

Will the Fall of an Aussie Bank Rock Wall Street? Apocalypse Down Under

By [Mike Whitney](#)

Global Research, July 30, 2008

Counterpunch.org 30 July 2008

Region: [Oceania](#)

Theme: [Global Economy](#)

Monday's trading on the New York Stock Exchange (NYSE) was a real humdinger. It started off with the White House announcing that this year's fiscal deficit would soar to a new record of nearly \$500 billion. That was followed by news of rising oil prices, weak quarterly earnings and a slowdown in consumer spending. By mid-morning the markets were in full retreat. That's when investment giant Merrill Lynch announced that it would notch a \$4.6 billion second-quarter loss and write-downs of \$9.4 billion on collateralized debt obligations (CDOs) and other mortgage-related assets. Stocks quickly went verticle and the rout was on. By the closing bell the Dow was down 240 points. Traders staggered from floor of the exchange slumped-over and bedraggled, looking like they just got a missive from the draft board.

And, yet, on Tuesday, the market staged a valiant comeback, surging 260 points in a matter of hours. It was enough to give the fund managers a bit of a lift and hope that things are finally turning around. But the market's woes are far from over. The International Monetary Fund summed it up in warning they issued earlier in the week:

"Global financial markets are 'fragile' and indicators of systemic risk remain 'elevated'...Credit quality 'across many loan classes has begun to deteriorate with declining house prices and slowing economic growth.' Bank balance sheets are under 'renewed stress' and the decline in bank share prices has made it more difficult to raise new capital. (There is an) 'increased likelihood of a negative interaction between banking system adjustment and the real economy.' (Financial Times)

The IMF also stuck by its earlier prediction that total losses to financial institutions from the credit crisis would reach \$1 trillion (\$945 billion) a sum that will have savage consequences for industry, consumers and the global economy.

Over at Nouriel Roubini's blog, Dr. Doom made this observation about the Merrill Lynch's troubles:

"Merrill Lynch's decision to 'sell' a good chunk of its remaining CDOs at 22 cents to the dollar has been widely praised as the firm finally recognizing the full extent of its losses on these toxic instruments. This batch of \$30.6 billion of CDOs was already marked down to \$11.1 billion. Now with the 'sale' of it to Lone Star at a price of \$6.7 billion Merrill Lynch is taking another \$4.4 billion write-down and 'selling' it at 22% of the original face value. But is this a market-based 'sale'? No way, calling this transaction a 'sale' is a joke." (Nouriel Roubini's Global EconoMonitor)

Indeed. This isn't a "sale"; it's more like abandoning a sinking ship. The investment chieftains are getting scorched by their downgraded assets and have started dumping them at any cost. There's no market for mortgage-backed anything now, and there won't be until housing finds a bottom.

The Merrill Lynch deal illustrates just how crazy things have gotten. Merrill said it "will provide financing to the purchaser for approximately 75 per cent of the purchase price." Whoa. In other words, the banks are so anxious to off-load their junk-paper, they're almost paying people to take it off their hands. Now that's desperation! The problems haunting the financial markets have cross-pollinated with the real economy and are spreading misery everywhere. Unemployment is rising, growth is slowing, inflation is up, the dollar is down. We've heard it many times before, but it's still jarring to see General Motors stock fall below Bed & Bath, or Starbucks shut down 600 stores, or million dollar McMansions sell for \$425,000.

Now that the working stiff is maxed out on his mortgage, worried about losing his job, and trying to keep food on the table; the least congress can do is scatter the oil speculators; right?

Wrong. On Monday, the Financial Times reported that: "A US Senate proposal designed to curb speculation and increase transparency in the energy markets was blocked by Republican legislators on Friday. The move frustrates Democratic efforts to show the party is taking action on record petrol prices. The Stop Excessive Speculation Act, sponsored by Harry Reid, the Senate majority leader, fell 10 votes short of clearing a procedural hurdle."

The scariest news of the week comes from down-under, where the National Australia Bank (NAB) announced it would "slash a £400m bond sale by two thirds. The retreat comes days after the Melbourne lender shocked the markets by announcing a 90pc write-down on its £550m holdings of US mortgage debt, an admission that its AAA-rated securities are virtually worthless....The decision by National Australia Bank to make drastic provisions on its US mortgage debt could have ramifications in the US itself. It opted for a 100pc write-off on a clutch of "senior strips" of collateralized debt obligations (CDO) worth £450m - even though they were all rated AAA. (Ambrose Evans Pritchard, "Australia faces worse crisis than America", UK Telegraph)

The original article appeared in the Business Spectator and was titled "NAB will shock Wall Street", by Robert Gottlieb. "Shock" is an understatement. This is more like a meat cleaver crashing down on a butcher block. Schwook! This is a must-read for anyone who is following the meltdown in the financial markets. Here is an extended excerpt from Gottlieb's article:

"The National Australia Bank's decision to write off 90 per cent of its US conduit loans will have dramatic repercussions around the world. Wall Street will be deeply shocked when they understand the repercussions of what NAB has done. It is clear global banks have nowhere near provided for their exposures to US housing loans which in the words of John Stewart are experiencing a 'meltdown'.

"We are now way beyond sub-prime. NAB says that it is suffering a 55 per cent loss on American housing loans - an event that has never happened in the history of a developed country in recent memory. This is an unprecedented event and means that the cost of bailing out the US financial system is now far

beyond the highest estimates. A US recession is now locked in, but more alarmingly, 55 per cent loan losses point to the possibility of a depression.

“It means the cost of bailing out housing exposures to the two mortgage insurers will be so great that it will leave no room to bail out anything else and there are several US banks that are now in big trouble. NAB says that the dislocation in the residential market is separate from the corporate market, but the flow on is inevitable.” (The Business Spectator, “NAB will shock Wall Street”)

The conduits are off-balance sheets operations run by the banks which contain hundreds of billions of dollars of bonds which are now essentially worthless. So far, many of the banks have not accurately reported the losses from these operations hoping that the housing market will stabilize and the value of the bonds will rebound. The action taken by the National Australia Bank is a “game-changer”.

Gottliebsen again:

“The global banks have been marking to market the assets they held on their balance sheet, but the vast amounts held in so called ‘conduit trust accounts’ have not been written down because they were not marketable. NAB wrote them down when they saw the bad mortgages....US banks have written down \$450 billion in bad housing loans. The revelation from NAB means that they will now certainly need to take provisions to \$1,000 billion. But write-downs of \$1,300 billion and perhaps even more are on the cards.”(Business Spectator.)

Mike Whitney lives in Washington state. He can be reached at: fergiwhitney@msn.com

The original source of this article is Counterpunch.org
Copyright © [Mike Whitney](http://Counterpunch.org), Counterpunch.org, 2008

[Comment on Global Research Articles on our Facebook page](#)

[Become a Member of Global Research](#)

Articles by: [Mike Whitney](#)

Disclaimer: The contents of this article are of sole responsibility of the author(s). The Centre for Research on Globalization will not be responsible for any inaccurate or incorrect statement in this article. The Centre of Research on Globalization grants permission to cross-post Global Research articles on community internet sites as long the source and copyright are acknowledged together with a hyperlink to the original Global Research article. For publication of Global Research articles in print or other forms including commercial internet sites, contact: publications@globalresearch.ca
www.globalresearch.ca contains copyrighted material the use of which has not always been specifically authorized by the copyright owner. We are making such material available to our readers under the provisions of "fair use" in an effort to advance a better understanding of political, economic and social issues. The material on this site is distributed without profit to those who have expressed a prior interest in receiving it for research and educational purposes. If you wish to use copyrighted material for purposes other than "fair use" you must request permission from the copyright owner.

For media inquiries: publications@globalresearch.ca