American Bank Bailout

Where is the Bailout Money?

The bailout has been a topic of conversation at nearly every social gathering I am been at in the last few weeks. And most of the time one question surfaces, where is the bailout money? The reason taxpayers are asking that is due to a news story that came out before Christmas stating that the largest banks can't exactly track how they are spending the money.

Now I did have one lawyer explain to me that often these funds are placed in a pool so it isn't easy to track them. And I will give the banks some slack on that since I realize that is probably the case. But let's think about this for a moment.

If I were asking for a loan from the bank, wouldn't you expect them to ask me where the money is going? And if I needed an additional loan, wouldn't you expect the bank to want a detailed history of what I did with the previous loan? Now keep that in the back of your mind as you hear what some of the bank officers have been saying.

A spokesman for JPMorgan Chase said: "We've lent some of it. We've not lent some of it. We're not given any accounting of, 'Here's how we're doing it.'"

A spokesman for SunTrust Banks said: "We're not providing dollar-in, dollar-out tracking." By the way, they have already received $3.5 billion in taxpayer dollars.

A spokesman for Regions Financial Corp said: "We manage our capital in the aggregate." They also have received $3.5 billion from the financial bailout.

I don't know about you, but that doesn't inspire much confidence in me. Remember that lawmakers did bring bank

executives to Capitol Hill and encouraged them to lend the money and not hoard it or spend it on corporate bonuses. It appears that some have, but there does not seem to be any negative consequences for doing so.

One of my recent guests [on the Point of View radio program] is Representative Scott Garrett (a member of the House Financial Services Committee) who asks: "Where is the money going to go to? How is it going to be spent? When are we going to get a record on it?" These all sound like good questions that need to be answered.

What Caused the Financial Crisis?

What caused the financial crisis? We have heard lots of accusations and criticisms, but it is hard to know who to believe. President-elect Barack Obama said throughout the presidential campaign that it was deregulation and a conservative approach to economics that was to blame. He said: "Eight years of policies that have shredded consumer protections, loosened oversight and regulation, and encouraged outsized bonuses to CEOs while ignoring middle-class American have brought us to the most serious financial crisis since the Great Depression."

So is the current crisis a result of these policies? Is deregulation the culprit? Kevin Hassett proposes a simple test of this view. He points out that countries around the world have very different regulatory structures. Some have relatively light regulatory structures, while others have much more significant intrusion into markets.

If the premise by Barack Obama is correct, then those countries that have looser regulations should have a greater economic crisis. But that is not what we find. If you plot the degree of economic freedom of a country on the x-axis and the percent of change in the local stock market on the y-axis, you find just the opposite of what Barack Obama states.

The correlation is striking. Draw a line from countries with low economic freedom (like China and Turkey) to countries with greater economic freedom (like the United States) and you will notice that most of the countries hug the line. Put another way, the regression line is statistically significant.

If Barack Obama is correct the line should be downward sloping (meaning that countries that are freer economically had a biggest collapse in their stock markets). But the line slopes up. That seems to imply that countries that are economically free have suffered less than countries that are not. Of course, a single graph and a statistical correlation certainly does not tell the whole story. But it is interesting that the current data seems to prove just the opposite of what Barack Obama has been arguing.

Cost of the Bailout

How much is that bailout going to cost us? Nobody seems to know, but even when I try to give some numbers for it, it doesn't compute. So I was encouraged to see that someone took the time to put the current bailout numbers in perspective.

Barry Ritholtz is a financial blogger and Wall Street analyst. He has found (as I have found) that people have a hard time comprehending the dollar amounts. While doing research for his book, *Bailout Nation*, he needed some way to put this into proper historical perspective. He says that if you add the latest Citi bailout, the total cost now exceeds $4.6 trillion dollars. By the way, I have seen numbers much larger than that (which may include loan guarantees which may not actually end up costing us). But what does $4.6 trillion dollars look like?

Jim Bianco (of Bianco Research) crunched the inflation adjusted numbers. The current bailout actually costs more than all of the following big budget government expenditures. The Marshall Plan ($115.3 billion), the Louisiana Purchase ($217 billion), the New Deal ($500 billion est), the Race to the

Moon ($237 billion), the Savings and Loan bailout ($256 billion), the Korean War ($454 billion), the Iraq war ($597 billion), the Vietnam War ($698 billion), and NASA ($851.2 billion).

Even if you add all of this up, it actually comes to $3.9 trillion and so is still $700 billion short (which incidentally is the original cost of one of the bailout packages most people have been talking about).

Keep in mind that these are inflation-adjusted figures. So you can begin to see that what has happened just in the last few months is absolutely unprecedented. But until you run the numbers, it seems like Monopoly money. But the reality is that it is real money that must either be borrowed or printed. There is no stash of this money somewhere that Congress is putting into the economy.

The current economic meltdown is significant, but the solution that members of Congress and financial experts on Wall Street are offering is terribly expensive.

Government Ownership of Banks?

One of the lingering questions about the bailout is how long the government will have ownership of the banks. At the moment, the federal government is planning on purchasing $250 billion worth of shares in American banks. Is it possible that government will hold the bank shares indefinitely? Terrence Jeffrey of CNSNews.com believes that this could be an unintended consequence. Let me explain.

While the law doesn't say that government can buy ownership interest in banks, it does allow purchases in "any financial instrument that the secretary, after consultation with the chairman of the Board of Governors of the Federal Reserve System, determines the purchase of which is necessary to promote financial market stability." This act also allows

“such actions as is necessary, that the secretary might deem.”

So how long can the treasury secretary hold these assets? Actually, the law sets no limits. A Treasury spokesman told CNSNews.com that “We can hold them for as long as we want.” Now, let’s be fair, Treasury Secretary Hank Paulson does not envision the government having a permanent ownership stake in various banks. But let’s also be realistic. He won’t be the treasury secretary next year.

The plan that was drafted envisions the government selling the stock back to the banks. It also prevents elected officials from using government ownership of the banks for their own political advantage. This is oversight actually takes place through the Office of Thrift Supervision, the Office of the Comptroller of the Currency, the Federal Reserve, and the Federal Deposit Insurance Corporation.

Now the plan does allow banks to buy back its shares from the government in the first three years, if it can raise 25 percent of the value of the shares by selling stock. But these are subject to the approval of the primary bank regulator.

But the bottom line is this: banks are not guaranteed they can buy back their stock. Although Congress didn’t intend for government to permanently own banks, it is possible they may do so anyway.

Seven Hundred Billion

How much is $700 billion? When these numbers are so big we lose all proportion of their size and potential impact. So let me use a few comparisons from a recent Time Magazine article to make my point.

If we took $700 billion and gave it to every person in America, they would receive a check for $2,300. Or if we decided to give that money instead to every household in America, they would receive $6,200.

Here’s another idea, if we took that money and decided to start paying the income taxes for each American, it would pay the income taxes for every American who makes $500,000 or less a year.

Since gas prices have been high, what if we decided to use this money to buy gasoline for every car in America? If we did that, no one would have to pay for gas for the next 16 months.

What if we were able to use $700 billion to fund the government for a year? If we did so, it would fully fund the Defense Department, the State Department, the Treasury, the Department of Education, Veterans Affairs, the Department of the Interior, and NASA. If instead we decided to pay off some of the national debt, it would retire seven percent of that debt.

Are you a sports fan? What if we used that money to buy sports teams? This is enough money to buy every NFL team, every NBA team, and every Major League Baseball team. But we would have so much left over that we could also buy every one of these teams a new stadium. And we would still have so much money left over that we could pay each of these players $191 million for a year.

So how would $700 billion stack up against the economies of various countries in the world? This amount of money would create the 17th largest economy in the world, roughly equal to the economy of the Netherlands.

Is $700 billion a lot of money? Of course it is, and we all need to think about this the next time Congress votes to spend money. I’m Kerby Anderson, and that’s my point of view.

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