

# ThePost.ie

## Why the banks need the guarantee

08 August 2010 By Cliff Taylor

It had the look of a coordinated approach. First, AIB chief executive Colm Doherty, and then Anglo boss Mike Aynsley last week called for a renewal of the state guarantee on bank liabilities.

*The reason is simple:*

without the continuation of this guarantee, Ireland's banks will not be able to keep raising the cash they need to remain in business.

Ireland's bankers know this and they are warning the EU Commission that it has to give the green light to continued state support of the banking sector.

The original guarantee on the bulk of outstanding bank liabilities - depositors and cash invested by bondholders - runs out at the end of September, two years after it was granted on the night when the government decided a guarantee was essential to save the banking system. A separate guarantee - which covers new debt raised by the banks - is due to run out at the end of December.

The banks' fears will be twofold. First, that the ending of the original guarantee will make it harder to hold onto large mobile deposits and, secondly, that not renewing the guarantee covering new debt will make it hard for them to raise fresh funds.

There has been a lot of talk about the number of bonds which the banks have maturing in September - Minister for Finance Brian Lenihan revealed in June that some €58 billion in longer term bank debt and €16.4 billion in shorter term borrowings fell due to be refinanced before October.

The immediate challenge facing the banks may not be that serious.

This is because they do not need to replace all the funding that matures, because they are shrinking in size and transferring assets to Nama. Smaller banks with smaller balance sheets need less cash to operate.

Also, according to estimates by bond experts Glas Securities, banks have already raised about €19 billion this year.

Finally, the bonds that the banks get from the government in return for Nama loans can be used as collateral to get cash from the European Central Bank (ECB) - one of the original key points of the Nama scheme.

So the banks have some leeway. However, they are a long way from where it was hoped they were going to be.

The intention earlier this year was that, by the end of the year, the Irish banking system would be recapitalised and would be able to raise cash normally on international markets - without the cover of a government guarantee.

The renewed bout of nerves in the markets following the Greek crisis has put paid to this timetable, meaning that, as the two chief executives said, banks were likely to need a continuation of state guarantees to allow them to raise more cash.

Delicate negotiations are already under way with the EU on this. The key issue is the scope of an extended guarantee. What existing liabilities will be covered, and what new debt will the banks be able to raise under the guarantee in 2011?

The EU will probably give the green light to some kind of extension, if only to try to wean the banks off their current reliance on funding from the ECB.

And, for as long as our banks find it difficult or expensive to raise cash internationally, they will be under pressure to restrict lending at home, which will make it more expensive by pushing up interest rates.