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Sunday Business

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BANK FAILURE!

By ROBERT GEARTY
Daily News Staff Writer

The scene in front of the Central National Bank of New York on Manhattan's Third Ave. this past week was eerily reminiscent of the Depression.

Each day, hundreds of depositors lined around the corner, anxiously waiting their chance to pull their money out of the bank in the wake of its failure.

Most had little inkling Central National was in trouble before the Controller of the Currency declared the bank insolvent Sept. 11 and named the Federal Deposit Insurance Corp. as receiver.

To government regulators and private analysts, however, there was no mystery as to what went wrong.

For one thing, they say, the bank made a number of bad loans that were eating up assets — among them, a loan for $100,000 to a reputed mobster who later defaulted. For another, it had made an unusually large number of loans to insiders at the bank, considered a poor practice.

More troubling were other indicators of the bank's instability. With $179 million in assets, Central National's ratio of stockholder equity to assets was well below the minimum at similar size banks. Central National also had higher than normal overhead costs. It was unclear why these costs were higher than at comparable banks.

"All this paints a picture of a bank in deep trouble," says Dean Zentner, technical director of Veribanc, a Wakefield, Mass. firm that analyzes and reports on banks.

Analysts say that Central National had been unprofitable since Jacobo Finkielstain, an Argentine real estate mogul, purchased the bank in 1981.

Finkielstain has reportedly had one other noticeable failure. His posh condominium development, "The Manhattan," on W. 52nd St. failed to attract enough buyers because of the high price for apartments, forcing lenders to foreclose on the project last year. Today the project sits empty as Finkielstain tries to work out the problem with lenders.

The federal government regularly keeps a watchful eye on banks, but it wasn't until two years after Finkielstain took over that Central National came under closer scrutiny as problems with its loan portfolio became more apparent, government sources say.

Last July, according to the sources, federal bank examiners began an on-site review of the bank's books and determined that a number of loans would never be repaid. At that point, the bank's liabilities outstripped its assets and the bank was declared insolvent.

Complicating matters, say other sources, was the disappearance of $32 million in Argentine bearer bonds the bank was supposed to be holding as part of repurchase agreements with about 20 individuals and corporations. When asked to produce the bonds during the review, the bank was unable to do so.

These sources say the bank already was insolvent by the time the discrepancy was discovered. Investigators now are trying to determine what happened to the bonds.

Central National's collapse was barely noticed by the financial community. The bank is one of the smallest in the state.It had just 13,400 depo-

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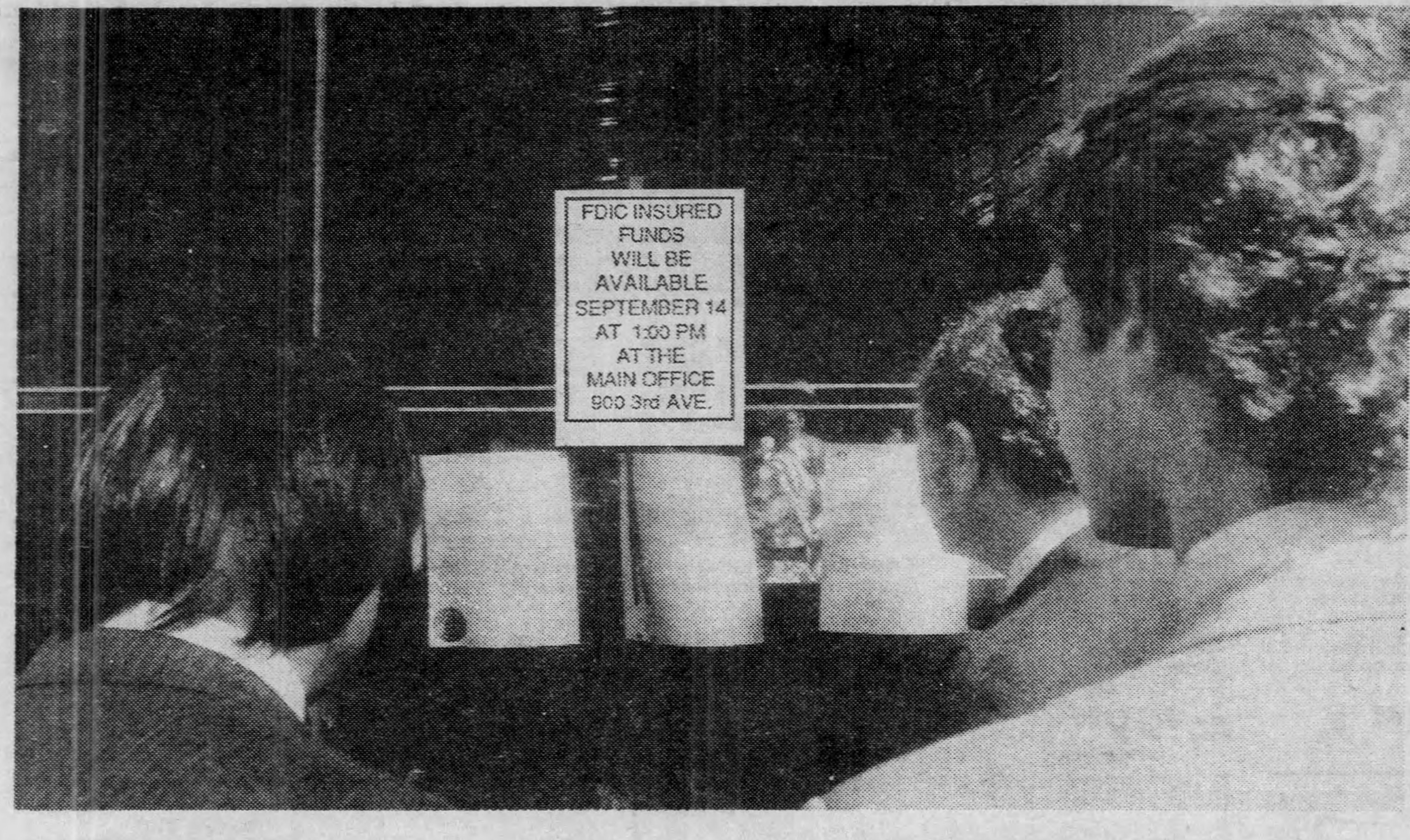

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siters. In addition to its main office, the bank had two branches in Brooklyn and one in Long Island City.

Central National's failure was the first in New York in two years. "Most banks in New York are doing well," says Thomas Schettino of Lyons, Zomback & Ostrowski, a bank consulting firm.

Particularly troublesome for Central National was the large dollar amount of its "problem" loans — loans earning no interest, rolled over or renegotiated. Analysts say it was much higher than in comparable banks.

Zentner says most of these loans went to businesses. "That says they were loaning to people no one else would lend to," says Zentner.

According to court records, in December 1981 Central National loaned $100,000 to Michael Franzese, a reputed captain in the Colombo crime family. The loan was rolled over three times, before Franzese defaulted. In 1984, the bank obtained a judgment against Franzese, who now is serving a 10-year prison term on racketeering charges.

In 1985, the bank lent $506,000 to an export company that was operating out of a couple's Coral Springs, Fla., home. Last year, the firm defaulted on nearly $400,000 of the principal.

Last July, lawyers for the bank filed papers in Manhattan Supreme Court alleging that the bank was defrauded out of $880,000. Named as defendents were a Venuzuelan businessman and several companies in Venuzuela. Details were unavailable.

Loans to insiders totaled $1.6 million as of last March, more than half the bank's equity, analysts say. At least a third of the total had been loaned to one unnamed official. Banks are not required to identify insider loans.

"It's very unusual," says Zentner. "Most banks avoid it because it gives the appearance of impropriety to be doing that much business with officers and stockholders."

Neither Finkielstain nor any bank officers could be reached for comment.

An FDIC spokesman says an investigation has begun to determine what role, if any, bank officials played in the collapse. If warranted, civil charges could be brought against individuals to help pay off uninsured depositers.

The FDIC guarantees deposits up to $100,000 and issues IOUs for the remainder, which will be repaid as the government locates more assets. Officials say they originally estimated that $37 million in deposits at Central National were uninsured. They now say that deposits totaling $24 million were uninsured.

FDIC regional director Michael Martinelli says that the agency had been paying out insured depositers at a rate of 1,000 a day.

New bankers have $16M incentive

By R.B. PLUNKETT JR.
Daily News Staff Writer

At the annual meeting last May, J.A. Elkins Jr., chairman of faultering First City Bancorp of Texas, said he was looking for an investor who could serve the best interests of all shareholders.

Last week, with the help of the FDIC, the bank got its financial backing — in the form of Chicago banker A. Robert Abboud, who is taking over the Houston-based bank.

But the question now is who is being best served, the shareholders or Abboud?

Under a complex restructuring plan settled with the FDIC, Abboud has secured a $16.6 million incentive bonus for himself and four executives he will hand pick to help run the bank.

The bonus comes in a stock-for-performance incentive package, which is common in attracting investors to failing businesses but rare in the banking industry — especially in an FDIC-assisted merger.

Under the FDIC-approved recovery plan, the bank will sell stock to the public later this year at $25 a share and the Abboud management team will hold the warrants giving it the right to buy 667,000 new shares of the stock at a later date.

If Abboud can stem the bank's losses and turn a profit within the next five years, he and his management group will be allowed to exercise their warrants for 7.5 cents each. So, for a $50,000 investment they can own $16.6 million in bank stock.

However, if Abboud can't turn a profit after five years, the team won't earn any warrants.

In addition, Donaldson, Lufkin & Jenrette, the investment counsel to Abboud stands to earn $50 million dealing with the bank — $25 million in fees and another $25 million exercising warrants for a future stock purchase.

Small banks, big problem for FDIC

By LAURIE COHEN

The bailout earlier this month of First City Bancorp. of Texas lifted a huge weight from the shoulders of the Federal Deposit Insurance Corp., but the agency still is burdened by many smaller problem banks.

The FDIC, which insures bank deposits, has faced mounting financial strains since 1982 because of loan calamities in energy, real estate and agriculture. Its expenses more than tripled to $3 billion in 1986, mainly because of the cost of closing or assisting with mergers of failed banks.

Now the FDIC may have weathered the worst of the storm — at least the part that's visible — some observers say. In the rescue of the Houston-based First City, the agency will inject $970 million, with the guarantee that it will be repaid at least $100 million. Former Chicago banker A. Robert Abboud and his investment bankers will raise an additional $500 million through public offerings for the $12.2 billion-asset company.

"For a long time, the FDIC has viewed First City as the largest problem on its agenda," says Paul Horvitz, a University of Houston finance professor and former FDIC research director. "To get this out of the way is a big relief."

"Once this deal is done, the FDIC will have turned a corner," adds the agency's former chairman, William Isaac, now a bank consultant. "Assuming we don't get into a recession, there aren't any other major bank failures on the horizon.'

In particular, prospects for BankAmerica Corp. seem to have improved with a change in management and plans for a capital infusion from Japanese banks, sources say. The second-biggest U.S. bank-holding company, with assets of $82.2 billion, has been a major question mark for two years because of its heavy load of problem loans.

But even with the important qualification about economic conditions, many experts aren't so sanguine about the agency's health.

"I don't think the FDIC is out of the woods by any means," says Bert Ely, a banking and savings and loan consultant based in Alexandria, Va."There are still a lot of problem banks out there.'

Reasons for continuing worry include the recent jump in interest rates, which could hurt bank profits and further weaken troubled borrowers. Major banking firms have taken steps to bolster their reserves for problem Third World loans, but the actions haven't completely shielded them from the developing-country debt situation.

"This is a business where disaster can happen any time," says New York-based consultant David Cates.

Some observers predict that the bailout of First City could force the FDIC in 1987 to post the first loss in its 54-year history, causing the first decline in its $18.4 billion insurance fund. "This pushes them more toward the possibility of showing a loss on their 1987 statement," says an official of the General Accounting Office, the agency's auditor.

An FDIC spokesman says the agency's income statement for this year will reflect the maximum cost of the First City rescue, now estimated at between $800 million and $900 million. The agency's auditor, the General Accounting Office, forced the FDIC to revise its 1984 statement because it hadn't included any provision for losses on bad loans acquired from Continental Illinois National Bank and Trust Co. of Chicago.

But the FDIC spokesman says that even after the First City transaction, the agency, which insures deposits of about $1.6 trillion held by more than 14,000 banks, expects to break even or turn a slight profit this year.

The agency says that bank failures are likely to hit a post-Depression record 200 this year. That would be up from 138 in 1986 and 10 in 1981. But next year the number is likely to go down for the first time in seven years, FDIC Chairman L. William Seidman has said, because of expected improvements in the economies of Farm Belt states.

The agency's list of problem banks has eased recently for the first time since 1981. Moreover, the number of banks close to or posing a serious threat of failure stood at 1,607 at the end of August, down from 1,635 in July. The list included 1,098 banks at the end of 1985

Seidman says the agency expects First City to be the last of the big Texas banks requiring aid.

Despite such optimistic signs, some experts argue that the fund's reserves are overstated. They point out that the FDIC's auditor, the General Accounting Office, hasn't required the FDIC to record a contingent liability, covering the cost of closing or merging institutions now on its problem list.

"The FDIC has been striving to break even because it doesn't want to show a loss," says Ely. "It hasn't been booking the reserves it should be."

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