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Adventures in the Loan Trade

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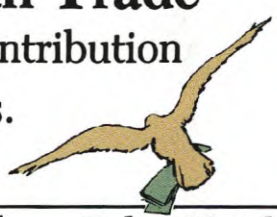

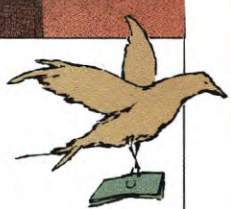

Garry Wills on Seymour Hersh. . . John Naisbitt's

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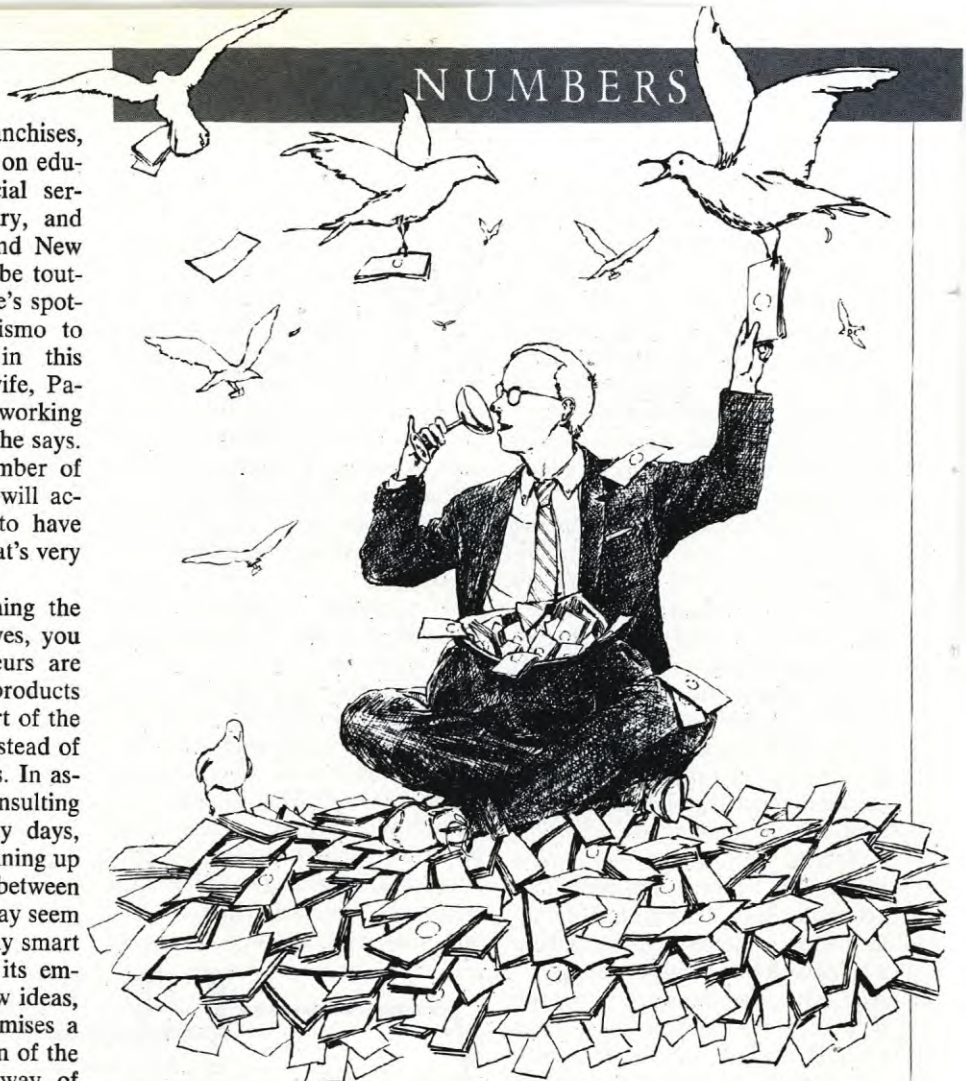
the works are foreign franchises, special-issue *Trend Reports* on education, health care, financial services, and the food industry, and new offices in California and New England. Naisbitt will also be touting the newest megatrend he's spotted, "the shift from machismo to androgyny." Caught up in this force, he and his second wife, Patricia Aburdene, "will be working closer and closer together," he says. "We've been making a number of speeches together and that will accelerate. It will be useful to have more couples as models. That's very rarely done."

Naisbitt will be establishing the School for Intrapreneurs (yes, you read that right). Intrapreneurs are people who develop new products and services with the support of the companies they work for, instead of starting their own businesses. In association with a Swedish consulting firm, TNG will offer twenty days, over a six-month period, training up to three intrapreneurs for between $70,000 and $100,000. It may seem painfully self-evident that any smart company would encourage its employees to come up with new ideas, but the TNG literature promises a "systematic conceptualization of the intrapreneur as a normal way of life. . . ."

Naisbitt will also be exercising his evangelical side on the lecture circuit: "I really think the great, if not the only hope for world peace is the global economy [which, incidentally, is Megatrend number three]. We are going that way, except for this neoprotectionism. I want to make speeches about world peace through world trade. . . ."

"I've become a more spiritual person recently," he says. "I've seen the powerful relationship between mind, spirit, and body. You can't deal with these things compartmentally. We know everything is related to everything else. The trick is to see the whole. When I start to learn too much about something I back off. I want to know a little about a lot."

If that trend continues, he'll eventually know nothing about everything. ■



ADVENTURES IN THE LOAN TRADE

by S. C. Gwynne

A young banker reveals his contribution to the international debt crisis.

IT IS an odd business, selling money door to door at the edge of the civilized world. It is odder still when the money comes not from out of the anonymous depths of the Eurocurrency market—some dark relay through Nassau, Hong Kong, or Zürich—but from the savings accounts of Americans living in Ohio.

S. C. Gwynne is a banker turned writer who lives in Los Angeles.

Those Americans, like Americans everywhere, are just beginning to realize that their money is no longer being used to build the house next door.

I used to sell their money for a living. I used to travel the world for a medium-sized Midwestern bank with $5 billion in assets.

Along the way, I was engaged in some of the startling "business as

usual" banking practices that have begun to plague the world financial system.

IT IS 1978. Thanks to the venal, repressive regime of President Ferdinand Marcos of the Philippines, I am safely and happily roosting in one of Manila's best hotels, the Peninsula. I am about to set in motion a peculiar and idiosyncratic process that will result in a $10 million loan to a Philippine construction company, a bedfellow of the Marcos clan—a loan that will soon go sour. I am unaware that any of this is going to happen as I enter the lobby of the Peninsula on my way to dinner, still trying to digest the live octopus that a Taiwanese bank served me last night, and attempting to remember exactly what it was they wanted and why they had gone to so much trouble.

International banking is an interesting business anyway, but what makes it rather more interesting in this case—both to me and to the hapless Ohioans whose money I am selling—is that I am twenty-five years old, with one and a half years of banking experience. I joined the bank as a "credit analyst" on the strength of an MA in English. Because I happened to be fluent in French, I was promoted eleven months later to loan officer and assigned to the French-speaking Arab countries of North Africa, where I made my first international calls. This is my third extended trip, and my territory has quickly expanded. I have visited twenty-eight countries in six months.

I am far from alone in my youth and inexperience. The world of international banking is now full of aggressive, bright, but hopelessly inexperienced lenders in their mid-twenties. They travel the world like itinerant brushmen, filling loan quotas, peddling financial wares, and living high on the hog. Their bosses are often bright but hopelessly inexperienced twenty-nine-year-old vice presidents with wardrobes from Brooks Brothers, MBAs from Wharton or Stanford, and so little credit training they would have trouble with a simple retail installment loan. *Their* bosses, sitting on the senior loan committee, are pragmatic, nuts-and-bolts bankers whose grasp of local banking is often profound, the product of twenty or thirty years of experience. But the senior bankers are fish out of water when it comes to international lending. Many of them never wanted to lend overseas in the first place, but were forced into it by the internationalization of American commerce; as their local clientele expanded into foreign trade, they had no choice but to follow them or lose the business to the money-center banks. So they uneasily supervise their underlings, who are the hustlers of the world financial system, the tireless pitchmen who drum up the sort of loans to Poland, Mexico, and Brazil that have threatened the stability of the system they want to promote.

The system is under severe strain. In 1975, American banks had $110 billion in loans outstanding overseas. By the end of 1982, the figure had risen to $451 billion. The top nine U.S. banks have roughly $31 billion, or *over 112 percent of their combined capital,* in loans to Mexico, Brazil, and Argentina alone, all countries that have had to "reschedule" debt in order to avoid catastrophic defaults.

MANILA is heating up as I walk through the lobby of the Peninsula. From the balcony, a Filipino band plays to the crowd of traders, tourists, bankers, local businessmen, and old Asia hands, who sit at small tables waiting for girls or contacts or nothing at all.

Though I don't know yet what is going to happen, I know that something's up. I arrived in the morning on a China Air flight from Taipei. At the edge of the jet ramp, to my surprise, I was met by an "expediter," an odd creature of the third world who specializes in facilitating arrivals and departures of important people. The "expediter," who introduced himself as "Joy," was an envoy of a client of mine, the Construction and Development Corporation of the Philippines (CDCP), a local Philippine construction company we had been courting for years without success. "Joy" had apparently paid off the security agents at the customs and immigration line. We went through in two minutes what took the other 300 people, sweating and cursing in the tropical heat, an hour and a half. He then took me through the crowd of screaming touts on the arrival deck to a waiting Jaguar, which came equipped with air conditioning, a good stereo system, and a very pretty twenty-year-old girl. The girl was unexpected. Bangkok Bank gives me a silver Lincoln, but no girl. The Saudis give me a stretch Mercedes and a clandestine liter of Johnny Walker Black, but no girl. In the intricate world of Asian business, where the quid pro quo is the essence of every deal, such things are done for a good reason. Yes, I thought, something *is* up . . .

Now, hours later, I am met again by Joy under the porte-cochere of the Peninsula Hotel. He wears an immaculate white uniform. He takes my briefcase, containing $5,000 in traveler's checks, a $9,000 negotiable airline ticket, my passport and credit cards—in short, all that's standing between me and a jail in Intramuros—and disappears. We are playing the "good faith" game. A minute later, the red Jaguar slides up to the dispatch, with my briefcase intact and the girl smiling prettily, and we go off in splendid, smooth silence into the honking, grid-locked traffic jam that is Manila on a Saturday night. On the way, the girl tells me that she and the Jaguar are "at my service" for the remainder of my stay.

I am taken to an expensive restaurant in Makati, where the president of the company, whose name is Rudy, is throwing a gala dinner bash in my honor. My bank has been calling on this company for five years. We have bought them twenty dinners. We have taken them golfing and scuba diving. We send them whiskey and cigars at Christmastime. Until now, all we have gotten in return is polite conversation. After eight courses, and enough

liquor to intoxicate the Muslim population of Mindanao, the other shoe drops. Rudy announces, in slurred English, that he would like to borrow money. He says he wants to buy earth-moving equipment from my bank's client in the U.S., for a reclamation project on Manila Bay.

"How much were you thinking about?" I ask, in equally slurred English.

"Ten million," he says, and laughs. "My vice president will give you the details in the morning."

Five minutes later, the finance minister of the Philippines "drops by" to meet me. Nothing is said about the loan. But he is unctuous and polite, and makes a point of calling Rudy "my good friend." Maybe I'd like to go to Baguio, they suggest. A nice gesture, I think, unaware that the plane, owned by the company, is gassed up and waiting to take me to a fabulous hotel in the northern mountain resort, which is also owned by the company.

THE international banker moves in a narrow ambit overseas. Because he is dressed in a suit that costs more than the average native makes in a year, he does not take excessive interest in the local people. He does not take a walk down a blind alley, or sample the local bars on a Tuesday night. He rarely walks anywhere, thus keeping a safe distance from the prospect of physical danger. But there is still danger, in different, more subtle forms: such as forgetting to hide your "Israeli" passport as you pass through customs in Algiers; or forgetting to leave your bottle of scotch behind when you enter Saudi Arabia. The penalty for these offenses is "detention," usually in an immigration jail, for an indefinite period of time, Then there is the possibility that your driver in one of the strict Muslim countries will have an accident, or run someone down. According to current exegesis of the Koran, the driver and car would not have had the accident if you had not hired them, and thus you are fully and personally liable for all damages. This accounts for the rather humorous and not infrequent sight of American bankers fleeing from the scene of minor accidents, briefcase in hand, into the relative anonymity of the bazaars and tenements. In Manila you are fairly safe, but if you enjoy too much of your host's hospitality, it is likely that you will contract a social disease.

As a loan officer you are principally in the business of making loans. It is not your job to worry about large and unwieldy abstractions, such as whether what you're doing is threatening the stability of the world economy. In that sense, a young banker is like a soldier on the front lines: he is obedient, aggressive, and amoral; his efficiency depends precisely on that very narrow view of the world around him. American banks, through the agency of loan officers like me, have made a number of questionable loans in countries whose balance of payments is so far in arrears that, according to Citicorp's Walter Wriston, "ability to repay" is no longer the main consideration. All that matters now is "access to the marketplace," meaning the ability to borrow even more. This is a convenient rationale, in view of the big banks' exposure in countries that have recently been unable to service their debt. The theory goes something like this: as long as a country can continue to borrow money, it will, in effect, be able to "roll over" its debt indefinitely, in much the same manner as the U.S. government "rolls" the national debt. As long as the country can roll its debt, the banks will be paid on schedule and the country will not become insolvent. But the banks are cornered. Unless they pump in more money, they stand to be forced into massive write-offs, and even more serious chain-reaction consequences, owing to the "cross-default" clauses in many of the loans.

There is another curious aspect to this: even though the banks may allow a country such as Poland to "reschedule" its debt—allowing it twenty years instead of ten to repay, for example—the *interest* payments keep coming. And it is interest that hits the bottom line of a bank's profit-and-loss statement. This means that Citibank can have a very good year even though many of its loans may be in serious trouble. The banks may have been imprudent in making the loans in the first place, but they are both clever and scrupulous when it comes to protecting the value of their assets.

At the root of this worldwide lending problem is a very simple concept called "security." When you borrow money to buy a car, the bank takes title to the car as "security." If you default under the terms of your loan, the bank can sell the car and recoup the rest of its money. But international banks cannot "collect" a power plant in Thailand, or a hospital in Dubai, or even a Caterpillar tractor in the jungles of Kalimantan. They cannot "tag" a banana crop in the Philippines, or grab the copper as it comes out of the mine in Chile and sell it in Chicago. In international lending, American banks frequently violate the oldest precepts of lending against security. As a domestic credit analyst, I was taught to develop reasonable asset security for all loans unless the borrower was of impeccable means and integrity. As an international loan officer, I was taught to forget about that, and instead to develop a set of rationales that would make the home office feel good about the loan, even though, technically, it was "unsecured."

IN MANILA, I move dreamily through my appointments, fairly salivating at the prospect of a single $10 million loan. I strike myself as a rather glamorous individual at this point, moving huge sums of money with a stroke of the pen, greasing the vast machinery of international trade. Of course, I cannot personally approve this loan. The bank may be ignorant in certain ways, but it is not stupid. This loan will have to be presented back at the home office to the gray-haired, pink-faced bankers on the senior loan committee. They will peer at me over the rims of their bifocals and ask questions like, "Why is their

current ratio declining, in view of increased sales?"

The remainder of my trip includes stops in Hong Kong, Kuala Lumpur, Tokyo, and Seoul. I am able to develop a few prospects, and a severe case of dysentery. But mainly I'm dreaming of that loan, writing pages and pages of pros and cons, imagining what it will be like inside the loan committee. In spite of my enthusiasm, and my growing sense of self-importance, there is a certain con that keeps cropping up and is finally given life by a fellow banker from Chase Manhattan, whom I sit next to on the flight into Kuala Lumpur.

"Who do you do business with in Manila?" he asks, after ordering our fifth round of scotch, which is what keeps international bankers happy on their long trips. CDCP, I tell him.

"They're in bed with Marcos," he says. "That's okay. But they're leveraged up to their ears."

When a banker says that a company is "leveraged," he means that the company's debt greatly exceeds the owners' equity in the company. In the United States, bankers are taught early on that leverage is a no-no, that it puts the lender in the high-risk position of having to fight for the company's few capital assets in the event of bankruptcy. I sneak a glance at the leverage ratio of CDCP. It is seven to one. One to one is considered healthy, two to one dangerous. It suddenly occurs to me that it might be pure insanity to make this loan.

"You better have Marcos's signature, *in blood*, on that one," the Chase banker says, laughing.

BACK AT the home office, high above the murky winter air of Cleveland, still bleary from four weeks of accumulated jet lag, I begin to sort out my trip. I am trying to remember all those three-hour lunches with five courses and two bottles of wine and what on earth I was talking about.

It is something of a cliché to say that bankers are trained pessimists. While this may be true of the retail banker, what characterizes the international banker nowadays is optimism. For example, when the senior vice president asks you how a certain country is doing in general, you don't say "Well, Phil, I think it's going down the tubes." Even if it's true, it is not in your interest to say that, because Phil can easily make it impossible for you ever to develop a loan in that country. And your job performance is rated according to how many loans you make. As a credit analyst, I once remarked to the vice president in charge of Mexican loans that in my opinion no amount of petroleum was going to change the fact that 30 million people would be living in Mexico City by the year 2000; and that no amount of social engineering could make all that oil money trickle down to that many people. I was told not to put this in my country report.

"We're concerned about repayment, pure and simple," he said. "Not demographics. We're not demographers. They've got so much oil they don't know what to do with it. Play that up."

We made the loan, and the borrower defaulted three years later, in the wake of the devaluation of the peso.

Ah, optimism. It worked in Mexico, Argentina, Brazil, Poland—all countries that have had to "reschedule" debt, the current euphemism for "default." If it worked for them, I figure, it can work for me too, in a volatile, corrupt Asian country with serious balance-of-payments problems, and with a company leveraged seven to one.

But before I can develop this specious line of reasoning, my telephone rings. It is the chief financial officer of the earth-moving equipment company, a subsidiary of a major auto company and an old client of the bank.

"I hear you've been talking to our friends in Manila," he says. He is chatty, as though the difference in our rank means nothing to him.

"They were very hospitable."

"Charming fellows."

"They want us to finance the purchase of your equipment."

"I know," he says. "And we'd like you to give it a good, hard look," he continues, in a voice meant to remind me that his company has a great deal of money lodged with us in the form of demand deposits and pension funds.

I assure him that a good, hard look will be given to his proposal, and hang up. Ten minutes later, the president of my bank calls on the same subject. I am told to give it a good, hard look. What he means by that is that he wants to see this thing in loan committee, ASAP, damn the company's leverage, and damn the balance-of-payments problems in the Philippines, period.

THE INSTANT the wheels begin to turn on this deal, my enthusiasm wanes. I realize that I may well end up the whipping boy. After analyzing the company more closely, I can now see clearly that this is an "undoable" deal. I will take it before the senior loan committee, undergo a thirty-minute grilling, and be thrown out in disgrace. The president of the bank can then tell the client, in good conscience, that we gave it a "hard look," in spite of the fact that a young loan officer was made to look like a fool. I therefore undertake to develop one of the handy rationales that I have learned. I attempt, in bankers' parlance, to "cover my ass."

Now we're getting into real international banking, the sort of banking that makes it possible for Citicorp to lend $2 billion to a shaky country like Brazil. We are now in the realm of the "guarantee" and the "standby letter of credit," both nifty ways of shifting the borrower's weakness into some new area of supposed strength and reliability.

Let me explain. When the international loan you are proposing is less than sound, you may secure the guarantee of a third party to shore it up. The third party may be a private commercial bank, a government-owned commercial bank, or a foreign government. A government guarantee is best of all. If the guarantee party looks good on paper, most U.S. loan committees will buy it. Never mind that thousands of bad loans around the world were cheerfully supported by foreign governments, including those in Poland, which don't stand a snowball's chance in hell of being repaid before the millennium. But American banks persist in the decades-old notion that "banks and governments won't default."

Well, that's fine with me, and I set about securing a partial guarantee from the Philippines' largest bank, which has already put its name on more guarantees than it can possibly pay off. It is an easy process. The heads of both the bank and the construction company are wired into the same political terminals. This strategy will not only secure the affection of my president and my client but will also advance my career.

It takes only a month and a few dozen overseas phone calls to get the guarantee from the Philippine bank, which is handing them out these days like free samples. With the help of a cooperative credit analyst, who is three months out of an English degree from Ohio State, we package a stunning little credit that sweeps through all of the loan committees without even a flesh wound.

I am patted on the head by innumerable vice presidents, given a small raise, taken to the opera by the client, and sent to Hong Kong for the signing of the loan.

Three weeks later, we disburse $5 million, the first in a series of "drawdowns" that will correspond to shipments of earth-moving equipment. Although our transfer bank, Chase Manhattan, manages to lose the $5 million for a few frantic days, the money eventually lands in the right account.

A YEAR and a half after making this loan—and about a year before this loan went into nonaccrual—I left the bank for a job with one of the big West Coast banks. By the time the borrower suspended its debt payments, *all* of the loan officers who had worked on it had moved on to other banks. Such rapid job movement is common in banking. The market these days is so hot that, if you have done reasonably well in your job, you can not only double your salary but you can virtually pick the city in which you would like to live. Thus many of the people who make the big international loans are not around to collect them when they go bad, and, conversely, the people who are collecting the bad loans are not the people who made them in the first place, and therefore feel only vaguely responsible.

My Philippine loan went "bad" very quietly. Interest and principal payments simply stopped coming one day, without notice. It was impossible to get any sort of recent financial statement from the company, and it was equally impossible to track down the principals, who were ducking a host of other creditors as well. My successor spent several months on the intercontinental telephone lines trying to locate them. When he did, he was assured of immediate payment. The payment never came. There were further negotiations, and the bank deemed it prudent to "reschedule" the loan, in a way that would enable the company to repay over a longer period. As of this date, the bank has received only a fraction of the money owed by the borrower. To my knowledge, the guarantee of the Philippine bank has not been called.

So I move on, someone else is hired to clean it up, and the old boys on the senior loan committee are left to wonder what went wrong. They are doing a lot of wondering these days, with a large Mexican portfolio, 50 percent of which is in technical default, and with millions of dollars in loans to Eastern-bloc countries. They are doing nothing "wrong" as they see it, and certainly nothing even remotely as daring as the kind of thing the "go-go" banks in the money centers are up to. It is all just "business as usual," and will continue that way until some catastrophe descends on them, by which time it will be too late to do anything about it. ■