Geithner Says Plan for Banks Is in the Works

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WASHINGTON — As lawmakers pressed the Obama administration for details of how it would assist financial firms that have been rapidly deteriorating, Treasury Secretary Timothy F. Geithner said Wednesday the administration is working on a comprehensive plan **to "repair the financial system."** Mr. Geithner declined to provide any specific details or to address rising calls for the creation of a government institution to buy or guarantee the declining assets at several of the nation's largest banks. **He discouraged speculation that the plan would include the nationalization of some banks. "We have a financial system that is run by private shareholders, managed by private institutions**, and we'd like to do our best to preserve that system," he said.

But b**ank stocks surged on hopes the government was moving toward creating a "bad bank" to purge toxic assets from balance sheets that are rapidly deteriorating as the economy worsens**. On Wednesday, the Federal Reserve cautioned that the economy was still spiraling downward on many fronts.

According to several Wall Street officials, senior administration members spent the weekend and the last few days reaching out to top bankers for their views on how a bad bank should be structured. Lawrence H. Summers, head of the White House's National Economic Council; Sheila C. Bair, the Federal Insurance Deposit Corporation chairwoman; and Mr. Geithner have been involved in the talks, the Wall Street officials said.

Federal policy makers are discussing how to use the second $350 billion portion of bailout funds. **About $50 billion to $100 billion is expected to be allocated to stave off home foreclosures. That would leave up to $250 billion available for the banks, with the bulk going to buying troubled assets**. On Wednesday, the head of the Congressional Budget Office told lawmakers that weakening banks would probably need **hundreds of billions in additional funds beyond the Troubled Asset Relief Program, or TARP**. **But administration officials believe that trillions of dollars more may be needed to buy the majority of bad assets from banks. "The size of the problem is so large that no one knows if you just wiped out all the assets, how much it would cost," said Senator Charles E. Schumer, Democrat of New York and vice chairman of the Joint Economic Committee. He added that a number of officials estimate it may take up to $3 trillion to $4 trillion to buy the bad assets**.

Federal officials are trying to find a delicate balance between stabilizing banks and **keeping the nation's finances steady**. Mr. Summers privately expressed concern last week that spending too much to buy bad assets could cripple the dollar, according to a person who spoke with him.

Administration officials are also worried that lawmakers might reject the high price tag. At the same time, **spending too little may not provide enough to plug the deepening hole**. “None of the solutions are very easy,” Mr. Schumer said. “All of these proposals sound very appealing until you start to examine them in detail. And then you find that all of them have problems. The good bank-bad bank idea — the problem, first and foremost, is how do you value the assets? No one knows how to do that.”

Lawmakers have complained that the $350 billion already spent under TARP has failed to prevent institutions from continuing to decline. On Wednesday, several senior members of Congress, including Christopher J. Dodd, chairman of the Senate Banking Committee, and Barney Frank, chairman of the House Financial Services Committee, urged the administration to detail swiftly how it will run the assets program.

Administration officials have been moving with some caution. They say that they hope to avoid the spectacle of the last administration, which lurched from policy to policy, and in the process lost some credibility in Congress.

Senior officials including Ben S. Bernanke, the chairman of the Federal Reserve, and Ms. Bair have recommended that the new administration consider a **so-called aggregator bank that would relieve banks of their worst assets.** Such a move, they contend, would **restore investor confidence in the banks and encourage investors to provide them with fresh capital**. One version of the plan being floated by bankers would have the F.D.I.C. take the lead in running the “bad bank” and buying the toxic assets for a combination of cash and notes backed by the bad bank. In return, the government would demand **some sort of equity stake**. The banks would still be responsible for collecting payments on the loans that they sold, according to bankers briefed on the situation.

Other issues still need to be resolved, including how the government would determine what to pay for the toxic assets, which assets would qualify, and what conditions might be attached. Also under discussion was whether to require banks that dump their assets into the fund to separately raise private capital. That could put pressure on weaker banks.

Government officials are considering other ideas for stabilizing the financial system. Those include expanding the types of government guarantees given to Citigroup and Bank of America to cover more assets at more financial companies. Another idea is to pour even more federal money into the banks, possibly in return for common stock.

In a sense the debate over creation of an aggregator bank or nationalization is really a discussion over how much to expand policies begun during the Bush administration, officials said on Wednesday. **The government in effect has already nationalized several large institutions, including the American International Group, Fannie Mae and Freddie Mac, when it seized control**. And it has taken the same steps as creating a bad bank when it took $29 billion in assets held by Bear Stearns and guaranteed more than $300 billion in declining assets at Citigroup.

Officials said the debate within the administration was over how much and under what terms to extend those programs to other institutions. Compounding the complexity is the fact that the administration is simultaneously asking for a stimulus package of more than $800 billion.

Moreover, as the excesses of Wall Street — from expensive corporate jets at Citigroup to huge bonuses and extravagant renovations at Merrill Lynch — ring through Capitol Hill, the idea of a large bailout that does not penalize shareholders and senior executives becomes a tough sell.

The concept of a bad bank has gained momentum in the financial industry as the economy deteriorates, slashing the value of risky assets on banks' books and increasing the need for banks to hold capital against those losses. **Shares in Citigroup and Bank of America, which both recently received a second taxpayer lifeline, surged 19 percent and 14 percent respectively as the stock market rose on optimism that the administration would relieve banks of money-losing assets.**

The Fed said Wednesday the economy remained gloomy, and vowed to use "all available tools to promote the resumption of sustainable economic growth and to preserve price stability." Its Federal Open Market Committee voted to keep the federal funds target rate at zero to 0.25 percent. Analysts estimated that the economy contracted by more than 5 percent in the fourth quarter, one of the sharpest quarterly drops in decades. Employers eliminated two million jobs from September through December.

In the past, the Fed has tried to steer the overall economy almost entirely through the federal funds rate, the rate that banks charge each other to lend overnight reserves. But because banks remained reluctant to lend, even after the Fed lowered the overnight rate time after time, the central bank began creating new programs last fall in which it stepped in as a lender itself.

To push down interest rates on mortgages, the Fed began a program this month to buy $500 billion in mortgage-backed securities issued by Fannie Mae, Freddie Mac and the federal agencies. Buying large volumes of a security pushes up its price in the market, which leads to lower yields or interest rates. Thus far, the **Fed has bought about $53 billion** of the securities. But rates for the kind of traditional mortgages that Fannie and Freddie guarantee dropped sharply and stayed low as soon as the Fed announced plans for the program in late November. The committee also served notice that it might purchase longer-term Treasury bonds, a move that would drive down long-term interest rates of all types.

In the next several weeks, the Fed expects to start a $200 billion program to finance securities backed by consumer loans, including car loans and credit card debt. This month, the Fed started a program to buy $500 billion in mortgage-backed securities.

Wednesday's policy vote was not unanimous. Jeffrey M. Lacker, president of the Federal Reserve Bank of Richmond, in Virginia, voted against the decision.

Help for Credit Unions: The United States agreed to inject $1 billion of new capital and provide backing for corporate credit unions facing mounting losses on their investments in mortgages, a federal agency said.

The agency, the National Credit Union Administration, said on Wednesday it would guarantee uninsured lender assets through next month and set up a voluntary program through 2010. The U.S. Central Corporate Federal Credit Union will get a $1 billion federal injection that will raise the public's confidence in credit unions, the lender said.

(emphasis added)

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