

Banking by John Hoefle

Olympia & York: the bankers' nightmare

The banks are taking huge losses on their O&Y loans, but that's only part of the story.

Papers filed by Olympia & York Developments Ltd. in its bankruptcy filing in Canada, even though they conceal more than they reveal, give the most detailed look yet at the failed company's balance sheets. The picture shows why bankers are quaking in their boots.

The Canadian banks have already reported their exposures to O&Y. Out of a total of \$2.5 billion in O&Y loans, \$2 billion has been declared non-performing. The Canadian Imperial Bank of Commerce reported that 81% of its \$714 million of loans to O&Y was non-performing, compared to 65% of \$648 million at the Royal Bank of Canada, 62% of \$523 million at the Bank of Nova Scotia, 100% of \$393 million at the National Bank of Canada, and 96% of \$274 million at the Bank of Montreal. Canadian Imperial set aside \$830 million in special reserves for its O&Y losses in the second quarter, giving it a loss of \$365 million, the largest quarterly loss in the history of Canadian banking.

According to the data filed with the bankruptcy court, which cover only the parent Olympia & York Development Ltd. and its 28 subsidiaries involved in the Canadian bankruptcy, the largest lender to O&Y was the Hongkong & Shanghai Bank, with an exposure of \$787 million. The bulk of that, \$750 million, is part of the \$2.5 billion loan made by a syndicate of banks to O&Y Resources Credit Corp. for London's Canary Wharf real estate boondoggle.

That syndicate also includes: the Royal Bank of Canada, which lent \$250 million; a syndicate led by Dai-

Ichi Kangyo Bank of Japan, which lent \$250 million; and a syndicate led by Crédit Lyonnais of France, which lent \$1.25 billion.

According to a study by Toronto brokerage McLean McCarthy, the securities used as collateral for this \$2.5 billion loan have a current value of only \$1.6 billion, or 65¢ on the dollar. That means that these banks have already lost \$900 million.

A syndicate led by Citicorp, which lent \$500 million, has done even worse, relatively speaking. The collateral backing the loan is worth just \$145 million, or 29¢ on the dollar. Two major Japanese banks are members of this syndicate: Tokai Bank, which loaned \$250 million, and Dai-ichi Kangyo, which loaned \$180 million. These banks have already lost \$355 million.

Overall, according to McLean McCarthy, the value of the collateral backing O&Y's \$4 billion in securities-backed loans, is now worth just under \$2.9 billion, or 72¢ on the dollar.

These loans do not tell the whole story, however. The Canadian bankruptcy filing covers only about \$7.5 billion of O&Y's admitted \$11.3 billion in debt. The Canadian filing does not include loans made directly to O&Y's Canary Wharf subsidiary, nor does it include loans made for U.S. real estate properties.

Furthermore, many billions more in liabilities do not appear in any of the above categories.

In its Canadian bankruptcy filing, O&Y reported \$78 million in so-called interest rate swaps, used to lock

in fixed rates of interest. In an interest rate swap, a party with a floating interest rate on an obligation, swaps interest payments with a party with a fixed interest rate obligation. O&Y's interest rate swap obligations, according to the *Wall Street Journal*, are actually \$140 million, nearly twice what was originally reported.

The notional amount of those interest rate swaps was reported in the May 14 bankruptcy filing as \$835 million, but, according to the *Journal*, O&Y has an additional \$800 million in swaps from banks such as Citicorp and J.P. Morgan, for a total of more than \$1.6 billion. According to the *Journal*, the question of whether the \$1.6 billion in principal is at risk along with the \$140 million in interest, is "a topic of debate."

As an incentive for firms to relocate to O&Y office buildings, O&Y often bought out their new tenants' existing leases. The amount of such buyouts has not been revealed, but American Express, one of the companies which agreed to move into Canary Wharf, maintained that the value of O&Y's promise to buy out Amex's current leases was large enough to give it a seat at the creditors' table in the bankruptcy negotiations.

Overall, according to European banking sources involved in the O&Y negotiations, the total debt of O&Y runs from a minimum of \$25 billion to as much as \$47 billion, once all the swaps, lease buyouts, and other exotic financing tricks are added in.

The fact that O&Y doesn't have enough assets to cover its liabilities, was made clear in both the U.K. and Canada. In Canada, the creditors were publicly feuding over where each stood in the repayment line. In the U.K., two potential bidders for the corpse of Canary Wharf said that the project was worth no more than one-fifth of the amount it cost to build it.