



Bank Nationalization: A Debate

William R. Cline and Simon Johnson debate the pros and cons of bank nationalization.

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Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics. Today's session of Peterson Perspectives will be with both William Cline and Simon Johnson, senior fellows at the Peterson Institute, who have different perspectives on the issue of bank nationalization. I thought we could benefit from hearing a discussion between them.

Simon, what is meant by bank nationalization?

Simon Johnson: Well, I think, Steve, different people use that term to mean very different things. The issue to my mind in the United States right now is whether you should have an FDIC-type takeover or bankruptcy procedure, if you like, managed by the FDIC for major US banks. Obviously, the FDIC does this for smaller banks on a routine basis. Now, this kind of FDIC takeover is, I think, what people are referring to in many contexts as nationalization. And some people think it's a bad idea. Some people think the FDIC would not be able to handle this and there are other ways to proceed with regard to any big banks that may be technically or otherwise deemed insolvent.

Steve Weisman: Just to clarify: When you say "takeover," does that mean that the government purchases the shares, whatever they're worth, or seizes them in some place, and takes them over? What's the procedure in which that happens?

Simon Johnson: Well, the determination by the regulator—which sometimes is the FDIC, sometimes the FDIC working with, for example, the state regular or one of the federal regulators—that certain banks don't have enough capital on a forward-looking basis in order to stay in business, and the regulator has the right to, at that point, declare that you're no longer in business. So, you're taken over and managed by the FDIC. Ordinarily, at least for smaller banks, the FDIC tries to sell off parts of the bank's operations. For example, the deposits of the bank, the retail deposits that are insured by the FDIC, are often sold off to another bank, perhaps immediately. So, the FDIC tries to not actually run a bank. At least that's the traditional model. But they manage the winding down of the bank. They're the official receiver, if you want to use a slightly technical term.

Steve Weisman: In your judgment, the federal government—whether the FDIC or regulators or other entities—should move more assertively in taking over banks at present. Let's talk about the context. There are 8,000 banks in the United States. But the

federal government has its eye on the 19 biggest banks, on which they are now conducting “stress tests,” as they put it. In your judgment, roughly how many of these banks are candidates for being taken over, without mentioning any names?

Simon Johnson:

I have no idea, Steve, and I don't think that's a terribly important issue right now. By the way, federal and state government has its eye on all banks all the time. The banks are very carefully scrutinized and I think everyone feels they've done a good job on small and medium-sized banks in terms of determining when they've run out of capital, when they're going to run out of capital, and when they're unable to replenish their capital sufficiently and rapidly through the usual private-sector means. So, the issue is the management or the oversight of the largest banks. There the government has the right approach in setting up a stress test in which they would ascertain which banks need more capital and presumably would be given the option of raising that amount of capital privately.

My issue is just that the stress test seems to be too mild, particularly in the “stress” scenario that's been announced. We know the general microeconomic parameter is pretty optimistic, in my view, given what's happening around the world. But I think the stress test, when you do it for all the banks, you do it quickly and you make a pretty tough determination and then you give the banks the chance to raise capital privately, again, moving quite quickly, moving over a one- or two-month horizon. If they can't raise it privately, then the government steps in with the recapitalization program. That would involve, obviously, government ownership of a substantial fraction of common equity.

Steve Weisman:

A number of people, perhaps surprisingly even Alan Greenspan and Republican senators, are using the word “nationalization,” suggesting that the United States should move more aggressively in this direction. Bill, what does it mean to you and do you see any dangers in that approach?

William R. Cline:

It seems to me that hard nationalization would be ownership of well over 50 percent of the shares of the banks, number one. I do see dangers. I think that the article today or yesterday by Alan Blinder set out the case against nationalization. He emphasized the domino effect, and the management challenge. Then people talk about the wonderful experience in Sweden. But when this bank in Sweden was taken over, it was just a tiny fraction of the size of Citigroup or Bank of America, which have just hundreds of thousands of employees all across the globe. Politicization, in other words, is a major issue. The banks get in the business of doing what some senator from Iowa tells them they should do instead of what is the profitable thing to do. And Blinder added a new factor, which I haven't really thought through but it's interesting to consider, which is the confidence effect. In this country, compared to some other countries, our tradition is such that if you did have the major banks nationalized, rather than giving people a sigh of relief that, thank God, they could count on their banks, they would instead lose confidence. If you think what you would do with your funds if the government took over a major bank where you had your assets, I could see people taking them out and putting them somewhere else. It seems

to me the prior question is: What are the capital requirements? And what's necessary? What you've had here is a collapse in the stock prices at Citigroup, for example, from \$50 to a dollar. But their capital levels look robust. They have 13 percent of so-called tier-1 capital to assets. The threshold that you need is 6 percent. They now have something like 3 percent or 4 percent of tangible common equity, which is what the market likes to see. That also meets the test. It seems to me that there is a certain "guilty until proven innocent" thinking going on here; that everybody knows that this stuff isn't worth anything and therefore they should be nationalized. The point is that they've got \$800 billion of tier-1 capital; they've already recognized \$400 to \$500 billion of losses on their write-downs. They are probably going to need another \$300 billion or so of capital in the aggregate. If you look at the IMF's and Goldman Sachs' loss projections, I think there's a good a chance that they can do that certainly with the preferred shares that the government is talking about. But secondly, it's not all clear to me that this would not be the time to use a sort of cyclically adjusted capital ratio. If you're going to have a particular threshold in the best of times, then we're talking about a cyclically adjusted ratio. In sum, it seems to me that the risk you're getting into definitely is contagious and an unnecessary foray into national control. I would point out that in the 1980s, you could have made a more compelling case than today that the banks should have been nationalized. Because of the Latin American debt crisis, their debt at risk was well in excess of their capital. So, why is Paul Krugman today saying that we should nationalize the banks, and he didn't say so in the early 1980s, when he was advising the government on how to grow its way out of the problem?

Steve Weisman: Let me ask for a clarification on the stress test. Simon just said that he thinks the criteria, if I can summarize it this way, is perhaps too lenient. Do you disagree with that?

William R. Cline: Well, I'm just not sure what it means. They have been careful not to say exactly how they would interpret their stress test. One way you can interpret their stress test is that they establish how much additional capital would be needed under certain circumstances. I do not interpret it, therefore, as that they're going to immediately insist on that additional capital. I interpret it as equally consistent with waiting and seeing if things look like they're getting that bad, then down the road, there will be a need for more capital. I continue to think that the most likely scenario is that this is something like the 1982 recession. And that's in their main case, that's not even their stress test.

Steve Weisman: Simon, what about this issue of the politicization of lending. There was even a story in the paper today about the TARP funds, where some members of Congress were complaining that the banks that had received these funds were making loans to businesses that were politically in bad odor among some in Congress. Shouldn't Americans be worried that some kind of nationalization would lead to political criteria in their lending?

Simon Johnson: Steve, politically directed credit—obviously what you're talking about—is a terrible problem wherever we see it in the world. If you look at how the

financial system of Ukraine or Pakistan or Indonesia operates, and how it goes bad periodically, it's very much about politicians telling banks to whom to loan and on what terms. What is the reality today? What is the situation in the US banking system right now? It's this enormous amount of political control. The credit system—not the banks perhaps but the credit system—was substantially nationalized in September, October, November by the actions of Mr. Paulson, secretary of the treasury, and his associates, particularly Mr. Bernanke, the chairman of the Federal Reserve.

So, we have a lot of political influence, a lot political control. We have compensation caps on executives, which you may be for or against, but those are definitely a form of political control. We have a lot of pressure from Congress to get the money out the door—get the money on the streets, I believe is the expression—again, political control. I'm not in favor of government control in the bank system—that is something I've worked against and helped people unwind over the past 15 to 20 years in different countries. I'm in favor of privatization of the banking system, the privatization of the credit system.

Right now, the whole credit system is held up by the Fed, with massive lines of credit of recapitalization money, which was put into banks, certainly in terms of Citigroup and Bank of America at their request most recently. I think it's a terrible arrangement. I think muddling through will just give you more and more of the exact same political control, political interference, and distortion of loans. I think on the current baseline, where we're heading right now, you'll have loan decisions being made that will make subprime loans look sensible and good in retrospect, okay. I think we're on the road to a very serious disaster here for exactly the reason you're identifying.

Steve Weisman: A technical question to help the listeners and readers. Does the kind of nationalization that you envision necessarily entail wiping out shareholders, and if so, is it possible that Bill's point, citing that interesting piece by Alan Blinder, that the mere talk of nationalization and wiping out shareholders is contributing to the run on bank shares in the market and a lack of confidence?

Simon Johnson: I certainly agreed that confidence is critical, and that's a point that Bill is emphasizing and Alan Blinder was making. It's certainly true that if you start to talk about nationalizing banks and if it seems at all plausible, people are going to worry much more generally about what's happening in the economy. So then you have two options, I mean, assuming that you think there is some problem in the financial system. Either you shut up completely and you allow no discussion at all, and there are totalitarian regimes where that is an appealing option. I mean, that's your choice. I wouldn't go there myself. Or you expedite dealing with the problem and you go through the stress scenario. You do an evaluation that is made sufficiently public so that people say, "Oh, OK, Bill is right," for example. That may be a conclusion and I'm totally open to this. When you look at all the numbers, and you look at the properly done stress test, you may say, "Bill Cline was absolutely right, Alan Blinder was absolutely right. These

banks have plenty of capital. They can withstand even the kind of severe global recession or slump that we now seem to be heading into. There's nothing to worry about." Then people are greatly reassured, Steve, and the confidence issue is sorted out.

Steve Weisman: But you don't think that will happen. I mean, you think that there are a number, and maybe even some of the big banks, that would have to go through this nationalization process, right?

Simon Johnson: No. That's not my position. My position, Steve, is I just don't know. I want a process to be put into place through which this information will be discovered. And I would stress, this is very important, that the information that is revealed be as public and as transparent as possible. Now, there may be some things that you can't reveal to the public. Then I would advocate, I am advocating, closed-door hearings on Capitol Hill just like you have for intelligence briefings, where you can show key senators who are skeptical of this point exactly why, for example, all the banks have sufficient capital. And if you can persuade them, just like what happens with secret intelligence briefings, then you're a long way down the road toward persuading the public.

I want a process, and I think the process should include a sensible intervention point and, if you like it, it's going back to the original point: It's a form of bankruptcy if you don't have enough capital. You're taken over by the FDIC, and in that takeover it is typically the case that shareholders lose substantially. But by the way, most of the shareholder value in these banks has already been destroyed, not by actions of the government, but by the actions of incompetent management and boards of directors who, as far as anyone can see, have not exercised the kind of supervisory role that they're supposed to perform.

Steve Weisman: Let's talk about another factor in solvency: the value of the assets of the bank and their so-called toxic assets. I wonder if you could address, at the heart of this, whether or not these toxic assets should be valued at the market value or at some other value that might make sense given their underlying ability to generate revenue down the road. Simon, why don't you answer this first? Should the stress test price these assets only at market value and should nationalization take place on this basis? Should these assets be sold at that value?

Simon Johnson: Well I think, Steve, that the most transparent way to do this is with market prices. I understand that people don't like that, and of course banks traditionally and by rule are allowed to hold some part of their assets, a part that they intend to keep for a long period of time, at book value. And this is part of what, of course, is creating the massive uncertainty, because people feel that as the banks come under pressure, they may have to sell some of those assets or try to sell them for a price that's far below the book. Now, there are different ways to do this. I think, looking at the value of the assets based on market prices, but not necessarily using that as the single determinative factor on whether or not the bank is out of business makes a lot of sense to me. Other people have different

ways of doing this, but I think more market pricing in terms of assessing the assets is going to address the confidence issue, because if you do accounting tricks, or if you do things that aren't fully understood by people, it's going to be very obvious, particularly at this point. No one's going to believe the results of the stress test. Then you've undermined the credibility of the government further because the government endorsed the stress test. That's a very a bad path to go down.

Steve Weisman: Bill?

William R. Cline: If you want a concrete place to look at this, look at the market index of mortgage-backed securities, which became a derivative, and they just absolutely plunged close to zero. Where those assets really worth zero? The folks who go through default probabilities, through delinquency rates, etc., etc., were coming up with values that are much higher. There's a specific study at the OECD that was using the market index, to begin with, and then suddenly these prices are ridiculously too low, and then shifted over to sort of an expected-value approach. The Treasury, of course, has been going back and forth on evaluation. The original idea of the TARP was to buy these things and create a liquid market. You really have to have an incredible faith in the free market to think that under extremely distressed conditions, whatever you can get for the asset is its appropriate long-term price.

Now, I guess that's fine. But it seems to me that complete faith in free markets ignores what economists call multiple equilibria, where you can have a good outcome or a bad outcome. There's no single market price that in some broader sense is unambiguously the equilibrium price. There's no recognition that any price could ever be low or too high. We've got colleagues at the Institute, John Williamson or Arvind Subramanian, who want market intervention when a major exchange rate price is too low or too high.

So, there's an interesting implicit commitment that instantaneous market prices are always right being made by the folks who want to say that this stuff is worth nothing, and therefore that these banks are bankrupt and they should be taken over. There's also a failure to come to terms, I think, with the fact that if you take over banks, you're stuck for a decade with bureaucrats running these institutions. It's so different from taking over little tiny banks. The classic way that you get rid of the bank that the government takes over is that it sells it to a bigger fish. Well, there's no bigger fish, okay? So, then you somehow have to take over the two biggest banks, let's say, and you cut them into tranches. You're shopping around in a terrible market. How do you do that? So, you're stuck with this for a long time. But that's a little off from the specific question of asset valuation. But in some sense they're graded because eventually, you have to sell the assets.

Steve Weisman: But, Bill, the market, political commentators, Republicans, even some Democrats seem to feel that the status quo is just one of banks and the federal government kind of muddling along and hoping that the market will improve,

hoping that this public-private entity that they want to create that would buy some of these assets would kick in to gear and maybe value them higher than they are now. Meanwhile, there seems to be a loss of confidence, judging from both the market and political commentary. Isn't there something that should be done now to clarify at least the value of these assets or the status of these banks?

William R. Cline: This is precisely why Geithner's new approach is attempting to bring in market players with some sort of sweeteners so that they will look at these assets and assign a price to them when presumably, if you bring in a market participant, he doesn't want to overpay, and if he sees a bargain, he'll be willing to snap it up. So, yeah, there's an attempt and there's a need to develop a method of pricing these illiquid assets. But you talk about muddling through. Look, my experience would suggest—certainly with the Latin American debt crisis—that muddling through was the right way to go. Judging semester by semester, 1984 looked pretty good: The world was recovering, exports were going to go up, and we were working our way out of it. In 1986, Mexico has an earthquake! So, by the time you eventually got around to the Brady Plan, which was not that much of a haircut, 30 cents on the dollar, you had reestablished the strength of the financial system.

Now, Simon said at the outset he had no idea what would have to be taken over. He said later, "I just don't know." I think there's a bit of disconnect with the image that is being established by the most aggressive commentators on this—that is, that we know that this is a house of cards. We know that these banks are bankrupt. We know it's high time to do what Sweden did, to do what Japan did, so we don't have to lose a decade—by the way, in my calculations 1.5 percent lost output over a decade is all you're going to attribute to a zombie bank, but that's another story. I can go into that if you want. But it seems to me that the commentariat is unwilling to be attributed: "I don't know, I'm just not so sure about it, let's look at it." I mean, that's fine. But I wish every time that such a view is expressed by the commentariat, that they put up front and center a warning label that things may not be this bad at all, instead of the overall impression that comes across: that if we don't take over these banks immediately, we're going to have terrible problems.

Steve Weisman: Simon, do you think that if we don't take these banks over immediately we're going to have a terrible problem?

Simon Johnson: I think there is a danger of losing a decade. President Obama said that, I think it was three weeks ago at this press conference, although that was an extraordinary statement and a very nice indication of his awareness really of the kind of predicament we face. I think that rapid resolution of the problems in the financial system is a good idea in this country. It's always a good idea. That's always the advice, Steve, of the IMF when it goes into countries that are having this trouble. Usually, it's with the implicit or explicit backing of the US Treasury that the IMF makes that point.

Now, of course, Bill's right. That doesn't always happen that way and sometimes, of course, muddling through is maybe okay. But I think in this instance we should figure out quickly the true situation of these banks. We should resolve that in a fair, transparent way in accordance with our rules. And the rules may be fine as they are. Maybe they need to be adapted given the severity of the situation, and then we should move on. And I think the United States is good at this. I think the United States will do this better and faster than most other industrialized countries and probably better than almost all emerging markets as well.

Steve Weisman: And Simon, you're speaking with people inside the government in Congress. What is your impression about how fast they're going to move on the stress test of these 19 major banks?

Simon Johnson: Well, I wouldn't want to give anyone the impression that I'm an advisor to the government or that I have insight into the Treasury...

Steve Weisman: I didn't mean to give that impression. But I think you have learned things in your discussions. I'm not asking for state secrets but what's your impression?

Simon Johnson: Well, my impression based on public information is that over the next month or so they will make these results clear. It's not obvious why they can't move faster, given that they are the regulators and they supposedly had this information already, but we'll leave that to one side. And then there's a question of how quickly they will want banks to address any capital gap that is identified. There, I think, we just don't know. There are various ideas that have been bandied around but we don't know what the policy is. I think the vagueness and the lack of clarity on the rules of this exercise are to my mind something of a problem. I think you want everyone to understand what you're doing and why, and you want as many cards to be on the table as possible.

Steve Weisman: What do you think of the idea of setting up this public-private partnership to purchase the assets or make judgments about them? I mean, is that their answer to the concept of the bad bank? Does that make sense to you?

Simon Johnson: I think it could work. It's hard to say. We haven't really seen enough detail. I think it would be very expensive. The question is: Do you really want to spend 10 percent of GDP to clean up the bank system, which is one possibility? That's what I would guess, just guess.

Steve Weisman: That would be how much?

Simon Johnson: About \$1.5 trillion, which I think is consistent with the kinds of numbers that Bill was identifying in terms of capital deficiency if you look forward. And this is also consistent with the IMF's view looking forward. Or do you want to embark on a course that could be substantially more expensive, perhaps 20 percent or 30 percent of GDP? So, it's really a question of how much to do you want to

transfer from the taxpayer to people operating in the financial system. I think, you could do that in various ways.

Steve Weisman: But do you think this public-private concept is workable or could work?

Simon Johnson: I think it's a fantastic deal if you're a hedge fund or a private equity fund or someone...

Steve Weisman: But not for the taxpayer?

Simon Johnson: Well, it doesn't seem to me or to others to really offer extremely good taxpayer value, but there's no question, it could be a very nice way to gamble. It's a nonrecourse loan so you keep the upside. On the downside, you just lose the capital that you put in. So, the government is offering loans to very deep-pocketed individuals that are extraordinary by any standards and hard, I think, to justify politically. But if they can do that, then maybe that will help us get out of this at enormous cost.

Steve Weisman: Bill?

William R. Cline: Well, first of all, there's a difference between the good bank-bad bank or aggregator bank approach and the public-private entity to go in and basically to do what the TARP was going to do on a leverage basis. So, let's talk about that. It seems to be that the notion here is one of reviving a market for these illiquid assets. Now maybe you could be pennywise and pound-foolish if you are terribly concerned about paying the hedge funds too much to come in and start buying some of this stuff, because, yes, you probably would have to give them pretty good guarantees, etc. But if the result is that they act as a catalyst to bringing an entire asset class back into something that's closer to the values that folks tucked away in the Federal Reserve are cranking out based on the loan delinquency rates and unemployment rates of their models and saying, "Well, this should be worth maybe not 100 cents on the dollar but it's worth 60 cents on the dollar instead of 2 cents on the dollar," then the ultimate savings to the country could be considerably greater.

So, I think that it's important to get back to the initial idea of the TARP in one fashion or another and the notion of leveraging the TARP money. Probably what's going on here, I think, is that Treasury knows that it's going to be hard to go back to Congress for more money at this point and so, if you could use some of that TARP money on a sort of leverage basis, you can get more bang for the buck. On the good bank-bad bank, I always come up with this conceptual snag: "Wait a minute, how can you, by just defining half of my bank as bad and the other half as good, how can you get out of the problem?" At the end of the day, the bad bank has to take the losses, and they could not have been absorbed by the entire bank or they would have caused it to go bankrupt. But there's some loss that has to be recognized at the point of legal separation of the two entities that used to be a single entity. So, I'm still not completely clear on how the

aggregator or the bad bank is supposed to solve this problem.

Steve Weisman: Simon, on the bad bank–good bank concept: That’s worked in other parts of the world, I think, even in Sweden. Do you think that makes sense here?

Simon Johnson: You’re right, Steve, it’s part of the standard template for dealing with these problems when a bank is determined to have failed in other contexts and the government takes it over in some form. The standard way you deal with that is that you split the operations or the assets of the bank into two parts, one which you want to minimize the losses on. So, that’s where you use the so-called bad bank. And the experience of the Resolution Trust Corporation was mostly about minimizing losses on commercial real estate after the debacle of the 1980s savings and loans crisis. And they did a pretty good job on that, maybe getting 40 cents or 50 cents on the dollar.

And then there’s another part that you regard as being relatively good loans and a sensible business model, and presumably some buildings and so on and perhaps even a name that you can save from the ruins, and this is kept as a so-called good bank. And generally, presumably and hopefully in all contexts, this is sold off to the private sector as quickly as possible. And remember, you don’t have to sell the entire new, private, good bank immediately; you can sell a controlling stake of your relatively small stake. You can have a shareholder agreement that the government will stay out of the management of that bank, let’s say, for three years. And over time will sell the shares of that bank at market price.

So, you’re bringing in new owners, and this is why I say in all seriousness, what we need in this country and in all situations where it has been determined that the banks are in trouble, is privatization of the banks: You need new private owners, not anything to do with national ownership or national control. You need private owners who come in and clean up the compensation schemes, for example, the massive advantages that the insiders give themselves. That I think is the core and key problem, and you need private owners to do that.

Government shouldn’t go anywhere near appointing CEOs. The government two weeks ago said that Vikram Pandit will stay on as CEO of Citigroup. To me, that was an extraordinary statement: it indicates that you have political control, that you have effectively a form of nationalization at Citigroup. Otherwise, where does the government get the authority to determine who is and who is not CEO? That’s not what I would push through. I would say: Bring in new private owners. Let them appoint a new board of directors. The board of directors determines who are and who are not executives and officers of the company.

William R. Cline: Steve, I think Simon clarified very precisely my problem, which is the premise that the bank is first taken over by the government, the entire bank. That the government then does its housekeeping by dividing the loans into a good bunch of loans and a bad bunch of loans and then packages off the good bunch of loans as a new entity, that’s fine. That’s perfectly logical. But I think sometimes, or

most of the times, I would argue, the talk about the good bank–bad bank model seems to think that there’s a way that we can save the three or four really most at-risk large banks, shall we say, by somehow letting them slim down to a good core and that this aggregator or this bad bank is going to come around and take the bad stuff off their books. Now, that’s a very different thing, because that is not a prior takeover by the government of the entire entity. And my point is that I still haven’t got the logic of how you can do this alternative thing. How can you do that without the eventual act of a legal divorce between the good bank and the bad bank? And if that divorce were in terms that would leave the good bank in good shape, then this somehow would not be reflecting all of these losses in the bad bank that caused the problem in the first place. If you’re talking about how the housekeeping works once you’ve taken the bank over, sure: Divide it into a good bank, divide it into two good banks and three bad banks, I don’t know, but I think that is a different issue.

Steve Weisman: Let me close by asking both of you: It’s obvious that more government money is going to be needed to clean the system, a lot more. Is that correct? And how much more?

William R. Cline: Well, I mentioned some numbers at the outset. I think something like \$300 to \$400 billion of addition capital could be required. Now, one approach would be to put that in the form of preferred shares and you’re home free. The new mode is that it’s in preferred convertible shares that basically are going to carry a price. The date has already been set retroactively, although maybe that’s not clear, but that would then involve more ownership. The government could convert shares into common equity and therefore start raising the question of the majority ownership. So, one can work through the numbers, but if you get this market for these assets starting to move, then that takes some of the assets off of the books of the banks. So, they don’t need as much capital. If you take a cyclical regulatory approach: Keep in mind that the point at which the FIDICIA takes over a bank is at 2 percent, not 12 percent or 13 percent, of tier-1 capital.

Steve Weisman: I’m sorry the term...

William R. Cline: FIDICIA is the entity that took over IndyMac ...

Steve Weisman: It stands for....

William R. Cline: The FDIC...that’s the first part of FIDICIA. It is the mechanism whereby the FDIC tells the bank, “Okay, sorry, you’re going to be closed.” I think I can actually make a pretty good case that another \$200 or \$300 billion on the terms of what’s been done so far might not be a bad approach. But it can also be done in this mandatory convertible preferred method, which is the mode that they’re now going. I don’t think it’s insurmountable.

Steve Weisman: Simon, a final word on the cost.

Simon Johnson: Well, the view of the IMF, which has been published, and also based on my private communications with some people with a lot of experience in this kind of banking situation is really you're facing a choice here. I would not want to lowball the damage at all in any way. I think if you do it quickly and you do it cleanly and relatively decisively, it'll cost about 10 percent of GDP. That's just the bank-cleanup cost, I'm leaving out recession and so-on cost. Bank cleanup will cost \$1.5 trillion. If you go a longer, more painful route, many bad things will happen, most likely along the way, and losses will be considerably larger. And that price tag will probably be somewhere between \$3 and \$5 trillion.

So, you can still get out. The good news is you get out of it either way. The good news is the United States has plenty of capacity for issuing debt and I don't think the credibility of the US government and the Treasury is going to be undermined by this. The bad news is, of course, that if you go the more expensive route then you and your children and your grandchildren will be paying for this a lot longer.

Steve Weisman: Well, on that note. I want to thank both of you for agreeing to share your views in this new experimental format. I'm sure that our listeners and readers will benefit from your different perspectives and I think this worked well and maybe we'll do it again. Thank you both very much.

William R. Cline: Thank you.

