Only a matter of months after Ireland thought it had fixed its banking sector by nationalising Anglo Irish Bank, Anglo has needed another bail-out and Allied Irish Banks is to become a government-owned bank under government-appointed management.

Eight years after a rogue US trader racked up close to $700m in losses and almost brought down the bank, Allied Irish Banks has had to look to government for a lifeline after a catastrophic mishandling of Ireland’s recent property boom. And with no sign of the property market recovering, some believe there could be more trouble ahead for the country’s banks, which have been among the worst hit by the global financial crisis.

Allied Irish Banks, once Ireland’s largest public company, is having to raise €5.4bn (£4.7bn, $7.6bn) in a placing and open offer to shareholders to bring its core tier one capital ratio to 8 per cent by the year end.

On paper this is Ireland’s largest ever rights issue. But officials are under no illusion about the likely take up by ordinary shareholders. The shares closed on Friday at 39.5 cents, well below the 50 cent offer price.

Brokers calculate the government could end up with more than 90 per cent, with the capital hole the bank is seeking to cover 20 times bigger than the current market value of the bank.

The National Pension Reserve Fund is underwriting the issue. It already owns 18 per cent of Allied Irish Banks after the bank was blocked by other creditors from paying the coupon on the government’s €3.5bn preference share investment. The NPRF will convert €1.7bn of the preference shares and make a €3.7bn cash investment.

The ultimate structure will keep the state’s voting shares below 75 per cent in line with European Union listing requirements, and the government’s stated aim to retain a public flotation. This is seen as the government’s best route to disposing of its investment.

But this is nationalisation in all but name, which the authorities and the bank, have long sought to avoid.
How did Ireland’s biggest bank come to this state?

After Anglo Irish Bank, Allied Irish Banks had the biggest property exposure, taking €10.8bn of losses on the land and development loans now being transferred to the National Asset Management Agency, the government’s bad bank.

The past two years’ losses have wiped out the profits of the last four years of the boom, says Sebastian Orsi, analyst with Merrion Capital, a Dublin stockbroker. A Dublin fund manager adds: “They were expanding the property loan book at this incredible pace, yet what they were putting aside as provisions was falling.”

Some trace the problems at the bank – always perceived as more aggressive than rival Bank of Ireland – to its decision to set up special business acquisition units, which were under orders to poach the clients of competitors.

Karl Whelan, economics professor at University College Dublin, says: “They were explicitly tracking Anglo. You can see in their balance sheet through 2004 and 2005, they had decided to ratchet it up. A bank that is growing its loan book at more than 20 per cent should have set off red flags.”

Instead three months before the government had to step in with its blanket guarantee in September 2008, Allied Irish Banks, far from conserving capital, was lifting its dividend pay-out 10 per cent.

“They were clearly in denial about the problems,” says Mike Soden, a former Bank of Ireland chief executive and now member of the banking commission looking into the crisis.

Eugene Sheehy, then Allied Irish Banks chief executive, said he would “rather die than raise equity” to bolster the bank’s capital.

When the bank eventually realised its predicament, Colm Doherty, the acting managing director who, with Dan O’Connor, the chairman, will leave the bank as part of the reorganisation, was slow to execute key asset disposals.

In the end the government’s patience ran out.

On September 30, with all eyes on Anglo Irish Bank, Matthew Elderfield, the regulator, took the markets by surprise, demanding that Allied Irish Banks raise an additional €3bn to the €7.4bn estimated in March.

Investors were stunned as to how the bank’s position could have deteriorated so dramatically in six months.
The main reason was the increased Nama discounts – a haircut of 60 per cent is now being applied to the €13.5bn that has still to be transferred, against 45 per cent on the first tranche.

Asked by MPs last week if the banks had lied to Nama about losses, Mr Elderfield said: “I honestly don’t know.”

In its decision to downgrade Allied Irish Banks last week Standard & Poor’s cited the damage caused to the bank’s “reputation” which it acknowledged may take years to recover.

Only when the bank has regained the confidence of the markets can the government hope to dispose of its investment. And only then will the hapless Irish taxpayer be able to judge the final bill for the Allied Irish Banks bail-out.

Three-year fall from grace

February 19 2007 Allied Irish Banks’ share price peaks at €23.95

July 30 2008 AIB raises dividend 10 per cent

Sept 30 Dublin guarantees deposits and most bank debt of its six domestic lenders

October 23 Eugene Sheehy, chief executive, says “we would rather die than raise equity” as brokers estimate the bank will write down €4.5bn of bad loans by 2011

Feb 11 2009 Government announces €3.5bn preference share investment in AIB, securing assurances on lending levels, executive pay and treatment of distressed mortgage holders

March 2 AIB announces profits of €885m, after bad debts of €1.8bn

May 1 Eugene Sheehy, Dermot Gleeson, chairman and John O’Donnell, finance director, announce they will resign

May 13 Mr Sheehy and Mr Gleeson pelted with eggs at shareholder meeting to approve government recapitalisation

March 2 2010 First ever annual loss of €2.6bn after threefold rise in bad debts

March 30 Nama imposes 43 per cent discount on first tranche of AIB property loans. Regulator tells bank it needs to raise €7.4bn by year end or face nationalisation
September 10 AIB sells 70 per cent stake in Polish bank WBK Zachodni to Santander for €3.1bn

September 30 AIB to raise €5.4bn by converting 1.7bn of government preference shares and open offer at 50 cents a share, fully underwritten by the national pension reserve fund, after regulator tells AIB it needs an extra €3bn in capital by year end

October 5 AIB announces disposal of 22.4 per cent stake in M&T bank through public offering

October 8 AIB share price at 39.5 cents

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