FINANCIAL TIMES

July 2, 2012 10:04 pm

Deal leads to lower loan costs for Ireland

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By Jamie Smyth in Dublin and Peter Spiegel in Brussels

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Ireland's borrowing costs have dropped to pre-bailout levels since Friday's unexpected summit agreement that could see the €500bn eurozone bailout fund take over a chunk of the €64bn in bank-related debt now on the country's balance sheet.

But Irish officials and banking experts acknowledged that because many Irish banks owned by the government are worth far less now than when nationalised, Dublin is unlikely to get back what it put in if, and when, it unloads its holdings to the rescue fund.

Irish officials will present options for shedding bank holdings at a meeting of eurozone finance ministers on July 9, and they expressed hope of getting a deal by October – despite the fact many believe creation of a eurozone bank supervisor, which Germany has insisted as a prerequisite to an Irish bank deal, could take far longer.

"We are not underestimating the very tough negotiations that will happen over the next few months," said Brian Hayes, Ireland's deputy finance minister. "But Europe needs a success story and we can provide it with the right help."

Ireland unexpectedly won the possibility to unload its bank debt after Spanish officials convinced Berlin to support a similar plan for its own teetering banking sector at an all-night negotiating session on the sidelines of last week's high-stakes EU summit.

Irish officials, who had been in close contact with their Spanish counterparts in the run-up to the summit, did not believe a deal on Spanish banks was in the offing and only learnt there was an opening on Thursday evening, when senior finance ministry officials from all 17 eurozone countries met to hash out a deal.

Under this plan, the new eurozone rescue fund, the European Stability Mechanism, will be able to inject money directly into weak banks instead of lending the money through national governments, which was the only option available when Ireland was bailed out nearly two years ago.

Rescued Irish banks fall broadly into two categories: so-called “dead banks” – Anglo Irish Bank and Irish Nationwide Building Society – and two “pillar banks” that are either partially or completely owned by the government, Allied Irish Bank and Bank of Ireland.

When Dublin took over the two “pillar banks”, it spent about €30bn shoring them up and returning them to health, funds that came mostly though the national pension fund. But the pension fund’s most recent performance statement values the banks at only €9.4bn, meaning Dublin would take a significant loss even if the ESM were to take them over.

Irish banks

Recapitalisation and support (€bn)	
IBRC*	34.7
AIB/EBS	20.7
Bank of Ireland	4.7
Irish Permanent	4.0
TOTAL	**64.1**

** Anglo Irish Bank, Nationwide*

Source: Department of Finance, Dublin

“I don’t see anything that would lead me to revise a view that the chances of other European countries absorbing already crystallised losses in the Irish banks are approaching zero,” said John McHale, chairman of the Irish Fiscal Advisory Council, a watchdog set up by the government to advise on its fiscal policies. “My sense is politically this just isn’t going to happen.”

More complicated is the state of the dead banks, particularly Anglo Irish, which was wound down through a €31bn promissory note, effectively a government IOU.

The Irish government has been pushing for that loan, which now must be repaid in annual instalments of €3.1bn over the next 10 years, to be refinanced so the repayments are spread out over a much longer period or at a lower rate.

With the summit deal, that hope now becomes more real, officials believe. Mr McHale said the ESM could make a low-interest, long-term loan to Anglo directly to replace the promissory note.

Mr Hayes refused to give a figure on the amount of bank debt Dublin would seek to write down or restructure, but he said the aim of the negotiation was to make the country’s debt more sustainable.

“There is a general principle in economics that if you have a debt to GDP ratio below 90 per cent it provides a boost to the economy and if we want to get back to the bonds markets we need a more sustainable level of debt,” said Mr Hayes. Irish debt levels are due to peak at about 117 per cent of GDP next year.

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