Benelux countries intervene to bail out Fortis

The rise and fall of Fortis

By Stephan Steinberg
1 October 2008

Stock markets across Europe tumbled on Monday following the news that leading banks across the continent were facing collapse.

The plunge in the stock markets took place prior to the announcement of the rejection of the Wall Street bailout plan by the US House of Representatives. It is an expression of growing panic by European investors over the potential meltdown of financial institutions across the continent.

On Sunday and Monday European governments and private banks bailed out no less than three major banks--Germany's Hypo Real Estate, Britain's Bradford & Bingley and the Dutch-Belgian Fortis group. Their action was followed by intervention in Iceland on Monday when the government in Reykjavik took over control of Glitnir, one of Iceland's biggest banks.

Of the four banks, Fortis is by far the biggest. It ranks among Europe's top 20 banks and has a global workforce of 85,000. It is active in 50 different countries and its involvement in international banks and financial institutions stretches from the heartland of Europe to Eastern Europe (Poland), central Asia (Turkey) and China. The affiliated Fortis insurance group is one of the 10 biggest insurance companies in Europe.

Last Sunday, the Dutch, Belgian and Luxembourg governments raced to rescue the Fortis group with a package costing almost €11.2 billion. The intervention came following a 21 percent fall in the share price of Fortis on Friday and rumours of a massive liquidity crisis. Belgian Prime Minister Yves Leterme intervened on the same day to reassure investors and promised customers they would not lose their money. Belgium Finance Minister Didier Reynders said the bank had "absolutely no solvency problems."

Over the weekend, however, the heads of government became convinced that the problems at Fortis were so serious that they had to intervene immediately with a deal involving the Benelux governments taking a 49 percent share in Fortis operations in their respective countries and thereby guaranteeing its liquidity with taxpayers' money.

Negotiations over the partial nationalization were led by Jean-Claude Trichet, the president of the European Central Bank. Trichet made clear that his intervention was motivated by the concern that a collapse of Fortis could destabilise the entire euro zone.

De Standard declared that rapid government intervention was the only alternative to a "European financial and economic bloodbath."

It asked, "Is it normal that the rules no longer apply for these masters of the market? Certainly not, but there is no alternative…. The imperative need to prevent Fortis from becoming the first domino to fall in a European financial and economic bloodbath makes this rescue plan necessary."

The paper goes on to state, "What we have witnessed with Fortis in the past few days is just one episode of a brutal purge in the financial sector. Only the joint efforts of policymakers and banks can prevent this purge from turning into a bloodbath."

As is the case with Paulson's proposal in the US, the Benelux partial nationalisation package is aimed at "getting the bank back on its feet," i.e., awarding billions in taxpayers' money to the speculators responsible for the current crisis at Fortis and for whom "the rules no longer apply." The Benelux governments have declared their intention to sell off their share of stock at a later date and once again permit Fortis to function as a fully privatised entity.

The entire intervention process, involving billions of euros, was carried out in a matter of hours and took place without any discussion within European parliaments, not to speak of any consultation with the citizens of European countries who will be forced to foot the bill.

Willem Buite, who supports the bailout, commented in the *Financial Times* on Monday, "Especially remarkable is the fact that it took much less time and effort to put together the multi-country fiscal rescue effort of the three EU member states than it took to cobble together the son-of-TARP [the Paulson plan] in the US. Incipient federalism triumphs over dysfunctional established federalism."

Despite the unprecedented intervention on Sunday by European leaders, the verdict of economic circles and shareholders on the Benelux deal was overwhelmingly negative.

Less than 12 hours after the deal was brokered and minutes after a press conference given by the company's new CEO, Filip Dierckx, in which he declared that Fortis will remain a strong private bank, its share price nosedived to a 16-year low of just over €4.

The rise and fall of Fortis

The rapid rise and fall of Fortis is symptomatic of the development of a broad spectrum of European financial institutions in recent years. The banking house was first founded in 1990 and grew steadily through a series of acquisitions of European banks and insurance companies. In 1999 Fortis extended its reach across the Atlantic and took over the American Bankers and Northern Star Insurance Groups.

Fortis was still a relatively minor player in the banking world until one year ago when it joined forces with the Royal Bank of Scotland and the Spanish bank Santander to take over the Netherlands' largest financial institution, ABN Amro. The consortium of banks paid €70 billion for ABN Amro, the biggest sum ever paid to acquire a bank. The Fortis share of this total was €24 billion. Since the purchase of ABN Amro, however, the extent of Fortis's lack of liquidity and involvement in dubious investments has gradually come to light.

This July the company sought to raise a sum of €5 billion in additional capital to maintain its solvency targets. In August, under pressure from European regulators to raise additional funds, Fortis sold off its 49 percent stake in a Chinese asset management business to a British company, Old Mutual.

None of these moves were sufficient to stem the run on the Fortis share price. Since taking over ABN Amro a year ago, Fortis shares have lost more than three-quarters of their value. Last week alone the company's share price dropped by over a third following renewed concerns over its liquidity.

The conclusion drawn by the Dutch business daily *NRC Handelsblad* is that "In a little over a year, Fortis has changed from a prestigious financial institution to a pariah in the banking world."

The collapse of the Fortis group graphically reveals the extent of the involvement of European banks and finance institutions in the "toxic debt" mountain that has emerged since the onset of the sub-prime mortgage crisis in the US. The crippling exposure by many European banks to such debts, arising from the uncontrolled growth of what is essentially fictitious capital worldwide, refutes the views of those politicians and commentators who still maintain that the European "welfare" model capitalism represents some sort of a viable alternative to its US counterpart.

According to the Dutch daily *Trouw* in a recent commentary, "American misconduct was the origin of the crisis. For years both the state and the citizens ran up an absurd number of debts, giving the impression that they would never have to be paid back."

The alternative, according to *Trouw*, "is another form of capitalism, known as Rhine capitalism…. This type of capitalism also creates prosperity by allowing business to compete freely on markets. But it has more securities built into it…. Luckily here we have maintained our differences. Luckily here the state and the citizens have fewer debts than in the US. And luckily we now know the direction in which we must develop to create prosperity without winding up as a casino economy."

The crisis of Fortis and a growing number of banks across Europe is testimony to the contrary--the inextricable involvement of European finance houses in the finance crisis reveals their vulnerability to precisely such a "casino economy."

Across the border the Dutch business daily *NRC Handelsblad* struck a much more sombre note in an editorial last week: "If for no other reason, the current financial crisis is a historic event because no one can maintain any longer that unlimited free trade automatically leads to a better world. And the old liberal fairytale that the market always corrects itself has also been discredited.... The late summer of 2008 will go down in history as the moment when the last political ideology of the 20th century experienced its demise. Almost 20 years after what looked like the definitive defeat of communism, the victor from those days is also down for the count. Both Cold War camps are now washed up. It will take a couple of years before the bankruptcy crystallises out. Then the 20th century will finally be over, just as the 19th century only ended in 1914."

The paper does not spell out the implications of its own analysis, but the fact is that the bankruptcy of 19th century capitalism heralded an era of wars of unprecedented brutality and the world's first successful social revolution in Russia.