E-Memo

TO: INVESTORS/MEMBERS/PARTNERS AND FRIENDS
FROM: Jon Bruss and James Bruss
DATE: December 23, 2009
SUBJECT: The Fat Cats and the Lender-in-Chief

I did not run for office to be helping out a bunch of fat cat bankers on Wall Street…. The people on Wall Street still don't get it. – President Barack Obama on *60 Minutes*, December 13, 2009

Nine days ago, on a Monday, President Obama met with several chief executives of the country's largest financial companies to explain to them how lending more money will help the economy. That is, on Monday the 14th of December. The day after excoriating those same fat cats. During a nationally televised interview on arguably the most important news show on TV. And they're the ones who "still don't get it."

We have endeavored to keep this monthly missive out of the political morass, but this time we've been forced off-piste. Bankers have enough to worry about just in dealing with (rightfully) discontented shareholders or getting their ears boxed by regulators (whose instructions are often inconsistent, but no less obligatory for that). What they don't need is the politicization of their industry they've experienced over the last year plus. It behooves no one—not Congressmen, not Senators, and, most of all, not the President—to turn any business into a political whipping boy. But with the banking industry reeling from the financial crisis, it now seems discretion is out the door and point-scoring potshots are in.

But perhaps worse—as we've now grown somewhat calloused to the noxious populism coming out of Washington—is the mixed message for bankers. Regulators have warned banks to clean up their acts and their assets—i.e., stop making stupid loans! Late to the party, perhaps, but prudent advice nevertheless. At the same time, squeaky wheels in Congress and the White House harangue banks to lend more. It is, we are told, their duty because we, the taxpayers, bailed them out. (On the subject of duty, we can argue all day whether TARP and its capital injections were necessary to save the financial system, but in all fairness we must recall that the chiefs of many of the largest financial companies were locked in a room by Lord High Treasurer Paulson, until they agreed to take the government's "bail out".)

Duty or not, perhaps one consideration the President should take into account is whether it makes good sense for banks to increase lending. As a bank increases its lending, it risks increasing bad credits. Does no one remember the word "subprime"? The massive financial crisis over the last couple years is the son of a thousand fathers: an easy money Fed policy; political entanglements like the Community Reinvestment Act (which actively encouraged bad credit underwriting); greed; institutionalization of too-big-to-fail ideology; etc. But surely, subprime lending and other risky loans were among the greatest villains.

Why does the President want the banks to do it all over again? Or does he? It's fair to ask whether the President is serious? One must assume, after all, that Secretary Geithner, Chairman Bernanke and Chairwoman Bair have communicated to the President that their employees—those regulators speaking directly with banks on a day-to-day basis—have different marching orders. Those regulators have more and more frequently required banks to raise capital levels well above the written legal levels and they've required banks to take larger reserves against performing loans. As a direct result, banks have less money to lend out. These actions run counter to increasing credit.

There's a more basic story here as well. As the economy has contracted, individuals and businesses alike have tightened their belts, spending less and borrowing less. Moreover, both were caught by the contraction in overleveraged positions and have been pressed into deleveraging. This isn't a back page story and shouldn't be news to anyone in Washington. As banks raise their credit standards, both out of prudence and because their regulators have forced them to, and demand for credit shrinks, the amount of outstanding credit is necessarily impacted.

If he's not serious, the President can only be trying to score political points at the expense of banks, attacking the fat cats for not "getting it" one day, and very publicly browbeating them for not fulfilling their duty to lend money the very next day. If he is serious—along with those playing the same tune in Congress—we have cause for concern. One can only marvel at the ability of politicians to hold forth on topics they nothing about. It is a skill mastered by any politician worth his salt. But apparently only some politicians (unfortunately, an ever smaller group) have mastered the skill of knowing when to shut up, of not laying bare their profound ignorance on a subject.

Perhaps this is a necessary side-effect of the sound bite political culture we live in, but when politicians talk there are real consequences. When Chrysler's bondholders were called to the carpet for attempting to enforce their entirely legitimate contracts last spring and denounced as "speculators" trying to get rich off the government's largesse, businesses around the country were scared and felt bullied. Not a good way to encourage companies to start spending money on production or investments. When the fat cats on Wall Street got dragged into Washington for a lecture on their duty to lend, businesses around the country were confused. These awful people who got us into this mess are supposed to do more of . . . what got us into this mess? The fat cats probably didn't feel bullied (three didn't even show up, attending by phone instead) but they should be concerned that many of those now driving financial regulation and policy don't really know what they're talking about.

Some problems are too important for Washington to solve. This must be a difficult truth for many in Congress and the White House to swallow. As George Will wrote in the December 13 *Washington Post*, the President "wants to fix *everything*." (Emphasis in the original.) When it comes to the banking industry, the best way to do that is step back and let the professionals do their job.

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