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## Tuesday, 7 October 2008

*'You're in a bit of trouble'*

Lord Myners to Fred Goodwin

Outside London's Ritz hotel, a chauffeur-driven S-Class Mercedes painted Royal Bank of Scotland blue sits waiting for Sir Fred Goodwin. Shortly after 8 a.m., the RBS chief executive makes his way through the revolving doors of the hotel, walks past the doorman on the steps, emerges onto Arlington Street and gets into the car. The London markets are opening for business and it promises to be another turbulent day. Yesterday, Monday 6 October, RBS shares had stood at just 148p when trading finished in the City, meaning that in six months of wild fluctuations the price has more than halved. The share price is simply a measurement of what investors – from massive institutions that control our pensions to individuals who play the markets – are prepared to pay to own a slice of a company. It is an indicator of a firm's health, monitored on screens by profit-seeking traders who look at moments of crisis such as this for clues as to how ill the patient might be. RBS is about to go into cardiac arrest.

Pulling away from the Ritz, Goodwin's car heads north, through Mayfair. The first appointment of the day is a long-standing engagement from which he is unable to extricate himself. The RBS chief executive has been booked as one of the first speakers at today's Merrill Lynch annual banking and insurance conference, being held in a lesser five-star hotel, the Landmark, on Marylebone Road. Such events, held in front of several hundred executives and banking industry analysts, are standard fare for chief executives, who usually do a bullish presentation on their company's prospects, take a few questions and then leave. Goodwin also knows the hosts well, the American investment bank Merrill Lynch. That relationship stretches back to Merrill's richly rewarded advisory work on the £21bn purchase of NatWest in 2000 that had made Goodwin's reputation. Matthew Greenburgh, one of Merrill Lynch's highest-paid dealmakers, had become a trusted counsellor and friend. Anyway, failing to turn up to the conference is not an option. It would suggest panic.

There is a lot to panic about this morning. For months investors and traders have been trying to rid themselves of shares in banks exposed to the sub-prime crisis, which has its origins in years of catastrophically lax mortgage lending in the United States. Merrill Lynch has itself already been swept up in the tumult. Riddled with sub-prime-related problems of its own, it was sold to Bank of America in September. Today, the next bank in the line of fire is RBS, a Scottish institution that has grown rapidly to become a global player. Goodwin and his colleagues have waded into the toxic swamp of sub-prime and are now stuck, up to their necks. It is not just the share price that is a problem. That is merely a reflection of a more fundamental weakness. The bank is leaking money at a phenomenal rate. Just raising the billions it needs every day to keep going has been a struggle for months, and now the situation is deteriorating as large depositors move their money out. A major oil firm is the latest to show that it has lost faith in RBS's ability to survive, suddenly withdrawing more than £1bn in deposits and quietly putting the money somewhere deemed safer.

Fearing that the entire banking system is about to collapse, government ministers and officials have been attempting to work up a rescue plan in collaboration with the Bank of England's governor Mervyn King and the chairman of the FSA Adair Turner. Several senior bankers and lawyers have been drafted in to help. Yesterday evening, Monday, as part of the latest effort to find a solution, Goodwin had gone to the Treasury in Whitehall with fellow chief executives from Britain's other big banks for what was meant to be a private meeting with the Chancellor of the Exchequer, Alistair Darling. Goodwin claimed, yet again, that the problem facing RBS was a temporary one of simple liquidity, or cash-flow, attributable to panic in the markets. The underlying business was sound, he said. Darling and the senior officials in the Treasury see it differently – as a question of capital, and the banks holding too little of it to cover looming losses. RBS is the worst exposed. The government will have to find a way of giving the weakest banks billions more in capital, which will mean the taxpayer owning large shareholdings in the bailed-out institutions. Darling is frustrated by the response and is convinced that the bankers, particularly Goodwin, are refusing to face up to the true nature of the problem. The meeting had broken up without agreement, and Goodwin retreated to his usual suite at the Ritz, his London base while the Savoy Hotel is refitted.

News of the Monday evening meeting at the Treasury does not stay private for long. At 7 a.m. on Tuesday morning the BBC's business editor Robert Peston publishes an account on his blog.[1] Peston had been briefed late the night before and then again first thing that morning. He knows he has a 'bloody great story', although he is not prepared for the scale of the sell-off on the markets that his report is about to help trigger. Peston reveals that the bankers who had met with Darling were unimpressed; their view is that the government simply does not have a serious plan in place to deal with the crisis and that ministers should get a move on. The message is clear. The bankers think that the government does not know what it is doing. This news takes a little time to ripple across trading floors, where already jumpy traders are looking for reassurance that someone is going to step in and avert disaster at RBS and the other banks. Now the parties supposed to be sorting it out are squabbling. Cue panic selling.