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As Big Banks Repay Bailout Money, U.S. Sees a Profit

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Nearly a year after the federal rescue of the nation's biggest banks, taxpayers have begun seeing profits from the hundreds of billions of dollars in aid that many critics thought might never be seen again.

The profits, collected from eight of the biggest banks that have fully repaid their obligations to the government, come to about $4 billion, or the equivalent of about 15 percent annually, according to calculations compiled for The New York Times.

These early returns are by no means a full accounting of the huge financial rescue undertaken by the federal government last year to stabilize teetering banks and other companies.

The government still faces potentially huge long-term losses from its bailouts of the insurance giant American International Group, the mortgage finance companies Fannie Mae and Freddie Mac, and the automakers General Motors and Chrysler. The Treasury Department could also take a hit from its guarantees on billions of dollars of toxic mortgages.

But the mere hint of bailout profits for the nearly year-old Troubled Asset Relief Program has been received as a welcome surprise. It has also spurred hopes that the government could soon get out of the banking business.

"The taxpayers want their money back and they want the government out of our banking system," Representative Jeb Hensarling, a Texas Republican and a member of the Congressional Oversight Panel examining the relief program, said in an interview.

Profits were hardly high on the list of government priorities last October, when a financial panic was in full swing and the Treasury Department started spending roughly $240 billion to buy preferred shares from hundreds of banks that were facing huge potential losses from troubled mortgages. Bank stocks began teetering after Lehman Brothers collapsed and the government rescued A.I.G., and fear gripped the financial industry around the world.

American taxpayers were told they would eventually make a modest return from these investments, including a 5 percent quarterly dividend on the banks' preferred shares and warrants to buy stock in the banks at a set price over 10 years.

But critics at the time warned that taxpayers might not see any profits, and that it could take years for the banks to repay the loans.

As Congress debated the bailout bill last September that would authorize the Treasury Department to spend up to $700 billion to stem the financial crisis, Representative Mac Thornberry, Republican of Texas, said: "Seven hundred billion dollars of taxpayer money should not be used as a hopeful experiment."

So far, that experiment is more than paying off. The government has taken profits of about $1.4 billion on its investment in Goldman Sachs, $1.3 billion on Morgan Stanley and $414 million on American Express. The five other banks that repaid the government — Northern Trust, Bank of New York Mellon, State Street, U.S. Bancorp and BB&T — each brought in $100 million to $334 million in profit.

The figure does not include the roughly $35 million the government has earned from 14 smaller banks that have paid back their loans. The government bought shares in these and many other financial companies last fall, when sinking confidence among investors pushed down many bank stocks to just a few dollars a share. As the banks strengthened and became profitable, the government authorized them to pay back the preferred stock, which had been paying quarterly dividends since October.

But the real profit came as banks were permitted to buy back the so-called warrants, whose low fixed price provided a windfall for the government as the shares of the companies soared.

Despite the early proceeds from the bailout program, a debate remains over whether the government could have done even better with its bank investments.

If private investors had taken a stake in the banks last October on par with the government’s, they would have had profits three times as large — about $12 billion, or 44 percent if tallied on an annual basis, according to Linus Wilson, a finance professor at the University of Louisiana at Lafayette, who analyzed the data for The Times.

Why the discrepancy? Finance experts say the government overpaid for the bank assets it bought, because its chief priority was to stabilize the teetering financial system, not to maximize profit.

“Had these banks tried to raise money any other way, they probably would have had to pay quite a bit more than the government received,” said Espen Robak, head of Pluris Valuation Advisors, which analyzes the value of large financial institutions.

A Congressional oversight panel concluded in February that the Treasury paid an average of 34 percent more than the estimated fair value of the assets it received.

Of course, many finance experts suggest that the comparison is academic at best, because there is no way to know what might have become of the banks or the financial system as a whole had the government not acted.

“Taxpayers should heave a sigh of relief that the investment in the banks protected them from even more catastrophic losses from more bank failures,” said Aswath Damodaran, a finance professor at the Stern School of Business at New York University.

A more direct comparison of profits can be made with the investment performance of other governments that poured money into ailing banks last fall.

The Swiss government, for example, said last week that it had pulled in a handsome profit for taxpayers on a $5.6 billion bailout it gave to UBS, the troubled Swiss bank, at the height of the financial crisis in October. The government netted $1 billion on its investment, a gain equal to a 32 percent annual return.

“They are substantially in the money,” Guy de Blonay, a fund manager at Henderson New Star in London, said after the announcement.

American taxpayers could still collect additional profits on their investments in two other big banks that have repaid their preferred stock but not their warrants: JPMorgan Chase and Capital One. They are expected to yield over $3.1 billion in gains for the Treasury in the next month or so, although the full tally will depend on how much they will pay to buy back their warrants.

And the government is owed about $6.2 billion in interest payments from banks that have not yet repaid their federal money.

But all the profits taxpayers have won could still be wiped out by two deeply troubled institutions. Both Citigroup and Bank of America are still holding mortgages and other loans that were once worth billions of dollars but whose revised values are uncertain. If they prove “toxic” because they cannot attract buyers, they could leave large holes in the banks’ balance sheets.

Neither bank is ready to repay its bailout money anytime soon, even though the banks’ stock prices have surged in the last month, leaving the government sitting on paper profits of about $18 billion between them.

Eric Dash contributed reporting.