European leaders leaning on banks in bid to encourage lending

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Given the intimacy of French society, especially at the top of the pyramid of political and financial power, Sarkozy's move was more than a polite request. Within days, the chief executives of the top six French banks committed themselves to increase their lending volume by 4 percent in 2009, or €75 billion, the equivalent of $97.4 billion, in return for €10.5 billion in loans from the state.

To support lending, European governments have come up with at least three models.

In Britain, faced with an American-style crisis and the bursting of a housing bubble, the government has veered away from its previous free-market rhetoric and is taking large equity positions in some banks, semi-nationalizing them and dictating some bank policies.

In France, where the banks are in better shape, the government is providing guarantees but taking no equity.

And in Germany, the government's plan has come down somewhere between the two others, combining penalties for banks with a few incentives to lend. The Berlin model is considered, for now, least effective, partly because it has become so politicized.

But the process of leaning on the banks to lend is becoming politicized everywhere. Politicians who initially focused on the more technical issue of unfreezing the interbank lending market are scrambling to respond to a worsening economic slowdown, and they are making the caution of the banks a further symbol of plutocratic selfishness.

"This is more about politics than about finance," said Philippe Waechter, chief economist at Natixis Asset Management.

"In the beginning the question was really about the monetary markets," he said. Now "politicians are trying to look like they're in charge."

Across Europe, serious lending is only beginning to resume.

"It's working very disappointingly slowly," said Thomas Mayer, the chief European economist at Deutsche Bank. "Perhaps it's because each country has a slightly different system, and no one knows what it means."

Even the French banks are taking their time. Last Thursday, Sarkozy warned the bank chiefs again — this time, publicly — to get moving and not choke off credit to consumers and businesses.

Sarkozy said that a new "credit mediator," René Ricol, might go public with "examples of unacceptable restrictions on credit," warning that "people will then compare who does his job and who does not."

His prime minister, François Fillon, was even more explicit in a television interview. "If the banks don't do their job," Fillon said, the government would not exclude "taking a stake and maybe changing the management."

A Sarkozy aide said, "The president was very clear: if the banks don't play the game, he'll use the atomic bomb."

Discounting the hyperbole, Sarkozy may yet have to use at least a conventional weapon. After increasing lending by 10 percent this year through August, even a 4 percent increase for 2009 can seem a lot to banks wanting to protect themselves against further losses in the face of an economic slowdown and the quickening pace of bankruptcies.

The French model, as officials describe it, is much less interventionist than the country's reputation for nationalization or even Sarkozy's own rhetoric. In general, French banks are in reasonable shape. They are largely consumer banks and have conservative requirements for mortgages and loans. Credit cards are rare; most French consumers rely on debit cards, with balances deducted as they take place or automatically at the end of the month.

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So there was no real need here to partly nationalize the banks, putting the full force of the government behind them, as Britain did with several of its big banks. And bank heads were intimately involved in drawing up the plan, in particular Baudouin Prot, chief executive of BNP Paribas, the largest French bank, and Philippe Dupont, head of Banque Populaire, the biggest lender to small business.

So far France has stayed away from trying to dictate banks' dividends, salaries or bonuses. A first €5 billion in guarantees has been approved, with another €5 billion expected soon.

The banks themselves had initially been reluctant to accept any state money. Frédéric Oudéa, the chief executive officer of Société Générale, was among those declaring publicly that his bank needed no new capital.

But the government insisted that all of them take part.

"We had to force them a bit," said one senior presidential adviser.

"It wasn't that hard," he added. "Today none of them has an interest to fall out of favor with the government."

Prime Minister Gordon Brown of Britain has been given credit for pointing the way for Europe and America, too, by injecting state capital directly into the banks.

But Brown, previously known for pushing the Labour Party toward more free market views, had little choice, with British banks deeply affected by the American crisis and in largely the same ways.

The United States and Britain had the kind of investment banks, mortgage banks, little or no down payments and interest-only loans that the Continent largely shunned.

Britain was driven to a more activist approach. The government acquired controlling stakes in the Royal Bank of Scotland and the soon to be combined Lloyds TSB and HBOS in exchange for a $64 billion capital infusion.

Brown announced limits on bonuses paid by the banks in which the government would have a stake, a stop to the payment of dividends and a return to 2007 levels of lending to small businesses. The government could, if required, mandate lending.

These were tough terms, but failing British banks had little choice but to accept them. The British package, in coordination with the Bank of England, totals about £500 billion, or $801.4 billion, in emergency loans, capital injections and lending guarantees.

The British chancellor of the Exchequer, Alistair Darling, summoned top banking executives in October to persuade them to reduce borrowing costs for smaller businesses.

But so far small businesses complain that these costly capital injections have done little to help their access to credit. In an editorial Friday, The Financial Times newspaper in Britain said that "there are no easy options for the government" to restore lending.

"Bullying will make little difference," the paper wrote. The government could effectively complete the nationalization of banks and order them to lend, taking both credit decisions and risk. "That may yet be necessary," the paper added, "but only a hopeless optimist would expect that story to end happily."

Whatever its drawbacks, Britain's plan seems to be working better than Germany's, economists say.

In Berlin, the process has already become deeply politicized in the bitter, pre-election fight between the rivals of the current "grand coalition": the Christian Democrats of Chancellor Angela Merkel and the Social Democrats, who run the Finance Ministry under Peer Steinbrück.

Steinbrück, who at first blamed the entire problem on the Americans, rejected an idea for a European-wide capital fund.

After being required to rescue Hypo Real Estate, a leading German real estate lender, Steinbrück then criticized banks and bankers in class-warfare terms and said that the government would now impose harsh conditions on them — not to help the bankers, who he promised to punish for their misdeeds, but to aid ordinary people.

"When you politicize and stigmatize a package to such an extent, you risk pushing people away," a senior West European diplomat said.

Germany announced a €500 billion package consisting mostly of loan guarantees, with the government offering €80 billion for direct capital injections into banks and to buy illiquid assets. In addition, the government is offering €400 billion in guarantees for interbank loans, and is setting aside an additional €20 billion in the budget to cover potential losses from loans.

But the price for participation is high. German banks are not allowed to pay dividends to stockholders. That could backfire, bankers say. With stock prices falling, the inability to pay dividends will send shareholders to other investments.

And unlike France, the German government wants a hand in directing bank lending and wants officials to monitor the bank boards. Germany would also oblige participating banks to cap executive pay at €500,000 a year, relinquish bonuses and abandon "risky" business.

Given the stigma, German banks have been slow to participate in a plan that does not compel them to join or provide much reason to do so — with the obvious exception of Hypo, which is getting €15 billion in return for a state-guaranteed bond. The package will prevent banks from failing, but provides them little motivation to lend.

On Monday, Commerzbank became the first commercial lender to take the cash, some €8.2 billion, as well as government guarantees for €15 billion of new debt.

BRIEFING

Spain's jobless claims rise 7.3%, 12-year high

MADRID: The number of people filing jobless claims in Spain rose 7.3 percent last month and is now at the highest level since 1996, the government reported Tuesday.

Those claiming unemployment benefits rose by 192,658 in October to 2.8 million. The government said the jobless rate, measured by a different survey, stood at 11.3 percent, the highest among the 27 countries in the European Union. The EU expects Spain to fall into recession this year. *(AP)*

■ **HUNGARY** received the backing of European Union finance ministers for a loan of €6.5 billion, or $8.4 billion, to cope with the global financial crisis. The loan is part of a €20 billion package with contributions from the International Monetary Fund and the World Bank to shore up the Hungarian economy. *(Bloomberg)*

■ **BANKRUPTCY FILINGS** by Americans rose 40 percent in October as home values sank and individual debt grew, the American Bankruptcy Institute said. Americans have filed more than 880,000 bankruptcy petitions this year, eclipsing 822,000, the total for all of 2007. *(Reuters)*

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