets as quickly as possible. In the first quarter of next year the RTC hopes to hold a series of auctions and accept sealed bids for almost all real estate properties under $100,000. We may even conduct sealed bid sales of single family homes for eligible buyers under RTC's Affordable Housing Program.

The RTC sales centers also are planning to package all delinquent financial assets with individual book values of less than $50,000. Most of these assets may be sold "absolute" with the highest bidder taking the property or portfolio. The faster disposition of these small assets will save money and free up our staff to concentrate on where the real dollars are recovered.

Well, in spite of all the good work done so far by the RTC, the problems generated by the S&L fiasco are going to be with us for a long while. And the cost of solving these problems will be enormous.

But you know, the experience we gain may be well worth the price if we learn our lessons: What lessons ---- these lessons:

* Government guarantees are not free........they can be devastatingly costly, and there are over 6 trillion of guarantees in existence.

* Deposit insurance is one of government's most dangerous institutions if it is not properly controlled.

* Items of ideological faith (such as deregulation) must be tempered by reality.

* And above all, sweeping our problems under the rug or packing them in ice will make them worse.

So let's just hope that the cost of the S&L disaster will be the full price of our wisdom. Let's hope we can learn from experience.

I've enjoyed being with you today, and I'll be happy to take your questions. Thank you.