Financial Crises, Real and Imagined

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Director, Asia Times Holdings
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Issuance of CDO’s

Financial Crises, Real and Imagined
Banks’ ROE Reaches New Normal
Levering the Levered Leverage: Take highly-levered obligations, put them in a levered structure, and let the banks buy it with 1.6% capital cover (20% of 8%). Then you lever the collateral.

“What's the point of skimming if we're being skimmed? Defeats the whole purpose of what we're doin' out there.”

Guess where Lehman invested the collateral?
Bubble Math

1. Banks target ROE of 18%-20%
2. True AAA’s swapped into floating rates pay less than banks’ cost of funds
3. Banks construct synthetic AAA’s with the connivance of rating agencies to pay LIBOR +30 basis points
4. Leverage of 62.5 * 30 bps = 18.75%
Federal Funds Rate
Subprime Delinquency Rate: Not as Bad As it Sounded
AAA Bond Prices in 2009

Commercial Mortgage Backed Securities

Home Equity Backed CDO’s
China’s public debt has room to grow
Bank Credit Growth by Country

Private Credit by Deposit Money Banks and Other Financial Institutions to GDP for China
Private Credit by Deposit Money Banks and Other Financial Institutions to GDP for United States
Private Credit by Deposit Money Banks and Other Financial Institutions to GDP for Japan
Private Credit by Deposit Money Banks and Other Financial Institutions to GDP for Greece
Private Credit by Deposit Money Banks and Other Financial Institutions to GDP for Spain

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Rising Currency Correspondents to High Real Rates

Chinese RMB Real Effective Exchange Rate
China Has World’s Highest Real Interest Rates

Financial Crises, Real and Imagined
Real 5-Year Interest Rates (Inflation Trackers)
<table>
<thead>
<tr>
<th>Dec-15</th>
<th>Balance (RMB trn)</th>
<th>Default Rate</th>
<th>Recovery</th>
<th>Loss (RMB trn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mortgage</td>
<td>10.4</td>
<td>5.0%</td>
<td>90%</td>
<td>0.1</td>
</tr>
<tr>
<td>Personal</td>
<td>16.6</td>
<td>5.0%</td>
<td>70%</td>
<td>0.2</td>
</tr>
<tr>
<td>Corporate</td>
<td>68.8</td>
<td>8.0%</td>
<td>50%</td>
<td>2.8</td>
</tr>
<tr>
<td>Trust</td>
<td>16.3</td>
<td>15.0%</td>
<td>25%</td>
<td>1.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>112.1</strong></td>
<td></td>
<td></td>
<td><strong>4.9</strong></td>
</tr>
<tr>
<td>NPL ratio</td>
<td></td>
<td></td>
<td></td>
<td><strong>4.4%</strong></td>
</tr>
</tbody>
</table>
Loan Default Risk, 2700 Listed Chinese Companies

FY14 A-shares Interest Coverage

Source: Bloomberg, REORIENT
Risky Proportion of Chinese Firms

Universe: No. of companies, Amt. of Debt

1H15 A-shares Debt Profile
Source: REORIENT

1H14 A-shares Debt Profile
Source: REORIENT

- EBITDA/Int < 1: 335 companies, RMB1.1 trn
- Debt > 2 x Cash: 206 companies (7.5%), RMB899 bn (7.6%)
- EBITDA/Int < 1: 285 companies, RMB749 bn
- Debt > 2 x Cash: 177 companies (6.8%), RMB622 bn (5.9%)
Italy vs. China NPL's

Financial Crises, Real and Imagined
Chinese Outflows Driven by Paydown of Dollar Debt

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Bank-reported capital flowed out of China in Q3 2015

Cross-border claims fall

Offshore renminbi deposits respond to CNY/USD

Onshore foreign currency loans fall

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1 A decline indicates a depreciation of the renminbi.

Sources: Central Bank of the Republic of China (Taiwan); Hong Kong Monetary Authority; Bank of Korea; Monetary Authority of Macao; Monetary Authority of Singapore; Datastream; CEIC; BIS locational banking statistics by residence.

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