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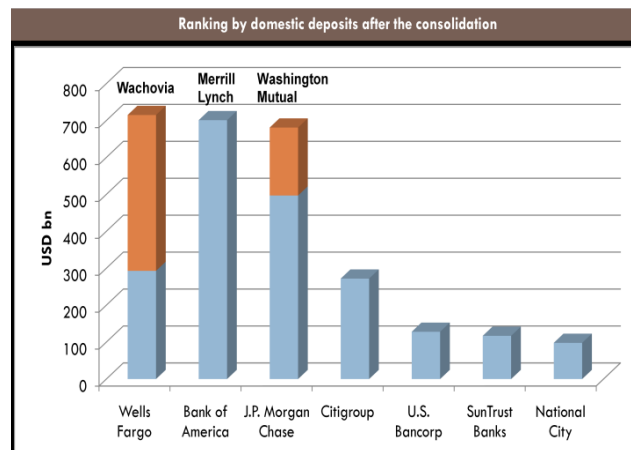
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What A Difference A Year Makes

“October. This is one of the peculiarly dangerous months to speculate in stocks in. The others are July, January, September, April, November, May, March, June, December, August, and February.” wrote, Mark Twain, the 19th century American humorist in Pudd’nHead Wilson published in 1894. A hundred plus years later, such satire is still just as cruel except this time around it is global.

With an annual blink of the eyes – taking inventory - the victims that range from the dead to the injured include: Bear Stearns, Lehman Brothers, Fannie Mae, Freddie Mac, Washington Mutual, Wachovia, and big names as well as the garden variety kind of commercial banks, investment banks, and hedge funds that have had to take government assistance package or sold off. And this is just the United States.

The subprime crisis which started in the summer of 2007 spun the market into a free fall when the US Government refused to provide any downside protection to potential investors of Lehman Brothers. Lehman scrambled to find a buyer but with no takers filed for bankruptcy. The fall of Lehman triggered a domino effect as depositors began to panic and liquidity was pulled back. The US government orchestrated a shot-gun approach to nationalization and sales of banks. Merrill Lynch sold itself to Bank of America. Goldman Sachs and Morgan Stanley converted themselves into bank holding companies to build market confidence and tap into the funds from the Central bank. Washington Mutual was closed by the government and later resold to J.P. Morgan Chase. Wachovia played a less-pretty-version of Helen of Troy and was bought out by Wells fargo after a tussle with Citigroup.



After these consolidation, the United States would be left with only three big banks. Collectively, these three big banks would hold around 22% of all United State's deposits. Wells Fargo would become the biggest bank by deposits, followed by Bank of America and J.P. Morgan Chase.

In the final analysis, the world seems to have agreed on one thing by pointing their collective plaintiff finger that the problem was brought about by froth – put straightforwardly – leverage. Alan Greenspan was fond of quoting a former governor of the Federal Reserve Bank William McChestney that: “the role of the central bank is to take away the punch bowl just when the party starts getting interesting”. While Alan Greenspan, to be fair (to him), did use words such as “irrational exuberance” to describe such liquidity-driven market and resultantly inflationary asset prices, he was however shy in actually taking away the punch bowl.

The US dollars is like salt water. The vast ocean surrounds every continent on the face of this earth and so do the dollars. Notice how every country in the world count their foreign reserves in US dollars and denominate a majority of the reserves in US dollars. So when dollar deposits flood the world markets, asset prices go up. And when the dollars are sucked out, so too collapse the asset prices around the world.

Beyond the borders of the United States, banks in the UK and Europe already skidded on ice. Three governments, Belgium, Netherlands and Luxemburg had to save Fortis bank. Britain has nationalized Northern Rock, Bradford & Bingley, and HBOS which may cost tax payers more than GBP 150bn. Private equity buyout fund J.C. Flowers also pulled out of potentially investing in Hypo Real Estate bank in Germany triggering the German government to rescue Hypo and guarantee private deposit accounts to maintain a modicum of stability in its market.

Scanning the world, the healthy banks with acquisitive means for the moment seem to be the Japanese and the Chinese banks. Nomura Holdings agreed to acquire Lehman in Asia Pacific amount up to USD 525mn. Mitsubishi UFJ Group invested USD 9bn in Morgan Stanley for a 21% interest.

Towards the end of last year (2007), many banks were trying to beef up its financial positions to prepare themselves for further write-offs. Most of these first wave came from the Sovereign Wealth Funds (SWFs). Citigroup was able to raise USD 37bn, including USD 7.5bn from Abu Dhabi sovereign wealth funds in Nov 2007 and USD 6.9bn investment from Government of Singapore Investment Corporation (GIC) and Kuwait Investment Authority (KIA) at top of 2008. China Investment Corporation (CIC) also bought 9.9% stake in Morgan Stanley for USD 5.6bn in December. Additionally, Merrill Lynch was also able to raise USD 13bn with USD 6.6bn from several funds including Korea Investment Corporation, KIA and Mizuho Corporation in the beginning of the year.

Besides that, in late April private equity giant TPG and consortium injected USD 7bn to save Washington Mutual but saw it's investment melted when

WaMU's stock price nosedived and then sold to JP Morgan Chase.

Private equities and their LPs including the SWFs are now conserving their "dry powder" waiting for the dust to settle with the inherent volatility and lack of confidence in the credit market. Besides, both private equity and SWFs are constrained by the regulation of not being able to hold more than a third of equity shareholding in US banks. As a result, several companies especially those in financial sectors and insurance companies are trying to strengthen themselves through alliances, increase capital or merging.

It seems that not only banks become insolvent but so do governments. In recent times, Iceland, Hungary and the Ukrainians have put their hands up for assistance from the IMF. It was only a few months ago that the IMF saw their role much diminished by the rise of SWFs and was reinventing themselves as a knowledge bank – a sort of "Mini-Me" of The World Bank. Over the next couple of years, the IMF won't have to worry about finding a new role for themselves.