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THE WHITE HOUSE

PRESS CONFERENCE
OF
WILLIAM E. SIMON
SECRETARY OF THE
DEPARTMENT OF THE TREASURY
AND
RICHARD DUNHAM
DEPUTY DIRECTOR OF THE DOMESTIC COUNCIL

THE BRIEFING ROOM

8:37 P.M. EDT

MR. NESSEN: Now, you have a text of a letter from the President to the Mayor of New York.

Mayor Beame and Governor Carey were at a dinner together and this letter was read to Governor Carey who passed on the information to Mayor Beame.

Q Who read it to him?

MR. NESSEN: Jim Cannon read it to him. A copy of the letter also was sent by Dex machine to the Mayor's office.

Cannon is talking to Beame, himself, now.

With that preliminary out of the way, I am going to let you ask any further questions of Secretary Simon. I think you know Dick Dunham, the Deputy Director of the Domestic Council.

SECRETARY SIMON: Thank you, Ron.

Ladies and gentlemen, the letter is self-explanatory. As you know, over the past two months, we have been meeting with City of New York officials attempting to ascertain exactly what their problems were -- the appropriate Federal officials -- the economic group, including the Federal Reserve here in Washington, and we have done a considerable amount of work on this issue to explore what actions the Federal Government could take.

Our options were severely limited. Let me just briefly give you the options that we had.

One, we could have advanced payments on Medicaid and revenue sharing. It would have amounted to really a relatively small amount of money, under $200 million, which did not even begin to meet their problem. They must raise $3.5 billion between now and August in the markets -- over $1 billion in the very near future.

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Their access to these markets in the absence of a demonstrated fiscal responsibility and balanced budget in the City of New York is very clear to the financial community, as well as the City of New York.

So, that was not a viable option for really either side not even to get into the dangerous precedents of advancing and utilizing revenue sharing and Medicaid payments which would have been passed through for purposes such as this.

The second option was to seek legislation in the Congress -- legislation that would empower the Treasury to either purchase New York City securities or to guarantee New York City government debt.

There again, we have a problem with precedents. Would the Congress indeed give us the permission through legislation to guarantee or purchase city or State municipal debt or would it spread across the entire spectrum to other cities that indeed would be asking for aid in addition to this?

Also, the question was co-legislation, if it were looked upon favorably -- and there is considerable doubt as to that, believe me -- would it come in the needed amount of time?

The third option available was the Federal Reserve Board, the traditional lender of last resort.

Actually, there is no precedent for the Federal Reserve action in matters such as this in assisting a State or municipality and create again a precedence that would shift the focus of the Federal Reserve from the institution that protects the integrity of the United States dollar setting monetary policy in the United States as an independent agency, and shifts its focus to one of a social institution with all of the monetary implications, that would be extremely dangerous.

So, the option that the President chose was really the only immediate option that we had, which was to attempt to talk to the State and the city about resolving their problems themselves, and the State does have options.

The State can guarantee on a first appropriation basis the City of New York's debt, the very large pension funds can purchase New York City securities, but this should be done simultaneously with New York City taking the necessary steps that is going to restore the confidence and the integrity of New York City in the financial markets.

Now, I will be delighted to respond to any questions that you might have. I tried to put that in short form for you.

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Q What happens, Mr. Secretary, if this option does not work and the confidence is not restored? What then?

SECRETARY SIMON: The next step is for New York City and New York State to take the necessary, extremely difficult actions, political actions, that they have resisted taking before. The first reaction is always to lay off firemen and policemen.

There are some fundamental problems in the fiscal area in New York City where their expenditures have grown at an annual rate of slightly in excess of 15 percent and their revenues grow slightly under 8 percent. One can see they continue to move their operating expenses into the capital budget, and that is an obvious problem.

The transfer of the $1 billion 700 million in the capital budget in New York City now, over $700 million of those can be deemed as operating expenses. When one issues long-term debt to financing operating expenses, obviously this has a great problem in the financial community as far as credibility is concerned.

Needless to say, it is also more expensive for taxpayers. An estimate would be 15 to 20 percent. So, they have to put their financial and fiscal house in order and do it so they will have the access to the marketplace.

A bridge is going to have to be built. As the President said to Mayor Beame in his letter, this bridge can be built by New York State legislature, and it can be done in sufficient time to allow New York City to have access to these markets.

Q Mr. Simon, are you convinced that if there is a default in New York City within the next 45 days, until the end of its fiscal year, that it will not have a severe effect on the national banking industry or have as devastating effect on the credit market as the UDC default did?

SECRETARY SIMON: Are you implying by your question that the UDC default had a devastating effect on the credit markets?

Q It had a severe effect certainly on municipal securities and New York City securities, and New York State paper.

SECRETARY SIMON: Now you are getting it very isolated, aren't you? Actually, what you did, it had an effect on the so-called moral obligation bonds in New York State, the agencies the housing finance agency and others, yes, that was another case.

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Again, they can avoid default. They can avoid default by doing the necessary things that should have been done a long time ago and indeed need to be done right now to restore the longrun and long-term viability to this city and it is going to be tough decisions.

I don't mean to suggest that it is easy for them to make these tough decisions, whether it be the raising of the subway fare or tolls on some of the toll-free bridges or whatever the steps are. That is not my position to recommend.

There is no doubt that a default by New York City would be very serious, yes, but let me assure you that the Federal reserve in its capacity as the lender of last resort, as far as our financial institutions are concerned, would perform this function that is inherent in their operations and also, let's remember that the total assets of New York City paper held by the New York banks does not endanger banks.

Q $3 billion?

SECRETARY SIMON: It does not endanger banks of that size. As I say, I don't think, and we do not believe, that a default is necessary if the necessary actions are taken.

Q If Congress were to pass a resolution in support of that kind of legislation that was considered, what would be the President's position and your position on that?

SECRETARY SIMON: I would have to say it is very difficult to comment on legislation that has not passed. I would refuse to believe it would be --

Q No, a resolution, I said. If there was a sense of the Congress supporting that kind of --

SECRETARY SIMON: A sense of the Congress would not give New York City the ability to finance, as far as the guarantee or the purchase.

Q Would it change your mind, is what I am asking?

SECRETARY SIMON: I would like to see again exactly what this resolution is. I have talked to a great many of the legislators on the Hill relative to this problem.

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As you well know, the recession has given some fiscal problems to many cities in this country and many States, and there had to be necessarily some belt tightening. I would find it hard to believe that our Congress would be willing to act in one city in the absence of attempting to assist everyone else -- not only attempting to assist everyone else as far as potentially Federalizing State and local debt by giving this guarantee authority, but also the other social priorities that are sometimes very popular in the Congress, such as housing and small business and others. This could turn out to be another way to allocate credit.

Q Do you feel that as of right now it would be impossible for the city to hold a public sale of its paper at this time between now and June 30?

SECRETARY SIMON: I would not comment on that. There again, I believe that if New York State, if the legislature does the necessary things, its city puts fortha credible balanced budget posture, and this bridge is built, as the President again suggested in his letter, then New York City will have access to the credit markets.

Q Mayor Beame said yesterday that he presented the President and yourself with evidence that the city was taking severe austerity measures and would come in with a balanced budget for its next fiscal year without any type of gimmickry. That was what he said.

Do you believe from the figure that you have presented that that is an accurate statement of the type of --

SECRETARY SIMON: It is very difficult to assess in a day. The President asked for a great many figures and as far as the specifics of this on the New York City budget and the State fiscal position, Dick Dunham, who is the former head of the Bureau of the Budget in the State of New York, and an expert in these matters, can respond to this.

MR. DUNHAM: In regard to that question, the one major open item is the so-called gap of $605 million, and that gap is dependent upon action of the State legislature so that whereas the Mayor did rightly say it is his intent to present a balanced budget, because of the lack of action in Albany on his request does not have the power to submit the balanced budget with that large unknown in it.

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Q Mr. Secretary, may I clear up one point? If there is a default, are you saying that the Federal Reserve will provide the needed funds?

SECRETARY SIMON: No, I did not.

Yes, I am glad you asked that question because I did not even imply it, no.

I said the Federal Reserve would carry out its traditional role as it affects the consumer banking system, if indeed there was a problem.

Q What do you mean by that?

SECRETARY SIMON: Then I went on to add that the size of the assets held by New York City banks -- remember, they are the largest banks in the world -- of New York City securities, it is in no danger of impairing their financial condition because it is a very small percent of the total assets of the bank.

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Q By carrying out its traditional role, precisely what do you mean?

SECRETARY SIMON: The Federal Reserve is a lender of last resort who assists financial institutions with liquidity problems and sometimes short-run problems like this present liquidity problem, and that is their function. But by no means, through that explanation, do I expect that to occur.

Q Then, you are talking only of lending institutions of that kind?

SECRETARY SIMON: You are talking about the commercial banking system, which is the Fed's responsibility.

Q You say in your letter to the Mayor that you have no doubt that the adoption of a sound budget policy would have a substantial and beneficial effect.

Are you satisfied that the sound budget policies will be adopted?

SECRETARY SIMON: As I look at the New York City situation -- and remember that there is no doubt that Mayor Beame inherited many of the problems he has -- and to date, he has taken a number of laudable steps.

But there are many more things that have to be done to assure the long-run viability of the city. I just gave you one example of the capitalization of operating expenses and many of the other areas of the budget that have to be pared back, looking at the growth of expenditures vis-a-vis the revenues.

THE PRESS: Thank you, Mr. Secretary.

END (AT 8:48 P.M. EDT)