April 15, 2009

Déjà vu all over again

I have, recently, been experiencing a strange sense of familiarity watching the Congressional Budget Office's (CBO) efforts to monitor the budgetary implications of the Troubled Asset Relief Program (TARP). On the one hand, the long-term costs are rising:

> "Since January, CBO has raised its estimate of the net cost (on a present-value basis) of the transactions covered by the TARP by $152 billion for 2009 and by $15 billion for 2010. Those revisions stem from three factors—changes in financial market conditions, new transactions, and a small shift in the anticipated timing of disbursements."

On the other hand, the CBO wants to book less spending in the near term than what the Treasury has in mind, for reasons that have to do with accounting procedures and the pace of actual TARP spending:

> "Budget accounting issues are clouding the deficit forecasts for this year. The above estimate of this year's deficit to date includes outlays of about $290 billion for the Troubled Asset Relief Program (TARP). Although the Treasury has been recording most spending for the TARP on a cash basis, CBO believes that the budget should record the program's activities on a net present-value basis adjusted for market risk. Using that approach, CBO estimates that outlays of $140 billion should be recorded for the TARP through March. That approach would yield an estimated deficit of $803 billion for the first half of the year."

After a few minutes of pondering why it seemed like I had seen this before, I flashed back to my early days in the Federal Reserve System and the saga of the Resolution Trust Corporation, the Congress-created vehicle that helped the country work its way through the aftermath of the 1980s savings and loan crisis. In August 1989, here's what the Congressional Budget Office was thinking:

> "The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (Public Law 101-73) is a complex measure affecting federal government taxes, premiums, spending, borrowing, and regulation. While the bill strengthens the government's system for insuring commercial banks, its primary focus lies in addressing the huge liabilities forced on the government by failed and insolvent savings and loan institutions.
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> "… The legislation establishes a new Resolution Trust Corporation (RTC) to merge or close currently insolvent insured thrifts. The RTC is to spend a total of $50 billion on this task… The $50 billion in resources available to the RTC are sufficient, in the Administration's estimate, to cover the government's liabilities for currently insolvent thrifts with $10 billion left over to help defray interest costs…"

The CBO, however, was not convinced that the RTC's resolutions would come so cheap.

> "… many observers, including CBO, doubt that this level of resources is enough."

And in January 1990, the CBO was unhappy with the Treasury's accounting procedures:

> "Last year's Financial Institutions Reform, Recovery, and Enforcement Act effectively excluded about $30 billion of deposit insurance spending from budget totals in 1990 and 1991, by having the funds borrowed through a newly chartered, government-sponsored enterprise, the Resolution Financing Corporation (REFCORP).
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> "REFCORP's status as a government-chartered enterprise is critical to the budgetary treatment of its borrowing. Normally, the U.S. Treasury conducts any necessary financing for the government. Treasury borrowing finances the deficit; it does not reduce the deficit. Otherwise, the budget would always be balanced. But because REFCORP is technically private, the funds that it borrows and turns over to the (on-budget) Resolution Trust Corporation count as offsetting collections. These funds offset the associated spending to resolve failed savings and loans. …
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> "CBO believes that REFCORP is a government entity, that its borrowing is government borrowing, and that the budgetary treatment that has been adopted is inappropriate."

By accounting for things the way they thought they should be accounted for, the CBO estimated as of August 1991 that the costs of the resolution process would in fact be quite a lot higher than initially assumed:

> "CBO now believes that the RTC will pay total losses of about $155 billion (in 1990 dollars) for a caseload of about 1,500 institutions."

What is more, the whole process was taking quite a bit more time than originally hoped:

> "CBO assumes that the RTC continues resolving institutions through calendar year 1994, more than two years longer than originally scheduled."

In August 1992, even that time frame was looking optimistic…

> "CBO assumes that the RTC or a successor will deal with a heavy caseload through 1998…"

But the news wasn't all bad:

> "CBO estimates the cleanup's cost at $135 billion. Sobering as this figure is, it actually represents a glimmer of good news: CBO's former estimate was about $155 billion."

Movement in the right direction notwithstanding, Congress did not exactly jump at the opportunity to extend the RTC's life span. From the January 1994 Economic and Budget Outlook:

> "The savings and loan cleanup is forging ahead after a prolonged interruption in its funding. From April 1992 until December 1993, the Resolution Trust Corporation (RTC) had only very limited authority to incur losses. It was largely confined to selling off its portfolio of assets and to resolving the occasional institution that could be closed or merged at little or no loss to the government; hence, the RTC recorded negative outlays in both 1992 and 1993.
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> "The Congress brought this drought to an end in late 1993 with the Resolution Trust Corporation Completion Act."

And when Congress eventually acted, the picture was brighter yet:

> "There is good news on the RTC front: the agency will not fulfill the gloomy predictions that were common even a year or two ago. CBO now estimates the total value of losses covered by the RTC since its inception in 1989 at about $90 billion (expressed, by convention, in 1990 dollars)."

And that is about where it ended up:

> "The total tab for the RTC lies somewhere between the sunniest and gloomiest projections made during its early years. CBO now estimates the total value of losses covered by the RTC and its successor through 2000 at about $90 billion (expressed, by convention, in 1990 dollars). …
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> "Four and a half years ago, CBO feared that the RTC's costs alone could be as high as $185 billion, and some outside experts were even more pessimistic. (The Bush Administration, in contrast, originally stated that $50 billion would be sufficient.)"

So there you have it. The last great experiment in working through financial crisis took longer than expected, involved some accounting pushing and shoving at the outset, confronted a skeptical Congress, and cost more than initially projected, but quite a lot less than feared.

Make of it what you will.

By David Altig, senior vice president and research director at the Atlanta Fed

April 15, 2009 in Banking, Financial System | Permalink