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Chase Manhattan Joins Citicorp

by LADB Staff

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On May 27, Chase Manhattan Corp. followed Citicorp's lead in acknowledging that many of its Third World loans are uncollectible. The New York-based bank holding company, the third largest in the United States, said that in the second quarter it would set aside $1.6 billion for losses on loans to developing countries, causing a $1.4 billion quarterly loss and a $850 million loss for 1987. According to the NEW YORK TIMES (05/28/87), the action will wipe out roughly 28% of Chase's shareholders equity, which on March 31 totaled $5 billion. More important is the effect that Chase's action will have on other giant lenders in particular, such institutions as the BankAmerica Corp. and the Manufacturers Hanover Corp. Analysts agreed that in the wake of Chase's decision, the pressure on BankAmerica and Manufacturers Hanover to set aside comparable reserves for their loan losses had become even greater. The longer those banks hold out, the analysts said, the more worried the financial markets will become as to why they have not acted.

"Now that Citi and Chase have moved, it creates a whole different ball game," said Livia Asher, the banking analyst at Wall Street's Fox Pitt Kelton. "Once two major banks do it, it is a lot harder to justify not doing it. If they don't it, the stock market will reflect the difference." On Wednesday Manufacturers Hanover in New York released this statement: "As we said last week, the matter is under careful study." In San Francisco, BankAmerica said there was "no change" from its earlier position, which is that the bank holding company is adequately reserved. In a previous interview, however, BankAmerica's chief executive, A.W. Clausen, suggested the possibility that reserves could be built if the whole industry followed that route or if regulators insisted.

Analysts have been calculating estimates of the impact that a move comparable to Citicorp's or Chase's would have on BankAmerica and Manufacturers Hanover. According to Ms. Asher's estimates, Manufacturers Hanover would have to add $2 billion to its loan-loss reserve, producing a 1987 loss of $800 million and wiping out roughly one-third of the bank's year-end net worth of $3.8 billion. For BankAmerica, she estimates, the addition to reserves would have to be $2 billion. That would produce a 1987 loss of about $1.7 billion and would cut the bank's net worth by more than half, to less than $2 billion. Both banks might then be forced to raise capital by selling common stock, thus diluting the value of their shareholders' existing investment. The banks face a type of dilemma: If they fail to set aside reserves, the stock market could penalize them now; if they take action, the market could penalize them later for the weaker earnings per share that might follow a public offering of more shares.

Chase said its move reflected several factors: Brazil's decision this year to suspend payments on much of its foreign debt; the rising protectionist sentiment in Congress, which presumably would hurt the ability of debtor countries to export goods; Citicorp's action on May 19, and a desire to get the problem of Third World debt behind it. Even though Chase will suffer an estimated $950 million yearly loss, it will be able to reduce the final loss to $850 million by selling some of its assets at a $100 million after-tax gain. "There has been a negative perception overhanging the New York banks,"
said Willard C. Butcher, Chase's chairman and chief executive. "If we can get that thing behind us, the real performance of the institutions can show through." Butcher warned debtor countries not to try to take advantage of the banks' move by demanding debt forgiveness. According to this line of reasoning, now that the banks have suffered an earnings setback, they are able to forget about their bad loans. Butcher indicated that Chase would not tolerate such an attitude.

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