Less wobbly now

The process of returning banks to private ownership begins.

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Will there be smiles all around, as ten banks in America begin to repay government capital that had been received during the depths of the financial crisis at the end of 2008? On Tuesday June 9th the Treasury gave approval to ten big banks, nine of which had earlier passed "stress tests" set by regulators, to allow them to repay money to the government's Troubled Asset Relief Programme (TARP). That should see a combined repayment of $68 billion: welcome funds for the government coffers, and also an encouraging indication that some banks, at least, are growing less wobbly.

Although the Treasury did not immediately identify which banks would start repayments, it is clear that those which passed the stress tests, including JPMorgan Chase, Goldman Sachs and Bank of New York Mellon, will be jostling forward in the queue to hand their money back. Such banks are keen to do so quickly, and loudly. By lowering the government's ownership of them they hope to reduce its influence over them. Paying back the state is also a way of advertising their regained strength.

"These repayments are an encouraging sign of financial repair, but we still have work to do," noted Timothy Geithner, the treasury secretary, on Tuesday. Signs of some recovery are clear enough. The financial system is more stable and profits and share prices are showing signs of life. The stronger banks have been able to sell new shares to raise cash—about $100 billion have been raised by American banks since the stress tests were conducted in May—and so can replace state funds without eroding their capital again. Mr Geithner, in turn, could use the money to pay down public debt or could recycle it into smaller banks which still need more equity.

Still, there is a long way to go. Paying off the first $68 billion is a healthy start, but western governments own roughly $450 billion in banks. If markets or the economy slump again, investors' appetite for new shares will evaporate. Of the ten banks, eight had been pressed by the government to take funds in October, amid efforts to shore up the banking system. Although some individual institutions may try to claim that they took the money unwillingly, government intervention was necessary to prevent the entire system from collapsing as banks were found to own hundreds of billions of dollars of hard-to-value assets.

Even today all banks remain plugged into government life support systems. Central banks provide generous collateral rules for borrowing, in an effort to provide banks with liquidity. Some banks have managed to issue debt without government guarantees, but the system needs to refinance some $25.6 trillion of wholesale funding by 2011: without an implicit state back stop this would be impossible. And the value of banks' assets is being sheltered by

central banks' asset purchasing programmes and in some cases flattered by more generous accounting rules. The truth is that the West has a thinly capitalised banking system that is being allowed to earn its way back to health. Save for defence and space exploration it is hard to think of a privately-run industry more dependent on the state.

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