Simmering Public Fury regarding the Bank Bailout: Judgment Day for Geithner

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Whether he deserves it or not, Timothy Geithner has become the poster boy for everything that's wrong with the government's scatterbrain financial rescue plan. Geithner was in the wheelhouse at the New York Fed when Bear Stearns and Lehman Bros defaulted, and he played a central role in the $165 million AIG bonus scandal which ignited a populist firestorm across the country. Now everything even remotely connected to the bank bailout has become a source of fist-clinching rage. The mood of the country has darkened from the steady downpour of bad economic news, the sharp decline in housing prices and the steep rise in unemployment. People are angry at the government, the banks and Wall Street. Their nerves are frayed and their patience is stretched to the limit.

It is in this atmosphere of simmering public fury that Geithner will announce the details of his long-awaited plan for removing up to $1 trillion of toxic assets from the balance sheets of some of the country's biggest banks. Information about Geithner's "Public-Private Partnership" and the so called Term Asset-Backed Securities Loan Facility (TALF) has been spotty so far, but enough is known about the plan to predict that it will likely be the noose into which Geithner thrusts his scrawny neck bringing his dismal career at Treasury to a end. The country will not endure another pretentious-sounding banker-friendly flim flam, which is precisely what Geithner has in mind.

According to the Associated Press:

"Officials said Geithner's plan will have three major parts. One part will be an effort Geithner spoke about last month – the creation of a public-private partnership to back purchases of bad assets by private investors… Treasury will hire four or five investment management firms, matching the private money that each of the firms puts up with government funds.

A second part of the plan will expand a recently launched program being run by the Federal Reserve called the Term Asset-Backed Securities Loan Facility, or TALF.

That program is providing loans for investors to buy assets backed by consumer debt in an effort to make it easier for consumers to get auto, student and credit card loans. Under Geithner's proposal, this program would be expanded to support investors' purchases of banks' toxic assets.

The third part of the Geithner plan would utilize the resources of the FDIC, the agency that guarantees bank deposits, to purchase toxic assets. Officials said that the FDIC will create special purpose investment partnerships and then lend those partnerships money so that they can buy up troubled assets." (AP)

Why in heaven's name would Shiela Bair attach her good name to Treasury's latest bunko-scam? As Bair undoubtedly knows, the main objective of the Public-Private Partnership and TALF is to provide inflated prices for garbage assets that investors refuse to buy. It's just a way of transferring losses from the banks to the taxpayer by using a middleman who looks like a partner but only has a 5 percent stake in the game. This is "tax cheat" Timmy's circuitous way of socking it to the public one more time. Here's how Yves Smith at Naked Capitalism explains it:

"First, the banks, as in normal auctions, will presumably set a reserve price equal to the value of the assets on their books. If the price does not meet the reserve (and the level of the reserve is not disclosed to the bidders), there is no sale; in this case, the bank would keep the toxic instruments.

Having the banks realize a price at least equal to the value they hold it at on their books is a boundary condition. If the banks sell the assets as a lower level, it will result in a loss, which is a direct hit to equity. The whole point of this exercise is to get rid of the bad paper without further impairing the banks."

Okay, so the auctions are rigged and the banks get overpaid for toxic waste. Surprised? Geithner's task from Day 1 has been to keep the money flowing from the vault at Treasury to the big banks. This is just more of the same. The TALF and the PPP are just clever acronyms meaning "corporate welfare" which is ladled out to bank tycoons who have their agents working the levers from the inside. The public, of course, takes it in the shorts once again.

Yves Smith puts it like this:

"Dear God, the Administration really thinks the public is full of idiots. But there are so many components to the program, and a lot of moving parts in each, they no doubt expect everyone's eyes to glaze over." (Public Private partnership emerging, Yves Smith, Naked Capitalism)

Geithner has been trying for weeks to lure hedge funds and private equity firms into participating in his program offering up to 95 percent leverage for the purchase of the banks bad assets. By providing loan guarantees rather than capital, Geithner can (in the words of the Wall Street Journal's David Wessel) "rely on the Federal Reserve's amazing ability to come up with unlimited sums without congressional consent." This means that Geithner has moved on to Plan B which makes good use of Bernanke's deep pockets and well-oiled printing press.

Geithner's strategy is nothing more than a trillion dollar stealth bailout of the country's biggest banks. The funding from the TALF and PPP are just the first part of a one-two knockout punch. Treasury will try to show that it paid less for the assets than their current book-value (which, of course, is grossly inflated) and then follow up with generous capital injections from the TARP program to make up the difference. That way, the banks will be "made whole" again while the public gets the double whammy. Geithner is hoping that the public relations hype surrounding the program will allow him to carry out his strategy before anyone figures out what's really going on. Fortunately, the blogosphere is following every little detail, which means that the plan will be picked apart just minutes after it is released. If the punditocracy gives it the "thumbs down", there's a good chance that Geithner will have to pack it in and resign. His credibility was wobbly to begin with. A failure here would surely be the last straw. Senator Richard Shelby, voiced the concerns of many elected representatives when he said on FOX News Sunday, that Geithner was on “shaky ground” and that “If he keeps going down this road, he won’t last long.” By late Monday, we should know whether Geithner will continue to serve at Treasury or hobble back to his dingy rookery at Kissinger and Associates.

According to the New York Times:

“The Federal Deposit Insurance Corporation will set up special-purpose investment partnerships and lend about 85 percent of the money that those partnerships will need to buy up troubled assets that banks want to sell.

… Private investors, then, would be contributing as little as 3 percent of the equity, and the government as much as 97 percent.”

The idea that 97 percent “low interest” funding constitutes a “partnership”, boggles the mind. Where can a businessman or a homeowner get gravy a deal like that? The Treasury is providing a subsidy to Wall Street crooksters to manage taxpayer money so they can fatten their own bottom line. It’s that simple. Geithner’s not only willing to empty the public purse for his buddies but, also, write another trillion dollar check on an account that is already overdrawn by $11 trillion. This is one gigantic looting operation concocted by bank lobbyists masquerading as public officials.

The whole purpose of the Geithner shakedown is to mislead the public. Why should the perilously underfunded FDIC provide a non-recourse loans to hedge fund sharpies and PE scalawags when its primary responsibility is to protect bank depositors? And why are they setting up more of the same Enron-type “off-balance sheets” special purpose vehicles which blew up the financial markets to begin with? This has disaster written all over it. The non recourse loans create a “no lose” situation for investors who can dump any type of crappy mortgage-backed sludge into the program and not worry about any legal backlash. Here’s how Paul Krugman sums it up on Saturday’s blog:

“The Geithner plan has now been leaked in detail. It’s exactly the plan that was widely analyzed — and found wanting — a couple of weeks ago. The zombie ideas have won.

The Obama administration is now completely wedded to the idea that there’s nothing fundamentally wrong with the financial system — that what we’re facing is the equivalent of a run on an essentially sound bank. As Tim Duy put it, there are no bad assets, only misunderstood assets. And if we get investors to understand that toxic waste is really, truly worth much more than anyone is willing to pay for it, all our problems will be solved.

To this end the plan proposes to create funds in which private investors put in a small amount of their own money, and in return get large, non-recourse loans from the taxpayer, with which to buy bad — I mean misunderstood — assets. This is supposed to lead to fair prices because the funds will engage in competitive bidding….

This plan will produce big gains for banks that didn’t actually need any help; it will, however, do little to reassure the public about banks that are seriously undercapitalized. And I fear that when the plan fails, as it almost surely will, the administration will have shot its bolt: it won’t be able to come back to Congress for a plan that might actually work.” (Paul

Krugman's blog)

Geithner's plan is a catastrophe. It's just a sloppy remake of Paulson's failed Super SIV that was supposed to save Citi from massive losses but closed without a single sale. Not one investor stepped forward to buy assets even though Paulson slapped the Treasury's seal of approval on entire operation. It was a complete bust. Now Geithner is following in the ex-Treasury Secretary's footsteps.

The banks are not going to fix themselves. Only government can do that, which means that someone will have to fill the leadership void and do the heavy lifting. But time is running out and the problems are getting worse. Public support is on the wane. Obama should take advantage of what little confidence in the system is left and take radical corrective action. Insolvent financial institutions have to be taken into receivership and liquidated. Shareholders and bondholders will have to take a haircut. And Geithner, Summers and the rest of the White House banking fraternity will have to resign or be fired. Obama should mull over Albert Einstein's sage advice when he said, "The problems we face today cannot be solved by the minds that created them."