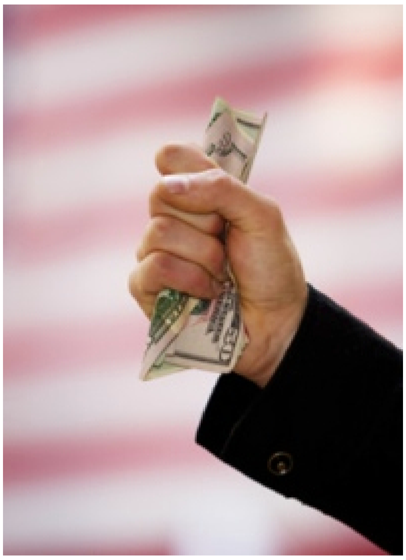
Forget TARP — the Real Bailout Came from the Fed



It took a Freedom of Information Act request, months of litigation, and even an act of Congress, but dogged investigators at *Bloomberg News* finally gained access to the figures, and, after crunching the numbers, concluded that the Fed — unilaterally and with zero congressional oversight — had doled out as much as $1.2 trillion in taxpayer monies. That's about $500 billion more than the separate, hotly contested, and widely publicized $700 billion bailout pushed through Congress at the same time.

Small wonder, then, that a firm like Morgan Stanley, widely expected during the crisis to be the next big financial to fall after the demise of Lehmann Brothers, suddenly announced, on September 29, 2008, that it had “strong capital and liquidity positions.” The markets heaved a sigh of relief and Morgan Stanley was able to hang on. What Morgan Stanley did not disclose was that it had received more than $107 billion from the Federal Reserve, a figure that, according to *Bloomberg*’s Bradley Keoun and Phil Kuntz, “was the source of almost all of Morgan Stanley’s available cash, according to the lending data and documents released more than two years later by the Financial Crisis Inquiry Commission.” What’s more, Keoun and Kuntz note, “the amount was almost three times the company’s total profits over the past decade.”

While Morgan Stanley got the biggest Fed bailout, other banking behemoths were not far behind. Bank of America got $91.4 billion and Citigroup took in $99.5 billion. Nor was the Fed’s largesse restricted to American banks. In confirmation of long-held (and publicly voiced) suspicions on the part of Congressman Ron Paul and other adversaries of the Federal Reserve, Bloomberg was able to determine that, of the top borrowers from the Fed, nearly half were European banks like the Royal Bank of Scotland ($84.5 billion), Switzerland’s UBS AG ($77.2 billion), and Germany’s Hypo Real Estate Holding AG ($28.7 billion, or roughly $21 million *per employee*). London’s Barclay’s Plc borrowed $64.9 billion and Frankfurt’s Deutsche Bank AG got $66 billion. Other European firms that benefited from the Fed’s largesse include Dexia SA (Belgium’s largest bank) and Societe Generale SA (France).

The Federal Reserve fought fiercely to keep these and many other similar bailouts secret, using the self-serving argument that publicizing the names of institutions that received bailouts would jeopardize public trust by raising the specter of insolvency. Write Keoun and Kuntz:

> Fed officials argued for more than two years that releasing the identities of borrowers and the terms of their loans would stigmatize banks, damaging stock prices or leading to depositor runs. A group of the biggest commercial banks last year asked the U.S. Supreme Court to keep at least some Fed borrowings secret. In March, the high court declined to hear that appeal, and the central bank made an unprecedented release of records.
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> Data gleaned from 29,346 pages of documents obtained under the Freedom of Information Act and from other Fed databases of more than 21,000 transactions make clear for the first time how deeply the world's largest banks depended on the U.S. central bank to stave off cash shortfalls. Even as the firms asserted in news releases or earnings calls that they had ample cash, they drew Fed funding in secret, avoiding the stigma of weakness.

As if loaning out such an enormous sum in taxpayer dollars to both domestic and foreign banks were not outrage enough, the Federal Reserve dramatically relaxed its own standards for collateral, in effect permitting borrowing institutions to dump junk assets as collateral for bailout monies. As Keoun and Kuntz explain:

> Typically, the central bank accepts only bonds with the highest credit grades, such as U.S. Treasuries. By late 2008, it was accepting "junk" bonds, those rated below investment grade. It even took stocks, which are first to get wiped out in a liquidation.
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> Morgan Stanley borrowed $61.3 billion from one Fed program in September 2008, pledging a total of $66.5 billion of collateral, according to Fed documents. Securities pledged included $21.5 billion of stocks, $6.68 billion of bonds with a junk credit rating and $19.5 billion of assets with an "unknown rating," according to the documents. About 25 percent of the collateral was foreign-denominated.

It is unclear how much of the $1.2 trillion has been repaid or was adequately collateralized. But the clear lesson to be gleaned from this unprecedented window into the workings of the Fed is that the international banking cartel, anchored by central banks empowered to print money as needed to paper over financial debacles like the crash of 2008, does not scruple to put others' money at risk. This is the ultimate form of moral hazard, in which the entire financial sector is systematically shielded from the consequences of its own follies. This "too-big-to-fail" mentality extends far and wide among the institutions that make up America's de facto financial aristocracy. Unfortunately, it also reaches overseas to their allies in Europe, whose interests are so interlocked with those of Wall Street that our own government is willing to put American taxpayers on the hook for bankers in London, Paris, and Brussels.