The Banking Inquiry

Why Ireland Experienced a Systemic Banking Crisis

Alternative Analysis and Conclusions to the Report of the Joint Oireachtas Committee of Inquiry into the Banking Crisis

By Joe Higgins TD, Member of the Joint Committee[1]

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Extreme Profiteering driven by corporate greed drove the property bubble and caused the crash;

Bubble Governments of Taoiseach Bertie Ahern, Tánaiste Mary Harney, Finance Ministers McCreevy & Cowen served the interests of bankers/developers Not those of ordinary people;

Enda Kenny, Fine Gael Leader, was a silent non Opposition

Witness after witness at the Banking Inquiry, including bankers and developers themselves, attested to the kind of cut throat competition between them for profit that drove the reckless lending practices that inflated the property/banking bubble and led to the disastrous economic crash. Dermot Gleeson, the Chairman of AIB from 2003 to 2009 testified as to how his bank aped the methods of Anglo Irish Bank which was lending recklessly to developers and raking in major profits. He maintained that they had a problem of:

> Anglo being held up to us as an exemplar…Commentators in Ireland and abroad repeatedly said, "Anglo is the best bank. Why can't you be more like Anglo?" It was determined by one international consultancy to be the best bank of its size in the world. It was the darling not just of the Irish but of European stock exchanges generally…

Ethna Tinney, who was an independent Non-Executive Director of EBS 2000-2007, told the Inquiry:

> The belief that there were substantial profits to be made for the society from these developments led us to emulate our peers…There was a sort of feeding frenzy as the banks clambered over one another to get a piece of the action, especially as new foreign banks had entered the market as competitors…There was a sense that we were becoming a minnow as

[1] **With major technical assistance and research by Diana O'Dwyer**

> INBS expanded its lending and started to post profits that were up to five times the profits we were posting.

Ms Tinney was highly critical of practices such as securitisation referring to herself having an image of it 'as a shark eating its own entrails' She further claimed that 'The banks have absolutely no sense of guilt about what they have done. And if left unchecked, they are going to do it all over again.'

The extreme drive for profits was encapsulated in the figures given to the Inquiry whereby the six banks eventually covered by the Guarantee, increased lending exponentially from €120 billion in 2000 to almost €400 billion by 2007, raked in €25 billion in profits from 2002 to 2008 and paid those banks Chief Executives an astounding total of €71 million in salaries and bonuses. This was then adversely mirrored in the disastrous €65 billion these banks lost in the crash.

The political leaders of the Fianna Fail/ Progressive Democrat Government 1997 -2007 relentlessly pushed the deregulation in financial services that resulted in this competitive race to the bottom in banking standards as major banks vied for profits. Taoiseach Bertie Ahern told an Irish Banking Federation lunch in March 2006*;* 'the Government is very conscious of its role in assisting you to maintain a healthy bottom line . . .there is a need to be more balanced and less negative about the essential services you provide.'

In March 2007, Mr Ahern was positively touting Ireland as a deregulated state for bankers when he told a breakfast meeting of the Financial Services Industry in New York, 'Our commitment to supporting foreign direct investment is absolute. Ireland is very lightly regulated compared with most of our European colleagues.'

Brian Cowen who became Finance Minister in 2004, was as enthusiastic as his Leader. In a speech to the Institute of Bankers in Ireland annual dinner on 2 November 2006, he said:

> But, in my view it is the innovation coming from within the sector which is the most remarkable driver of change. Increasingly sophisticated derivative products seem to be arriving daily as a sector seeks to become ever more professional in the way it manages and hedges its risks and chases after that elusive higher yield.

Billionaire Warren Buffet described the same derivative products as 'time bombs' and 'weapons of mass destruction.

Brian Cowen continued in what can only be described as an embarrassingly obsequious tone:

> Of course, not all of these brave new initiatives are successful. It's a hard game, but there's all to play for. Of course, that's easy for me to say because you are players on the field and I'm just an ardent supporter on the sidelines. I will continue to wear your colours.

Mr Cowen's predecessor, Charlie McCreevy, who was Finance Minister from 1997 to 2004 agreed at the Inquiry that he was a 'champion of the free capitalist markets'. He told the Financial Regulator in 2005 (now as EU Commissioner):

> Don't try to protect everyone from every possible accident. . . .many of us in this room . . . were part of the 'unregulated generation' – the generation that has produced some of the best risk takers, problem solvers and inventors.

The biggest political party in opposition in the Dail during the bubble was Fine Gael. At his appearance at the Inquiry, Enda Kenny, Fine Gael Leader from 2002, wasn't in a position to point to a single instance where he had demanded restrictions or regulation on the profiteering that was rampant in the property market.

Dismal failure of Central Bank/Financial Regulator rooted in deregulation mindset of Fianna Fail/PD Government;

Regulator must take full measure of responsibility but political establishment must not be allowed to scapegoat:

I have no doubt that the Report of the Joint Committee which finds that the Regulator took no enforcement action against any banks for excessive lending between 2000 and 2008 will be seized on opportunistically by the political establishment – especially Fianna Fail and the Progressive Democrats – to make the Regulator the scapegoat for the bubble and crash. In fact the evidence available to the Committee demonstrated that the most senior politicians of the day championed rampant deregulation in the financial services sector to enable the banks to make massive profits.

In 2003, the Fianna Fail/PD Government, gave the Financial Regulator a legal responsibility for the expansion of the financial services sector while at the same time being supposed to regulate it. This gave rise to the spectacle of the Regulator organising international 'roadshows' to tout for international banks coming to Ireland at the same time as it was supposed to control their profit seeking activities. In fact assisting the banks to make super profits was a constant concern of these politicians.

It shouldn't come as a surprise then that the Financial Regulator was promulgating the same message as the Government to which it was responsible when it said in 2005; 'We as Regulator, will not introduce or impose unnecessary regulatory burdens that will affect the continued competitiveness of our financial industry and will minimise the impact of such burdens coming from Europe.'

Again in its 2006 Annual Report the Regulator showed it was merely carrying out the wishes of the political leadership when it stated,

> we design and operate a regulatory regime conducive to an internationally competitive financial services industry . . . that is profitable and growing in both the domestic sector and the international sector based in Ireland. . . We provide world class service to financial institutions in all our dealing with them.

In not regulating, the Regulators were taking their lead from the political leadership of the State. On top of that, and really because of it, the numbers of staff assigned to track the major banks was derisory. Mary Burke, who was Head of Supervision at the Financial Regulator gave evidence to the Inquiry that only three FR staff members had responsibility for Bank of Ireland and Anglo combined while only two were tracking Allied Irish Banks and IL&P.

Government supposed to put interest of ordinary citizens first but FF/PD Government betrayed that trust to serve interest of bankers/speculators

At Election time the major political parties pledge to represent the interests of the majority in the State, the ordinary men women and children who make up society. During the property bubble the FF/PD Government utterly perverted that pledge.

The workings of the capitalist market allow cabals in the financial markets and in the property industry to gamble for super profits if conditions allow. It is considered a right to engage in flagrant speculation in building land even if this enriches the speculator at enormous cost to society. This was central to the rocketing of house prices in the bubble which evidence to the Inquiry showed increased stunningly by the equivalent of the average industrial wage EACH year for the ten years from 1996 to 2006. The championing of deregulation in the financial markets by such as Bertie Ahern and Brian Cowen and which gave financiers free reign to profit at the expense of society was enshrined in legislation. The laws that legitimised speculation and profiteering and the personal and corporate greed involved, were fashioned in Dáil Éireann under successive governments and voted for by the majority of Dáil deputies and Senators because they were believers and advocates for the capitalist ethos that underpins the economic system in which those markets play a pivotal role.

When questioned about the nature of their relationship with property developers as illustrated by their annual outing to the Galway Races and the Fianna Fail hospitality tent, the former Fianna Fail Leaders strongly denied that they were in any way influenced by the demands of property developers. Most ordinary people will find this simply incredible.

The Reckless Behaviour that inflated the bubble and caused the crash should have been criminalised:

Politicians, Bankers, Bondholders and Developers responsible for the bubble should have been facing jail instead of golden pensions:

It is often bemoaned that a miniscule number of former bankers - and no developers - have been charged with any crimes arising out of the blowing up of a gargantuan bubble of property speculation up to 2008 that saw six Irish banks shovelling out massive loans and reaping massive short term profits before an inevitable and catastrophic crash that devastated the lives of countless people in this State.

This is usually put down to a lack of any will among the political, economic and legal establishment to call former bastions of the same establishment to account. While this is undoubtedly true, the much more fundamental reason is that the vast majority of transactions that inflated the bubble over more than ten years, and saw fabulous short term profits for speculators and bankers, were quite legal. It was, and still is, legal to engage in the most outrageous speculation in urban building land. It was quite legal, as Quinlan Private did in 2001, to buy 11 acres of building land in Stillorgan for €32 million on behalf of a group of rich individuals and, without putting a brick on top of another, to sell it four years later for €85 million, a speculative gain of €53 million.

It was perfectly legal to put such speculative profits on the shoulders of young people buying homes and shackle them into mortgages of thirty five or forty years duration with an horrific level of monthly mortgage payments. Because this was how 'the markets' worked and a consistent majority in the legislature politically prostrated before those markets, powerful institutions and individuals were fully within the law in profiteering at will even if this meant that one of the most basic human needs, a modest place to live, was denied to very many and, for others, came at an appalling cost in human terms including the stress of trying to pay for the speculative gains of developers and bankers and beyond them the bondholders and the financiers in the European financial markets, - faceless, unelected and unaccountable to those they exploited.

The actions of the bankers, developers and the bondholders who financed them to inflate the bubble were blatantly anti-social. They caused enormous stress to a generation of young home purchasers during the bubble. They skewed the economy toward parasitic speculation and away from productive investment. As the bubble inevitably crashed they caused traumatic dislocation with savage cuts in public services, massive unemployment, the forcing out of their country of hundreds of thousands of working people.

The actions that caused this massive destruction were largely legal. By any standards they should have been seriously criminal. Had these activities been subject to laws that would have protected the big majority in society, all the central actors in the inflation of the bubble from bankers to developers to financing bondholders and the politicians that facilitated them, would have been facing criminal sanction and imprisonment instead of enjoying gold plated pensions.

As the Public Hearings were broadcast and the wide cast of bubble and crash actors came before the Committee, it was remarked to me again and again by ordinary people who were the victims of their actions, how much it galled to see how utterly immune they were to any legal sanction because the whole system had been legally rigged in their interests.

Banking & Home Provision should not be subject to exploitation and profiteering but should be public services

The disaster of the bubble and crash scream out that critical industries such as banking and the provision of homes should not be the subject of speculation, exploitation and profiteering by private interests. Hundreds of thousands of people are still suffering very severe hardship because that was, and is, the case until now. The horrific current housing and homelessness crises is a direct result. Banking and the provision of homes should be public services run in the interest of the needs of society as a whole.

The soft landing alibi - a big lie

The major excuse given to the Inquiry by developers, regulators, establishment politicians and international agencies for not taking strong action at any stage to stop the madness was that one and all expected a 'soft landing' to the property boom. The implication is that had such an end to the boom occurred, the policies and practices they followed would have been vindicated. That means it would have been fine to gouge a generation of young workers with a fourfold increase in the price of a new home in ten years necessitating them taking out 35 to 40 year mortgages with draconian levels of monthly repayments - all for the basic human right of a modest home.

More fundamentally, however, to believe that all expected a ‘soft landing’ is to believe a big lie. To believe this, you have to ignore all the past history from all over the world of previous property bubbles and busts, including recent crises in the US, UK and Scandinavia, as well as models used by the industry itself of the property market cycle. An alternative explanation is that bankers and property speculators did know on some level that a crash was inevitable but were so blinded by the huge profits they were making that hardly any of them ’got out on time'. Evidence presented to the Inquiry showed some estate agents were warning their clients off Irish commercial property from 2005, while from 2004 many of the big developers were diversifying outside of Ireland – which was one reason a third of the loans that ended up in NAMA were for commercial property overseas. Even Anglo made some half-hearted efforts to rein in Irish development lending in 2006.

Meanwhile an elite consensus was constructed around the fairy-tale of a ‘soft landing’ by property and banking interests and their political supporters, with the eager assistance of a media dependent on property advertising. This encouraged first-time buyers to keep taking out huge mortgages and helped keep the bubble going for bankers and developers until the last possible minute. Dissenters who called the crash were pilloried as unpatriotic ‘merchants of doom’ ‘talking down the economy’. Taoiseach Bertie Ahern even said they ‘should go off and commit suicide’.

The Central Bank was less crassly offensive but equally committed to not ‘frightening the horses’. Imprisoned by the ‘pro-cyclical boom/bust nature of capitalism, all concerned downplayed the crash for fear that taking their heads out of the sand and admitting the truth would cause a loss of ‘confidence’, spread ‘contagion’ and undermine profits. This profoundly undemocratic aspect of the capitalist economic cycle is of course treated as the natural order of things, no more avoidable than the weather. Like ancient peoples prayed for the coming of the rains or the ending of the floods, today we pray the ‘confidence fairy’ will charm the gods of the markets.

Significant sections of the Media not only glamourised and cheerled the bubble but were actors in it

Denials by senior media representatives at the Inquiry Public Hearings that they played no role whatever in the inflation of the property bubble, have no credibility. In fact major media outlets fawned on the major bankers and developers, never questioned the morality of the profiteering and speculations that was going on or carried out any serious investigation into the level of exploitation in the housing market and the social consequences that resulted. Significant sections of the media made a fortune from the property industry during the bubble, with glossy property supplements in the newspapers and ‘property porn’ programming on RTE

The *Irish Times* told the inquiry that its revenue from property advertising had increased along with the bubble, from €10m in 2002 to €22m in 2006, when it reached 17% of its overall income. The comparable figure at Independent News & Media was 9%, with property revenues increasing 89% from 2002-2007. Both of the two main newspapers also bought property websites; the *Irish Times* famously paid €40m for myhome.ie in 2006. This gave them an additional, direct investment in the performance of the property market. They were actual players in the property market.

The former editor of the *Irish Independent*, Gerry O'Regan was highly critical of myself for daring to suggest that media like his cheerled the property bubble. He claimed that 'there was no conscious attempt on my part, or on the part of the newspaper, to fuel what has been described as the property boom'. Independent Newspapers in fact sponsored the *Irish Property Awards* every year until 2008. The 2004 ceremony was described in its pages as 'A glittering showcase of the cream of Ireland's property and development industries…attended by a record 1,000 property professionals with several hundred disappointed'.

In 2007, 'Irish property deal of the year' was awarded to the Irish Glass Bottle site, which ended up costing taxpayers hundreds of millions of euro, while five of the seven award-winning developers were among the top ten debtors to Anglo.

The *Property Awards* reflected the INM's generally obsequious coverage of developers, who were celebrated as gods with the 'Midas touch' and credited with restoring Ireland's national honour after its colonial past. Rather than signalling that the commercial property market here was 'overheated', the fact Irish investors were spending twice as much in the UK as in Ireland was lauded as evidence of the growing prowess of Irish capitalists, who were finally taking their rightful place among the ruling classes of Europe!

My reason for not signing the Committee Report

The reason I refused to sign the final Report is because of a fundamental difference with the majority of the Committee as to where lies the responsibility for the property and banking bubble and crash. The ideological framework of the big majority of the members of the Committee of Inquiry and the political parties to which they belong meant that a most fundamental question wasn't posed let alone answered. That is why a small cohort of bankers, bondholders and developers should be allowed to wield massive economic power in pursuit of private, corporate profit and in the process inflict incalculable economic and social destruction on society. It is why the political establishment, not only deferred to this cohort, but in fact served their interests as they chased maximisation of profits. The ideological approach of the Joint Committee majority meant that many painful symptoms of a disease were examined in great detail but not so the root cause and source of the infection.

While the final Report has many observations on the frenetic rate of lending by banks to speculators and developers, there is no objection in principle to the free reign given to private individuals and corporations to control crucial swathes of economic activity such as development and construction and hold society to ransom for private profit.

The Terms of reference of the Banking Inquiry mandated the Committee 'to inquire into the reasons Ireland experienced a systemic banking crisis, including the political, economic, social, cultural, financial and behavioural factors and policies which impacted on or contributed to the crisis'. Several other individuals – Nyberg, Regling & Watson, Wright, The Comptroller & Auditor General, Honohan – have already produced reports into various aspects of the reasons for the crisis. These reports, like the Banking Inquiry Report, majored on the lending practices of the banks, especially the concentration of massive loans into the property sector as they poured money borrowed from the European financial markets into the arms of the developers leaving themselves fatally exposed to a crash. Not surprisingly, because all were conducted by various arms or representatives of the establishment, they in no way challenge the workings of the markets.

The majority of the members of the Joint Committee were not in the Oireachtas during the bubble but they emanate from the same ideological pool and political parties that were, and therefore see no issue with the right granted to players in the markets to speculate and maximise profits to the limits of 'what the market will bear'. For us the markets constitute a dictatorship of capitalist financiers over the lives of ordinary people dictating that corporate profit comes before the needs of society. This is an absolutely fundamental difference.

Inquiry legislation a serious hindrance

The Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013 under which the Banking Inquiry was held, was a serious hindrance to the kind of inquiry into the property bubble and banking crisis that the Irish people were entitled to. Those witnesses who were compelled to come before the Committee, because they were central to the inflation of the crazed speculative property and banking bubble and the resultant economic crash, were shielded by the legislation from the full force of what should have been a rigorous and radical questioning. This was evident in the bizarre situation of the Oireachtas' own lawyers being in a position of constantly monitoring the line and tone of the questioning conducted by the Members, lest any witnesses take offence and obstruct the Inquiry by resorting to the High Court arguing that they weren't receiving 'fair procedures'.

Moreover, it is simply untenable that further Inquiries can be held under this legislation where no adverse finding can be made against a person where there would be overwhelming evidence to support such a finding and only that person's denial against.

Public hearings were valuable

I believed that what was needed for a radical examination of the crisis and its causes was a broad based 'People's Inquiry'. However, once the Fine Gael/Labour Government finally decided to establish a Committee under the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013, and notwithstanding the inadequacies of the legislation, I resolved to bring forward and pose during the Inquiry, the questions in the minds of a majority of the ordinary people in society who have suffered grievously as a result of the crisis.

In particular and notwithstanding the restrictions on questioning in the Public Hearings, there was great merit in requiring many people and institutions who played key roles in the period in which the property bubble was inflated and during the crash and afterwards, to be questioned in full view of the public. Despite the frustrations caused by the legislation, I felt that I was able to pose many key questions and that this was the most meaningful and purposeful part of the Inquiry.

Tribute to Staff

The year and a half of work involved in the joint Committee entailed an enormous commitment in terms of time and effort by the elected members and staff. At end September 2015 when public hearings had ended, 131 witnesses had been heard at 111 such hearings. Apart from that the Joint Committee had held 70 private meetings. Over half a million pages of evidence had been submitted by participating parties. An average of about 45 staff worked on the Inquiry.

However the timeframe into which the Government shoehorned the work of the Inquiry put unbearable pressure on the elected members but more especially on the staff both the individual staff assigned to each member and the Inquiry staff whether permanent public service workers or staff taken on especially for the Inquiry. This caused some considerable problems and in addition to the problems caused by the legislation, affected the quality of the investigation. This was partly what prompted complaints by a 'whistleblower' member of staff who raised some quite legitimate points notwithstanding that a Senior Counsel engaged by the Houses of the Oireachtas Commission to examine those and other complaints didn't uphold them.

Our Analysis and Conclusions

Causes of the Crisis

International context, Chapter 1:

*A key context in the creation of the massive financial/property bubble in Ireland up to 2007 and subsequent crash was the policy of successive Irish governments in developing the State as an international haven for capital from higher tax and intrusive regulation. This allowed the ballooning of loans from the European financial markets into the Irish banks as they competed with each other in reducing credit control as these funds were passed on for speculative development.

*The debate about whether the crisis was primarily home-grown or international in nature is misconceived. The crash resulted from Ireland's peripheral insertion in the global capitalist system at a time of crisis. Ireland was particularly badly hit because of its over-reliance on Foreign Direct Investment and underdevelopment of the indigenous economy, which led it to deregulate finance to attract in foreign capital and also to over-investment in non-productive areas of the economy i.e. property.

The Property Bubble, the Banks, and the Relationships Beneath the Bubble Chapters 2 & 3:

* The fundamental basis of the property bubble was that greed for super profits by major landholders, bankers and developers was facilitated by the capitalist ethos underpinning the legislation governing banking, land speculation and construction development.

*Private corporations, land speculators and speculators on the financial markets were enabled to put profit maximisation before the needs of the majority in society.

*The constant of a right wing majority in Dáil Éireann, ideologically committed to the capitalist market system, before and during the bubble, meant that legislation enacted facilitated private greed at huge cost to social needs.

*The crisis was primarily caused by profit-seeking, speculation and profiteering by banks, builders and property developers, both in Ireland and internationally. This led to reckless lending and a giant credit bubble that drove up the cost of development land, construction costs and house prices.

*Commercial property lending to developers, builders and property investors rather than borrowing by ordinary owner-occupier mortgage holders was what brought down the banks. AIB, BOI & Anglo had combined commercial property loans of €8.63 billion in 1998. By 2008 the combined total was €146.7 billion – an increase of 1,600%

*Profit-seeking led to destructive competition between banks as they sought to win market share from each other. Competition led to banks cutting interest rates and making lower margins so that the only way to compensate was to recklessly increase the volume of lending and make riskier loans. All this was exacerbated by the entry of foreign banks into the Irish market whose large overseas businesses meant they could afford to make a loss temporarily in the Irish market to enable them to win market share.

*Competitive deregulation within the financial services sector was an aggravating factor. This was pushed by government to attract foreign direct investment (FDI) and boost the profits of domestic banks and Irish capital. The banks themselves progressively cut their lending standards to compete with their rivals.

*Lobbying by the financial institutions had a strong influence on deregulation. The banks in general had excessive influence over government and Central Bank/Financial Regulator policy

*The dominant neoliberal ideology dictated that the government should not interfere in markets apart from encouraging competition between financial institutions. As the Nyberg Report puts it: '. . .the paradigm of efficient markets provided the intellectual basis for the assumption that financial markets, left essentially to themselves, would tend to be both stable and efficient.' This led to light touch regulation also referred to a 'principles based' regulation. This really meant 'trusting' the banks to regulate themselves – all leading to the promotion of even fiercer competition, thereby facilitating the banks' profit-seeking and the growth of a credit bubble.

*Ireland's peripheral status within the European Union was shown by successive government's subservience to the ECB even when its diktats placed a huge burden on working people.

*A small group of capitalists profited from the bubble and caused the crash.

*An excess of liquidity – cash – on global money markets because of rising wealth inequality fuelled the property bubble and then caused the crash by giving banks the funds with which to recklessly expand their lending in pursuit of higher profits.

*Excessive government spending was not a cause of the crisis. Ireland had the lowest rate of public spending as a percentage of GDP in the EU-27 throughout the pre-crisis period.

*Property-related tax breaks which were really just tax shelters that incentivised investment in unproductive activity, sucking investment away from economically or socially useful purposes were an important direct factor in the bubble and the crash. Neither the bubble nor the crash would have been as large without them but there would still have been a bubble and a crash, as happened internationally.

*Over-reliance on property-related taxes was another factor in the severity of the crash. However, the restructuring of the tax base since has shifted this cost onto workers and the poor, rather than increasing taxes on corporations and the wealthy, which are more 'sustainable' sources of taxes from the perspective of the majority of the population.

*The media's dependence on property advertising, capitalist ownership, neoliberal ideological conformity and shared interests and identification with capitalist interests led it to cheerlead the bubble and to largely ignore signs of the oncoming crash.

Other conclusions and recommendation including the following:

*The Guarantee and Solvency of the Banks
The government and regulatory authorities had ample evidence to strongly suspect that both Anglo and INBS were facing imminent future insolvency and that without recapitalisation they would fail.

The two main banks – AIB and BOI – were largely responsible for the content and coverage of the guarantee.

*The Cost of the Crisis
Direct & Indirect, Gross & Net – Measuring the cost of the crisis should include the cumulative cost of austerity, including the €150bn in cumulative tax increases public spending cuts[2].. The cost of the crisis could have been greatly reduced if the government had made different choices and implemented different policies. Billions could have been saved by burning bondholders.

*Who Paid For It & Who Should Have Paid For It
Despite the fact that a very small group of people profited from the bubble and caused the crash, ordinary people have borne the brunt of the crisis. This is shown by statistics on rising income and wealth inequality since the crash, falling wages and living standards, and increased wealth for the top 300.

Major Policy Changes needed

*The Need for a Publicly Owned and Democratically Run Banking System to enable: rational planning of the economy for people's needs not profit; productive investment rather than speculation; and low cost personal finance. This obviously means that AIB and PTSB should not be privatised and that the government should not sell off its shares in BOI either.

*The need to outlaw speculation and profiteering in urban building land.

*The Need for a Publicly Owned and Democratically Run Construction Industry to enable rational planning of the economy for people's needs not profit and productive investment rather than speculation.

Joe Higgins TD, January 27, 2016

[2] Honohan, "STATEMENT BY PATRICK HONOHAN TO THE BANKING INQUIRY 'Nexus Phase,'" 8 n18.

Chapter 1 The Irish Bubble in a Global Context

It's become commonplace to try to separate the roots of the banking crisis into 'domestic' or 'international' causes. Regling and Watson[3] declare 'Ireland's banking crisis bears the clear imprint of global influences, yet it was in crucial ways "home-made"' and 'While global and domestic factors thus interacted in mutually reinforcing ways, it is feasible to disentangle the main "home-made" elements'. Former Central Bank Governor, Patrick Honohan[4], claims 'three quarters' of the damage was caused by 'local factors'.

In fact, it's not possible to disentangle 'domestic' and 'international' causes in this simplistic way. Both are rooted in a global capitalist system in which Ireland acts as a haven for capital from tax and regulation, which means we need to look at the Irish crisis in a global *context.* This takes on a special significance in the context of the banking crisis as the standard line from the 2007-2011 Fianna Fáil/Green government was to blame the 'international' liquidity crisis or credit crunch rather than the underlying 'domestic' insolvency (bad loans) of the Irish banks. In reality, 'international' and 'domestic' factors and liquidity and solvency were intertwined. The head of the IMF's mission to Ireland, Craig Beaumont, said as much in his submission to the Inquiry, declining to rank 'international' and 'domestic' factors and merely stating that 'a complex combination of domestic and international factors was at play in Ireland'[5].

Ireland's international role as a 'capital haven' reflects the longstanding 'development strategy' of successive Irish governments. It is rooted in the economic interests of Irish and foreign elites, who both benefit from it. Grasping for a way out of post-colonial underdevelopment which left the new Irish State largely agricultural with few indigenous industries, and being utterly incapable of developing an independent economy, Irish elites happened on the 'capital haven development strategy' in the 1950s[6]. This meant basing the economy on luring foreign capital here with very low headline corporate tax rates and even bigger tax loopholes like the notorious 'Double Irish', which allow multinationals to avoid paying tax. Increasingly, it also meant providing a haven to foreign and domestic capital from regulation as well, which played a significant role in the banking collapse. Crucially, this benefited both foreign and domestic capital as the tax breaks and freedom from regulation also applied to Irish companies and banks.

This has meant starving the country of the taxation resources it needs to develop: producing one of the lowest tax takes as a percentage of GDP in the EU, a culture of corruption, and an ecosystem of lawyers and accountants that devise elaborate schemes to avoid tax and regulation. Before the

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[3] Klaus Regling and Maxwell Watson, "A Preliminary Report on the Sources of Ireland's Banking Crisis," 2010, 5, http://www.betterregulation.com/external/A%20Preliminary%20Report%20on%20The%20Sources%20of%20Irelands%20Banking%20Crisis.pdf.

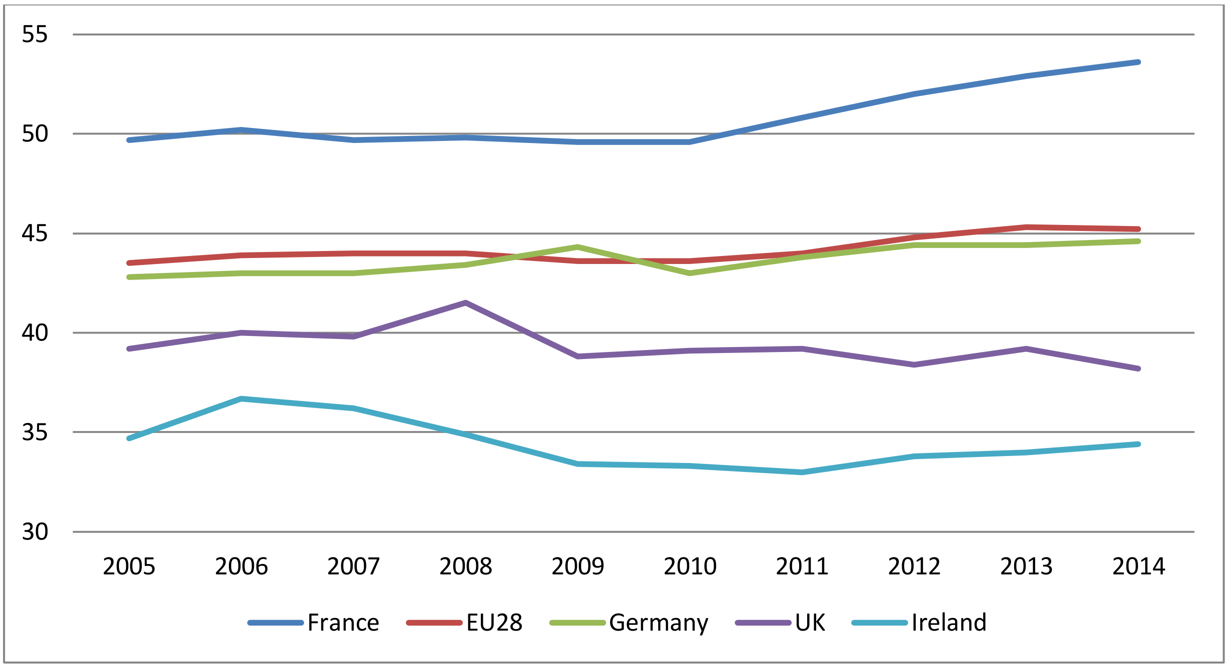
[4] Patrick Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," May 31, 2010, 32, http://www.bankinginquiry.gov.ie/The%20Irish%20Banking%20Crisis%20Regulatory%20and%20Financial%20Stability%20Policy%202003-2008.pdf.

[5] "Written Statement of Craig Beaumont," October 2015, 24.

[6] Joseph Ruane, "Ireland's Multiple Interface-Periphery Development Model: Achievements and Limits," SSRN Scholarly Paper (Rochester, NY: Social Science Research Network, August 10, 2010), http://papers.ssrn.com/abstract=2198933.

crisis, in 2005, government revenue was 34.7% of GDP, 8.8% below the EU average. After it, in 2014, it was 34.4%, or 10.8% below (Table 1.1). In 2005, only Latvia, Lithuania and Romania had lower levels of government revenue; in 2014 only Lithuania and Romania. By contrast, the major European capitalist powers, Germany, France and the UK, have consistently had much higher levels of government revenue (Table 1.1)[7]. Germany generally brings in around 10% more than Ireland. This is because their economies are primarily based on 'real' economic development rather than 'capital haven development', which doubly cannibalises revenue as a percentage of GDP by exaggerating the GDP booked here for tax purposes and levying minimal tax on it. It has other distorting effects too, such as making the economy appear larger and healthier than it is and our debt burden lower.

Figure 1.1 Total Government Revenue as a % of GDP - EU vs. Ireland (Eurostat)



Being a haven for domestic and international capital led to 'the costliest banking crisis in advanced economies since at least the Great Depression'[8]. To understand *why*, we need to look at the interconnection of international and domestic factors in an evolving global capitalist system. In response to the economic crisis of the 1970s, capitalism globally entered into a long process of neoliberal restructuring. As Professor Terrence McDonough outlined to the Inquiry[9], this involved: globalisation, 'financialisation', 'repression of labour' and the neoliberal 'free market' ideology to justify them. He went on to explain that 'The same set of institutions…would eventually create the most serious economic crisis since the Great Depression.' [10] In this new global context, Ireland's

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[7] Eurostat, "Government Revenue, Expenditure and Main Aggregates," December 17, 2015, http://appsso.eurostat.ec.europa.eu/nui/submitViewTableAction.do.
[8] Luc Laeven and Fabian Valencia, "Systemic Banking Crises Database: An Update" (IMF, 2012), 19–20, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2096234.
[9] Terrence McDonough, "Opening Statement to the Banking Inquiry," February 26, 2015, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/02/Opening-Statement-Terrence-McDonough.pdf.
[10] Ibid., 3.

‘capital haven development strategy’ initially became apparently more successful but also increasingly dangerous.

Globalisation

Professor McDonough defined globalisation as:

> “the disintegration of production processes into their component parts and the location of each of these components in that area of the world most congenial to making profits. The production process is then reintegrated through free trade across borders.”[11]

The main way Ireland is presented as a part of the world ‘most congenial to making profits’ – or as Enda Kenny likes to call it, ‘The Best Small Country in the World To Do Business’[12] – is by marketing it as a haven for capital from tax and regulation. This is particularly the case for international financial services, enticed here to cut costs and boost profits. Fintan O’Toole summarises this in his book, *Ship of Fools*[13]:

> The IFSC, with its low corporation tax rates, tax exemptions on dividends and interest payments, and access to Ireland’s large range of bilateral tax treaties, was attractive in this light. The 12.5 per cent tax rate was a little over a third of that prevailing in the US and most of Western Europe. By 2002, Ireland had become the single largest location of declared pre-tax profits for US firms (followed, aptly, by Bermuda). The other attraction, though, was the lack of regulation, or what the IDA called “a flexible and business focused tax and regulatory system.

The conscious political strategy behind this is evident in the Department of the Taoiseach’s 2006 Strategy for international financial services, which touts a ‘Flexible and Sound Regulatory Environment’ and ‘Attractive Legislative and Fiscal Environment’ as Ireland’s first two ‘Competitive Advantages’. It then helpfully alerts financial firms to ‘the opportunity to input each year, through the IFS Tax Group into the work being carried out in the preparation of the Finance Bill’[14] and lists a whole range of tax breaks granted as a result. Mention is also made of ‘specific domestic legal initiatives undertaken to facilitate the development of new activities and products for the international side of the Irish financial services industry (for example in the area of asset covered securities)’[15] – whose role in the global financial crisis was then just beginning to emerge.

Commenting on the Strategy to the Institute of the Bankers in November 2006, Finance Minister Brian Cowen praised the financial services sector for ‘an amazing surge in both growth and innovation’. He advocated continuing regulatory innovation to facilitate this and attract foreign investment:

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[11] Ibid., 2.
[12] Gordon Deegan, “Kenny Pledges FG Will Pull Ireland Back from Brink,” *Irish Times*, December 10, 2010.
[13] Fintan O’Toole, *Ship of Fools*, 2009, chap. 6.
[14] Department of the Taoiseach, “Building on Success: International Financial Services Industry in Ireland” (Stationery Office, September 2006), 41.
[15] Ibid., 20.

> The Strategy highlights the importance of the continued development and innovation in the legislative framework for financial services which will encourage international financial firms to locate here and passport their services across the EU[16].

Launching the Strategy in the IFSC, Taoiseach Bertie Ahern said: 'We are all committed to seeing cost effectiveness, responsiveness and the ability to facilitate innovation, competitiveness and growth, embedded in the Irish regulatory approach'. This summed up the high-level political priorities for financial regulation in Ireland. None of them had anything to do with regulation in the traditional sense but were all about expanding the industry and attracting foreign capital[17]. The Honohan report[18] confirms this in citing 'fear that more robust regulation might make Ireland less attractive for international financial investment' as one of the main reasons stronger regulatory action was not taken.

According to Mary Burke[19], 'there was very much a view that we needed to…sell the regulatory regime in the context of the promotion of industry'. In her written statement, Burke elaborated that 'a key message in promoting Ireland as a financial services centre' was to market regulation here as '"principles based"'[20]. This was evident in a speech by Taoiseach Bertie Ahern to bankers in New York in March 2007 in which he spelled out what this meant for the industry:

> Ireland's Financial Regulator is principles based, as opposed to the more prescriptive rules based approach. This fact is highly regarded by the companies who have invested in Ireland. They have found this approach extremely pro-business[21].

In practice, 'principles based regulation' was code for virtual self-regulation by both international and Irish banks. The former Chair of the Financial Regulator, Brian Patterson, confirmed this in his submission to the Banking Inquiry Report, explaining that 'principles-based regulation places the responsibility for prudent lending with the lending institutions themselves, while rules-based regulation places responsibility on rule-makers and enforcers to curtail reckless lending'.

This end result was a system of regulation designed to facilitate profit-making that was completely subservient to it. This is evident in the Financial Regulator's 2006 Annual Report[22], which states:

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[16] "Address by the Minister for Finance, Brian Cowen, TD, to the Institute of Bankers in Ireland Annual Dinner - 2 November 2006.," November 2, 2006, http://oldwww.finance.gov.ie/viewdoc.asp?DocID=4325.

[17] Bertie Ahern, "Launch of the IFSC Strategy Document, 'Building on Success' at the CHQ, IFSC," 2006, http://www.taoiseach.gov.ie/eng/News/Archives/2006/Taoiseach's_Speeches_Archive_2006/Launch_of_the_IFSC_Strategy_document,_%E2%80%9CBuilding_on_Success%E2%80%9D_at_the_CHQ,_IFSC.html.

[18] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 97.

[19] "Transcript of Mary Burke Hearing," May 27, 2015, 84.

[20] Mary Burke, "Opening Statement to the Banking Inquiry," April 29, 2015, 2.

[21] "Speech by the Taoiseach, Mr Bertie Ahern, T.D. at a Breakfast Meeting with the Financial Services Industry, in New York on Wednesday, 14 March, 2007," March 14, 2007, http://www.taoiseach.gov.ie/eng/News/Archives/2007/Taoiseach's_Speeches_Archive_2007/Speech_by_the_Taoiseach,_Mr_Bertie_Ahern,_T_D_at_a_breakfast_meeting_with_the_financial_services_industry,_in_New_York_on_Wednesday,_14_March,_2007.html.

[22] Financial Regulator, "Consumer Protection with Innovation, Competitiveness and Competition: 2006 Annual Report of the Financial Regulator," July 27, 2007, 12, https://inquiries.oireachtas.local/banking/participant/PUB/EvidenceDocuments/PUB01B01/2006%20Annual%20Report%20of%20the%20Financial%20Regulator.pdf.

> We design and operate a regulatory regime conducive to an internationally competitive financial services industry…that is profitable and growing in both the domestic sector and the international sector based in Ireland. We seek to be well informed about the needs and concerns of financial institutions through regular consultation and research. We provide world-class service to financial institutions in all our dealings with them[23].

This illustrates an understanding of the Financial Regulator as a 'service provider' for banks, competing with other jurisdictions to offer them the best 'service' and attract investment rather than regulate them in any normal sense. It explains why dangerously fast financial sector growth was actually cited as a *positive* indicator of success by the CEO of the Financial Regulator, Patrick Neary, who boasted that '2006 was a year of significant growth in the financial services industry: Total assets of credit institutions increased by 19% from €941 billion to €1,116 billion'[24]. Later on, a graph showing lending had almost doubled in three years is followed by the approving comment that 'Over a relatively short period, Ireland has become a significant financial services hub'[25].

Once again, this attitude went all the way to the top. In March 2006, by which stage the banking system had already grown dangerously out of control, Brian Cowen, who was then the Minister for Finance, told Financial Services Ireland that:

> Banking and Finance continues to be one of the main driving forces behind economic growth. It is one of the fastest growing sectors in the country…The Government is committed to supporting the further development of the financial services industry, and especially the internationally-oriented sector, as a key growth element in the Irish economy'[26] .

Cowen went on to say that 'the regulatory standards applied in the international financial sector are no less stringent than those that apply generally in the industry in Ireland'. But as Professor Gregory Connor testified, rather than this meaning that the regulatory standards applied to international banks were raised *up*, the opposite occurred:

> The IFSC…specialises in regulatory arbitrage and tax-type situations that are perhaps pushing the limits. That…is partly what offshore centres do, but it probably has been done to excesses in some cases in the IFSC. Furthermore, that tendency or philosophy washed back to the domestic economy. The regulation of financial markets in domestic Ireland was hobbled by the very light-touch approach that was one of the founding principles of the IFSC[27].

The former Head of the Banking Supervision Department of the Financial Regulator, Mary Burke, confirmed this, explaining that:

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[23] Financial Regulator, "Annual Report of the Financial Regulator 2006," 2007, 20.
[24] Ibid., 6.
[25] Ibid., 22.
[26] "Address by the Minister for Finance, Mr Brian Cowen TD to Financial Services Ireland on 2 March 2006," March 2, 2006, http://oldwww.finance.gov.ie/viewdoc.asp?DocID=3834.
[27] Gregory Connor, "Oral Testimony to the Banking Inquiry," February 25, 2015, 467, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/02/25022015_Connor_vol1.pdf.

> The desire to portray Ireland as business friendly led…to a reluctance to introduce prescriptive rules and a particular focus on keeping costs down in the context of industry funding of the regulatory authority. In addition, the strategic decision that there should not be two different regulatory regimes - one for domestic firms and another for those in the IFSC - meant that a different approach was not taken to the domestic financial services sector. This decision was driven by a concern that the IFSC might otherwise be categorised as an off-shore centre with associated negative connotations[28].

In other words, the desire for Ireland to be perceived as a respectable EU member state rather than an 'offshore' centre like Bermuda was a factor in why *all* financial firms – whether international or domestic – enjoyed the same 'Wild West'[29] freedom from regulation. Quoting from a chapter in a university textbook by Trinity College academic, William Kingston, Joe Higgins put it to Patrick Honohan that this situation pre-dated the establishment of a separate Financial Regulator in 2003 and went all the way back to Charlie Haughey's decision to establish the IFSC in 1987. According to Kingston, previous to this, regulation:

> had always been in the charge of the conservative Central Bank, so it was considered important to be able to signal to potential investors in the IFSC that they would not have to face this kind of regulation. Before Haughey left office in 1992, therefore, the ground had been laid for a fundamental transformation of the regulatory system[30]

The same assessment – and a concrete example of how it affected domestic banks – was provided by Brian Patterson. He explained in relation to the Regulator's non-enforcement of sectoral limits designed to prevent banks from lending too much to one sector of the economy (such as property), that:

> the Central Bank had effectively relaxed these limits in the 1990s, prior to the setting up of the Financial Regulator, in order to encourage the development of the IFSC and in particular to facilitate the arrival of one large foreign bank which had a major sector exposure. It was then felt that foreign and domestic banks had to be treated the same – in order to avoid giving substance to any impression that Ireland was host to an off-shore centre that was being treated more lightly than its domestic banks[31].

This 'relaxation' of regulation to attract financial investment was facilitated by Ireland's membership of the EU and its liberalised economic and financial relations with the rest of the world, particularly the US. These enabled international banks to use Ireland as an entry point into EU and global markets while benefiting from the haven it provided from tax and regulation. Honohan in his response to Joe Higgins preferred this as an explanation, saying:

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[28] Burke, "Opening Statement to the Banking Inquiry," 3.
[29] This phrase was first used in a *New York Times* article on the IFSC in 2005 and was referenced numerous times during the Inquiry. Brian Lavery and Timothy L. O'Brien, "Insurers' Trails Lead to Dublin," *The New York Times*, April 1, 2005.
[30] William Kingston, "Need the Irish Experiment Fail?," in *Irish Business and Society: Governing, Participating and Transforming in the 21st Century*, ed. John Hogan, Paul F. Donnelly, and Brendan K. O'Rourke (Gill & Macmillan Ltd, 2010).
[31] Brian Patterson, "Opening Statement to the Banking Inquiry," June 11, 2015, 6–7.

> I think the international regulatory environment, which moved very much in the direction of laxity during the 2000s, certainly spilled over into attitudes here as well. People thought they were behaving like the general trend. There was definitely a move towards lighter regulation globally from the mid-1980s on and that certainly influenced the environment[32].

This illustrates again how difficult it is to separate 'domestic' from 'international' factors as Ireland was simultaneously following and developing a systemic global trend.

The EU's role in globalisation

The founding purpose of the EU was to create a unified free market across Europe, making it a central actor in neoliberal globalisation. In the financial sphere, this was reflected in the European Commission's (EC) *White Paper on Financial Services Policy (2005-2010),* which declared as an incontestable article of faith that:

> Financial markets are pivotal for the functioning of modern economies. The more they are integrated, the more efficient the allocation of economic resources and longrun economic performance will be[33].

Consequently, it aimed 'to remove the remaining economically significant barriers so financial services can be provided and capital can circulate freely throughout the EU at the lowest possible cost'[34]. The main impact would be to increase the potential for financial profit. The Commissioner responsible for that strategy and financial regulation generally was former Fianna Fáil Finance Minister, Charlie McCreevy, who was European Commissioner for Internal Market and Services from November 2004 to February 2010. McCreevy described his 'central mission' as 'to secure…ever greater European market integration and to seek the removal of obstacles to the free movement of services and capital'[35].

That McCreevy, a self-confessed 'champion of the free capitalist markets'[36] was applying the same approach at the heart of the EU in the run-up to the financial crisis illustrates how perfectly compatible this was with EU policy. McCreevy made his attitude to financial regulation abundantly clear in a speech to the Financial Regulator in October 2005 when he said – as EU Commissioner with responsibility for financial regulation across Europe – that 'the benefits [of regulation] are sometimes more imaginary than real'. He elaborated:

> Don't try to protect everyone from every possible accident. Concentrate on the big things that really matter. And leave industry with the space to breathe and investors with the freedom to learn from their mistakes…Many of us in this room are from the generations that had the luck to grow up before governments got working and lawyers got rich on regulating our lives. We were part of the "unregulated generation" – the generation that has produced

[32] "Transcript of First Honohan Hearing," January 15, 2015, 144.
[33] European Commission, "White Paper on Financial Services Policy (2005-2010)," 2005, 4, http://ec.europa.eu/internal_market/finances/docs/white_paper/white_paper_en.pdf.
[34] Ibid., 3.
[35] Charlie McCreevy, "Commissioner McCreevy - Portfolio," accessed December 30, 2015, http://ec.europa.eu/archives/commission_2004-2009/mccreevy/portfolio_en.htm.
[36] When asked by Joe Higgins 'you would portray yourself definitely as a champion of the free capitalist markets, right?', McCreevy replied, 'Yes. I've no problem with that'. "Transcript of Charlie McCreevy Hearing," July 1, 2015, 132.

> some of the best risk takers, problem solvers, and inventors. We had freedom, failure, success and responsibility and we learned how to deal with them all[37].

Unfortunately, as alluded to by the current EC Director for Regulation and Supervision of Financial Institutions, Mario Nava, what this meant in practice was 'people taking risks and then shovelling that risk onto someone else'[38].

In this context, Ireland's traditional role as a capital haven was facilitated and reinforced by the EU's lowest common denominator approach to financial regulation, which existed before and after McCreevy. According to Nava, this 'followed a principles-based approach[39] that was embodied in the principle of minimum harmonisation', in which 'The degree of flexibility…granted to Member States and national supervisors…created opportunities for regulatory arbitrage'[40]. Asked by Joe Higgins what this meant, he explained:

> "Regulatory arbitrage" means there are different rules in different place…the fact that one has different rules in different places for the same activity…makes it possible, given the free circulation of capital in the Single Market, to go and shop in the place where more favourable rules are in place[41]

The government positioned Ireland to take advantage of this, strategising that:

> While financial services legislation in Ireland largely derives from EU requirements, the structure and operation of the legal framework has the potential to represent a significant competitive advantage for international financial services in Ireland[42].

In effect, by setting only 'minimum standards', the EU fired the starting gun for a race to the bottom among member states to compete to offer the least regulation and lowest taxes to investors. An example of the Irish government's participation in this appears in a speech by Taoiseach Bertie Ahern to the Irish Bankers Federation (IBF) and Federation of International Banks in Ireland (FIBI) in March 2006. Ahern inadvertently describes competitive deregulation across the EU in relation to asset covered securities:

> the Government introduced the Asset Covered Securities Act in 2001 and this has led to considerable Irish-based activity in this important niche sector. While our 2001 Act had several useful innovative features as compared with the longer-established legislative regimes in other Member States, your international rivals do not lightly tolerate newcomers on their patch! They have sponsored legislative refinements to match those initiated in Ireland and elsewhere. I am aware that you have been seeking technical adjustments to our 2001 Act as a matter of commercial and competitive urgency. Brian Cowen and his

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[37] quoted in Justin O'Brien, "IFSC Seen as Financial 'Wild West,'" *Irish Times*, January 9, 2006, http://www.irishtimes.com/news/ifsc-seen-as-financial-wild-west-1.999202.
[38] "Transcript of Mario Nava Hearing," February 5, 2015, 295.
[39] At EU level too, 'principles based legislation' was code for light touch, self-regulation. Nava admitted that, 'in line with the principle-based approach to regulation, Member States typically did not resort to…overly prescriptive rules'. Mario Nava, "Opening Statement to the Banking Inquiry," February 5, 2015, 3.
[40] Ibid., 1; 3.
[41] "Transcript of Mario Nava Hearing," 311.
[42] Department of the Taoiseach, "Building on Success," 18.

> Department have been cooperating with you in this regard and proposals for the necessary up-dating of the 2001 Act will shortly be brought to Government[43].

The resulting Asset Covered Securities Act (Amendment Act) was passed in early 2007. What it did was allow foreign and Irish banks to use commercial property loans as collateral for borrowing on international wholesale money markets, whereas previously they had only been able to do this with residential mortgages. In other words, as former Irish Times financial correspondent, Simon Carswell, explained, 'It was effectively a means of selling loans on to investors to generate cash to lend again'[44], thereby inflating the bubble.

Given this political context, nationally and at EU level, it's no wonder the Financial Regulator was reassuring bankers in 2005 that:

> we, as Regulator, will not introduce or impose unnecessary regulatory burdens that will effect [sic] the continued competitiveness of our financial industry and will minimise the impact of such burdens coming from Europe[45].

Such toothless EU and Irish regulation, which encouraged regulatory arbitrage by banks and regulatory competition by EU member states, did not fall out of the sky. They were a direct result of the power of finance capital and lobbying by banks at European and national level.

Financialisation

A second key component of global neoliberal restructuring is what became known as 'financialisation'. Professor McDonough defined this as "the increasing importance of financial markets, financial motives, financial institutions, and financial elites in the operation of the economy and its governing institutions, both at the national and international level"[46] . This includes the financialisation of everyday life through the extension of the financial sector into areas like housing, education, health and pensions where they previously had little or no role. Often this is linked to privatisation of public services. It's hard to believe now but banks in Ireland did not give out residential mortgages until 1975[47]. Prior to then, local authorities had a much greater role in mortgage provision and there was far more council housing to rent. In 1975, a third of all new housing was built by the councils[48].

Central to financialisation has been the increased power of financial market actors. They include not just retail banks but investment banks like Merrill Lynch and Goldman Sachs, hedge funds, insurance companies, credit rating agencies like Moody's and Standard & Poor's, and the big four accounting firms – KMPG, PWC, Ernst & Young and Deloitte. Their increased power has been facilitated by restructuring states to give more power to Central Banks and insulate them from democratic influence. In reality, as the crisis here demonstrated, Central Banks are not 'independent' but

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[43] Bertie Ahern, quoted in Finfacts Team, "Taoiseach Praises Contribution of Banks," March 31, 2006, http://www.finfacts.ie/irelandbusinessnews/publish/article_10005395.shtml.
[44] Simon Carswell, *Anglo Republic*, 2011.
[45] quoted in Con Horan, "Opening Statement to the Banking Inquiry," April 20, 2015, 3 n10.
[46] McDonough, "Opening Statement to the Banking Inquiry," 2.
[47] Conor McCabe, *Sins of the Father: Tracing the Decisions That Shaped the Irish Economy*, 2nd ed. (Dublin, Ireland: The History Press, 2013), 36–37.
[48] Jesuit Centre for Faith & Justice, "The Irish Housing System: Vision, Values, Reality," 2009, 4, http://www.jcfj.ie/images/stories/pdf/JCFJ_Irish_Housing_System_low_res.pdf.

represent the interests of the financial sector. Professor Costas Lapavitsas, an expert on financialisation at the University of London, calls them 'the dominant public institution of financialization, the defender of the interests of the financial sector'[49].

This is true across the world where a revolving door exists between Central Banks, finance departments, and financial firms. For instance, the heads of the Canadian and Italian central banks have both previously worked for Goldman Sachs, as have two recent heads of the Federal Reserve Bank of New York[50]. Ireland's niche in the global economy as a capital haven only made this relationship more crude and obvious, as it had to be loudly advertised to foreign investors. So the government wrote into the Central Bank Act in 2003 a duty 'to promote the development within the State of the financial services industry'[51]. And the Taoiseach flew to New York in March 2007 with the Financial Regulator to tell American bankers that 'Our commitment to supporting foreign direct investment is absolute' and 'Ireland is very lightly regulated compared with most of our European colleagues'[52]. The second quote was put to Ahern during the Inquiry. His response was to complain: 'you're trying to put "lightly regulated" as something that's bad'[53].

The increased power of the financial sector, which led to the shaping of state agencies in their interests, is rooted in the increased profitability of shorter term speculative financial investments, relative to longer term investments in the 'real economy'. New financial products to 'spread the risk', or 'shovel it onto somebody else', like asset-backed securities, have been part of this. Even more important has been the financial globalisation promoted by the EU, US, and successive Irish governments. The liberalisation and growth of the financial sector since the 1970s is associated with a much greater frequency of financial crises. According to documents released to the Inquiry, this was pointed out to the Central Bank board by the then Head of Monetary Policy and Financial Stability, Frank Browne in June 2004. Just how common financial crises have become is shown by IMF research identifying 147 banking crises, 218 currency crises and 66 sovereign crises from 1970–2011[54]. Browne touched on the underlying dynamics in his witness statement:

> In the new liberalised context, the monetary system seems to alternate between generating excess liquidity which then drives a search for yield and ultimately a bubble, followed by the bursting of the bubble, which then generates a deficiency of liquidity[55].

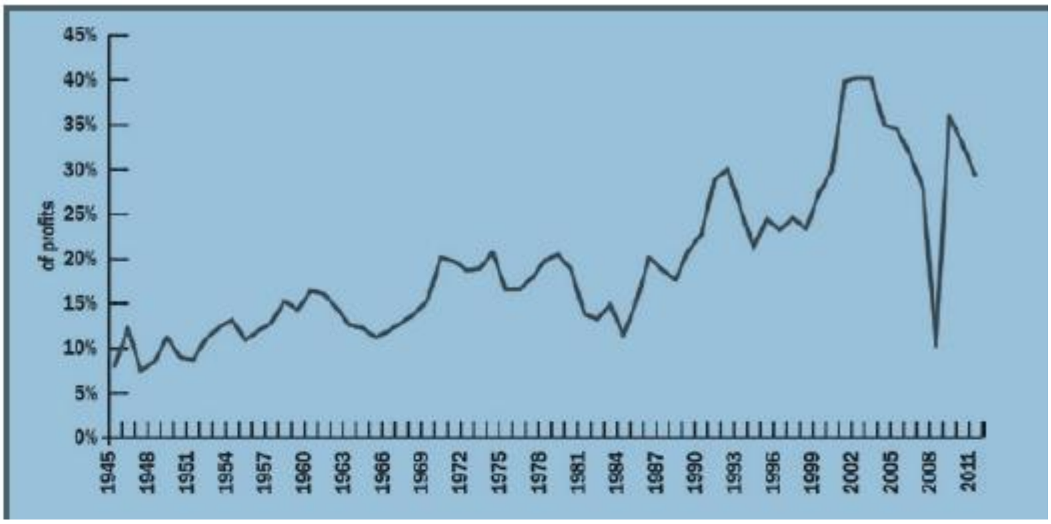
The IMF identifies 'the relatively large size' of the financial system 'amounting to multiples of GDP' as an important reason Ireland and Iceland suffered worse financial crises than anywhere else[56]. This

[49] Costas Lapavitsas, *Profiting without Producing: How Finance Exploits Us All* (London ; New York: Verso Books, 2013), chap. 1.
[50] Matt Taibbi, "The Great American Bubble Machine," *Rolling Stone*, April 5, 2010, http://www.rollingstone.com/politics/news/the-great-american-bubble-machine-20100405.
[51] Article 5(b) *Central Bank and Financial Services Authority of Ireland Act 2003*, 2003, http://www.oireachtas.ie/documents/bills28/acts/2003/a1203.pdf.
[52] "Speech by the Taoiseach, Mr Bertie Ahern, T.D. at a Breakfast Meeting with the Financial Services Industry, in New York on Wednesday, 14 March, 2007."
[53] "Transcript of Bertie Ahern Hearing," July 16, 2015, 136.
[54] Laeven and Valencia, "Systemic Banking Crises Database," 3.
[55] "Witness Statement of Frank Browne," November 2015, 41.
[56] Laeven and Valencia, "Systemic Banking Crises Database," 20.

indicates how a more financialised economy is a more unstable economy – and according Patrick Honohan, Ireland still has 'the 15th largest international financial sector in the world'[57].

As well as making the global economy more unstable, the reduction or elimination of barriers to cross-border financial transactions and creation of a single global financial market has cut the cost of international financial speculation and increased its profitability. This in reflected in bigger financial profits, which increased dramatically as a percentage of all profits in the US (Figure 1.2), Ireland, and to a lesser extent across the Eurozone, particularly in the UK with its large financial industry (Figure 1.3). The US (Figure 1.4), and Ireland stand out for the dominance of financial profits, which accounted for roughly 45% of profits in the US in 2007 and 55% in Ireland in 2008 – 30% above the Eurozone average (Figure 1.3).

Figure 1.2 Financial profit as a proportion of total profit; US[58]



57 "Transcript of First Honohan Hearing," 121.
58 Lapavitsas, *Profiting without Producing*, chap. 8.

Figure 1.3 Financial Profits as a % of All Company Profits[59]

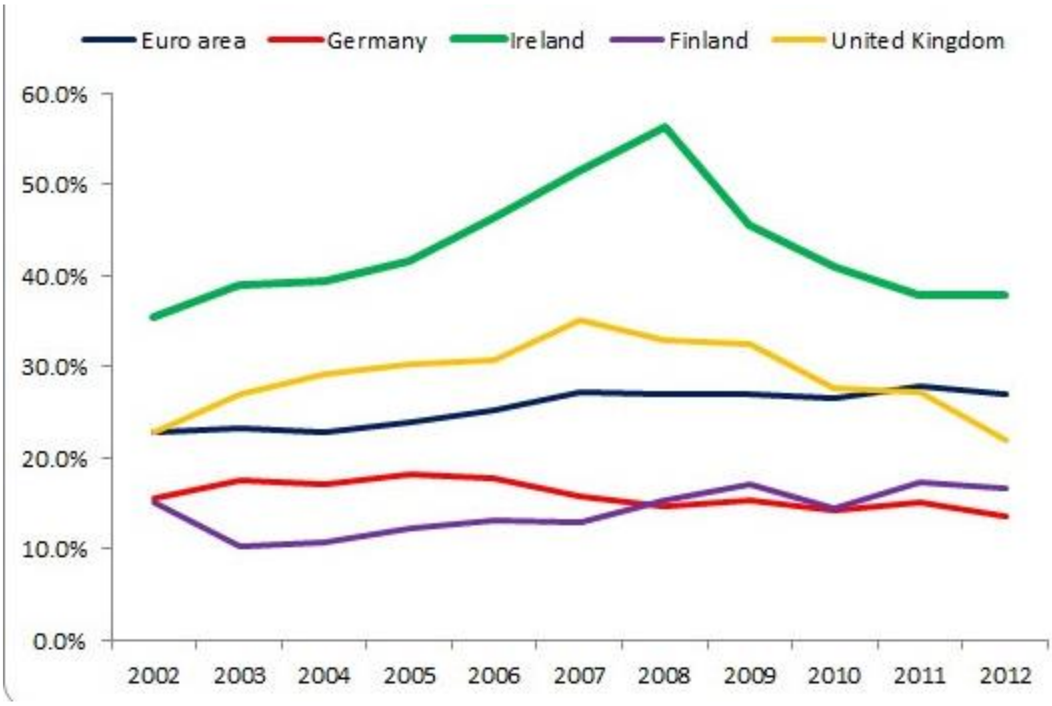
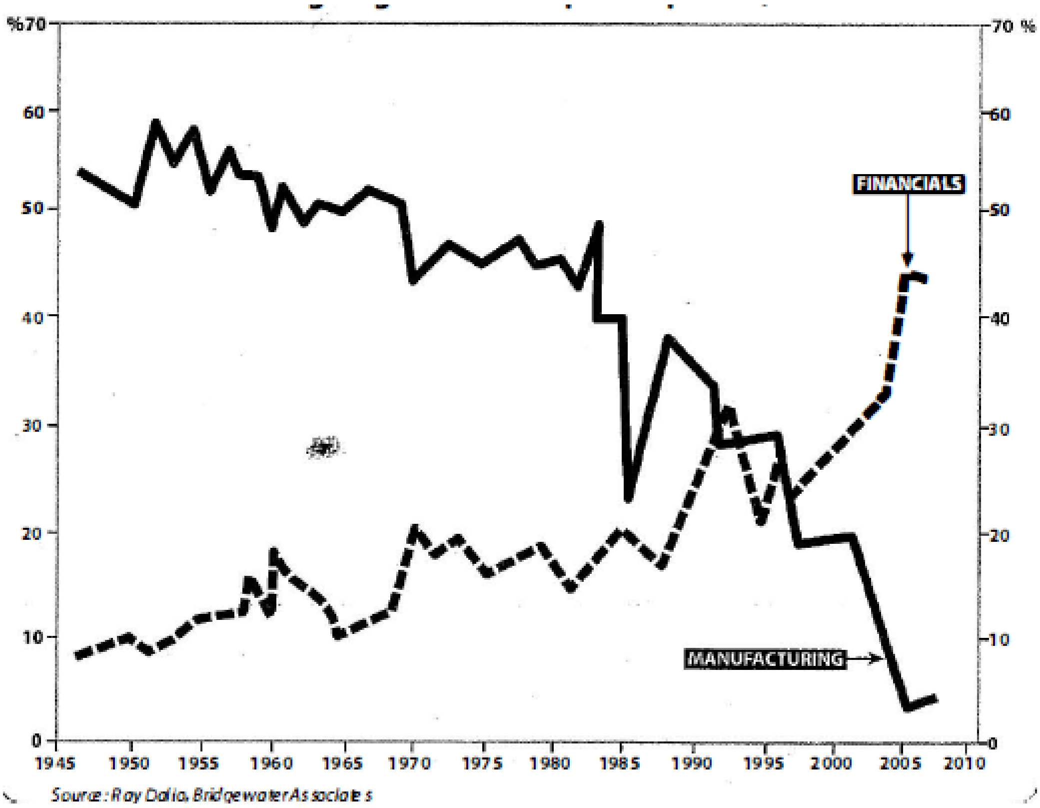


Figure 1.4 The reversing origins of US corporate profits, 1950-2007[60]



Eurostat figures on Financial Sector Value Added[61] as a Percentage of GDP also show the disproportionate size of the financial sector compared to other Eurozone countries (Figure 1.3)[62].

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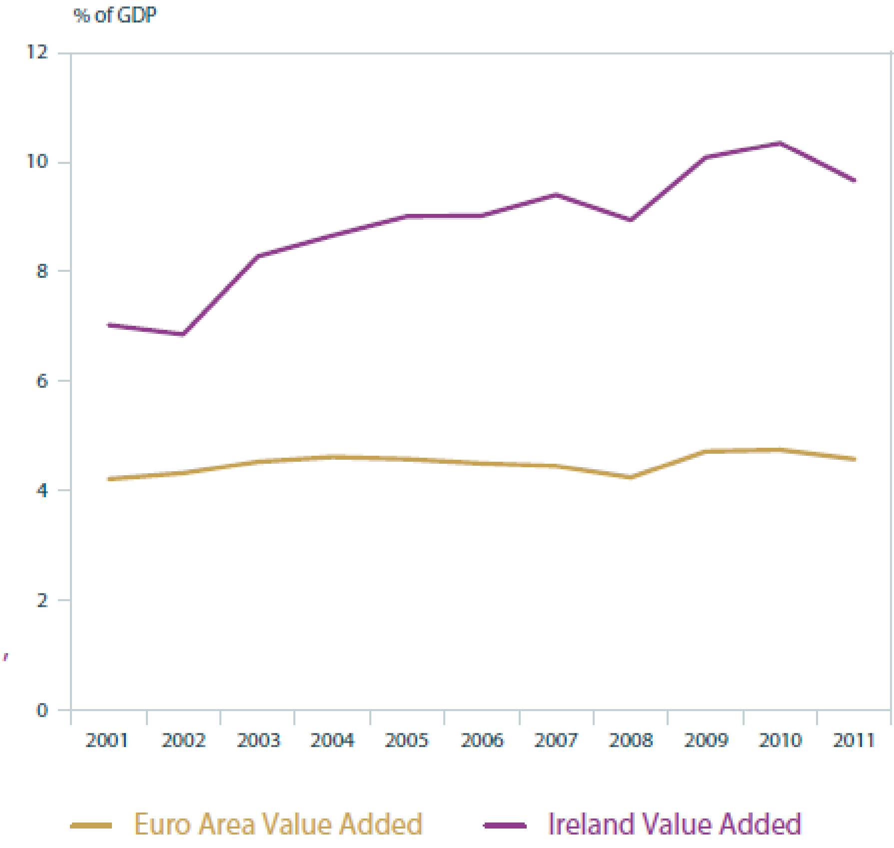
[59] Michael Taft, "Friday Stat Attack: The Financial Heaven That Is Ireland," *Irish Left Review*, January 31, 2014, http://www.irishleftreview.org/2014/01/31/friday-stat-attack-financial-heaven-ireland/.
[60] David Harvey, *The Enigma of Capital and the Crises of Capitalism* (Profile Books, 2010), 22.

Figure 1.5 Euro Area and Irish Financial Sector Value Added as a Percentage of GDP, 2001-2011[63]



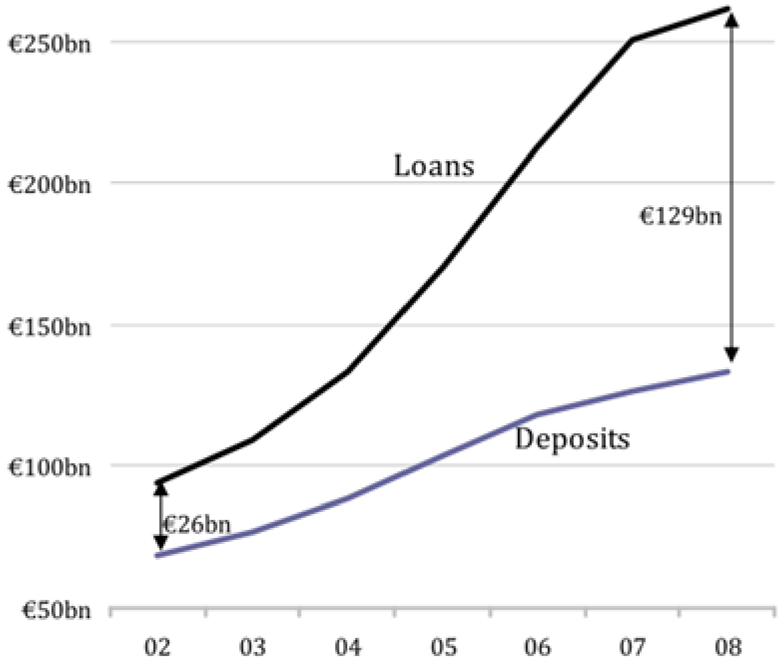
Source: Eurostat.

The size of the financial sector before the crash reflected the scale of the domestic property bubble as well as the Irish state's 'success' in attracting financial investment into Ireland on the back of tax breaks and competitive deregulation. But unlike in the US where Wall Street is largely indigenous, Ireland's dependence on foreign investment meant the growth of the domestic and international financial sectors was dependent on foreign finance capital – whether from foreign banks locating here or global money markets via the Irish banks. Both forms of financial dependence were exacerbated by the introduction of the Euro, which encouraged foreign financial institutions to use Ireland as an entry haven into the EU and allowed Irish banks to gorge themselves on an ocean of liquidity at similarly low rates of interest to German banks.

Between 2002 and 2008, the six Irish banks funding debts to the wholesale money markets (Figure 1.6), where banks borrow from other banks and from international investors, ballooned from €26bn to €129bn, an increase of nearly 500% in just seven years.

[61] in Mary Everett, Joe McNeill, and Gillian Phelan, "Measuring the Value Added of the Financial Sector in Ireland," *Central Bank Quarterly Bulletin*, no. 02 (April 2013): 87..
[62] These statistics obviously don't give a true picture of the 'real' value added to the economy given they continue to show a positive value during the crisis when the banks sucked in billions of public money. This is because this was just counted as increasing the size of the sector.
[63] Everett, McNeill, and Phelan, "Measuring the Value Added of the Financial Sector in Ireland," 87.

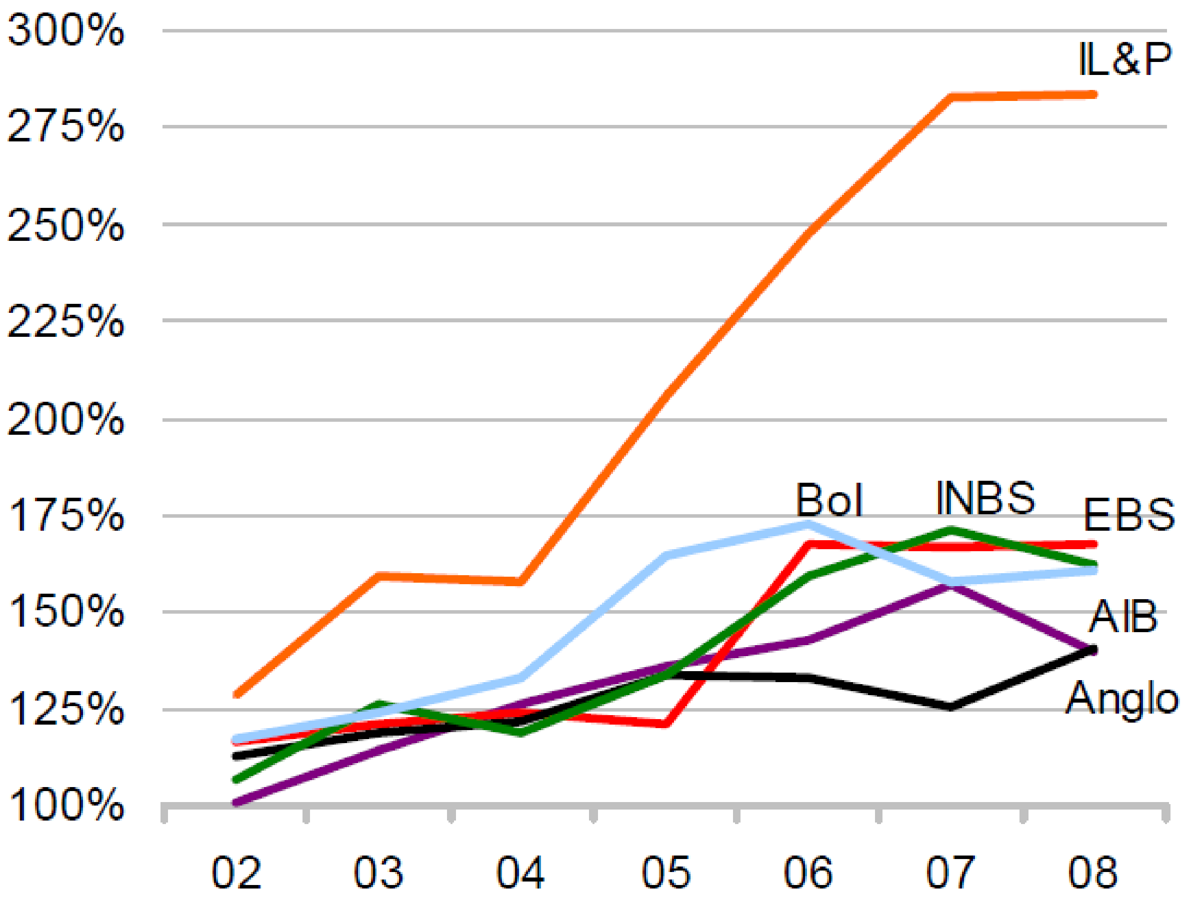
Figure 1.6 Irish banks' dependence on wholesale funding (2002-2008)[64]



This gigantic sum was equivalent to the gap between what the banks were taking in in deposits and what they were lending out to customers. In other words, if the banks hadn't been able to borrow all that money from the wholesale markets, most of which came from abroad, they couldn't have inflated the bubble anything like as much as they did. This was acknowledged in an internal post-mortem on the crisis by Bank of Ireland (BOI) released to the Inquiry, which states that 'Given that the rate of credit growth significantly outpaced the rate of deposits, there was a greater dependence on wholesale funding (much of which came from overseas).' The same applied to all the banks to differing extents and was reflected in the rapid increase in their loan to deposit ratios (Figure 1.7). A deposit ratio of less than 100% means a bank has more money on deposit than it's given out in loans; anything over 100% means a bank has lent out more than it has borrowed from its customers in the form of deposits and is reliant on wholesale borrowing to fund its loans instead.

[64] Peter Nyberg, "Misjuding Risk - Causes of the Systemic Banking Crisis in Ireland: Report of the Commission of Investigation into the Banking Sector In Ireland," March 2011, 39, http://www.bankinginquiry.gov.ie/Documents/Misjuding%20Risk%20-%20Causes%20of%20the%20Systemic%20Banking%20Crisis%20in%20Ireland.pdf.

Figure 1.7 Loan to Deposit Ratios of the Six Banks Covered by the Guarantee 2002-2008[65]



The resulting growing dependency of the Irish banks on foreign wholesale funding was commented on at the time. The IMF's August 2006 Financial Stability Situation Update pointed out that:

> Irish banks had the lowest customer deposits-to-assets ratio of all western European Union (EU) member countries as at end-2004. As a result, a growing share of banks' funding has been from other financial institutions, including from off-shore; heavy reliance on wholesale funding potentially increases liquidity risk[66].

Writing in the Winter 2006 *ESRI Quarterly Economic Commentary*[67] (Figure 1.8), Professor Honohan also highlighted that:

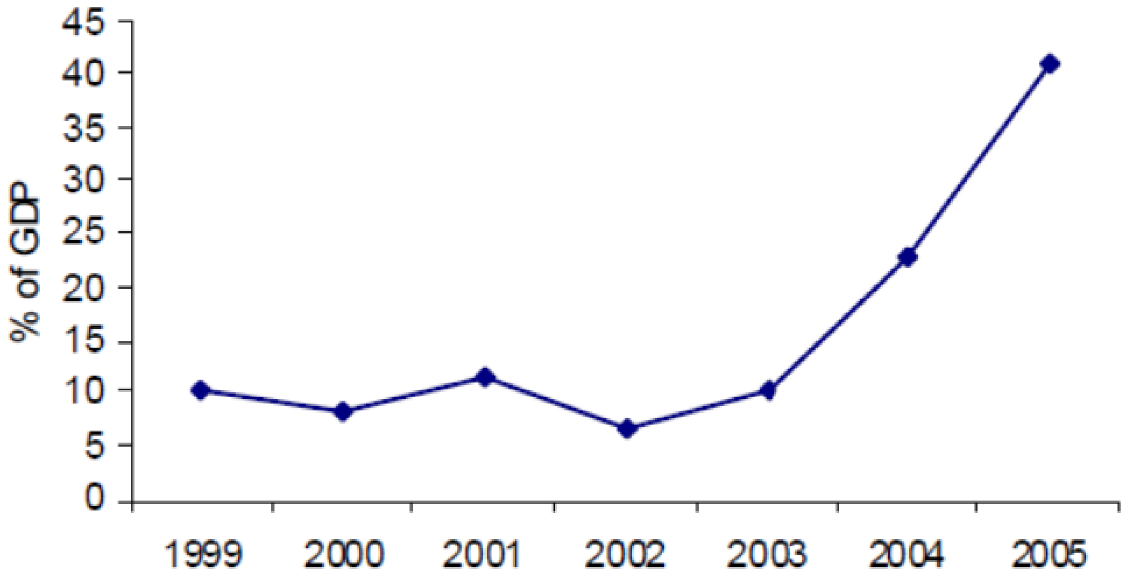
> the net import of funds [by] credit institutions doing business in Ireland to lend to Irish residents amounted to 41 per cent of GDP by the end of 2005. This has changed with astonishing speed (up from about 10 per cent at end 2003).This shows the extent to which it is global finance, and not solely the Irish financial system, that is providing finance to Irish borrowers.

[65] "Nyberg Report," 56.

[66] IMF, "Ireland: Financial Stability Assessment Update," IMF Country Report No (IMF, August 2006), 11, http://www.imf.org/external/pubs/ft/scr/2006/cr06292.pdf.

[67] Patrick Honohan, "To What Extent Has Finance Been a Driver of Ireland's Economic Success?," *ESRI Quarterly Economic Commentary*, no. Winter 2006 (Winter 2006): 70–71.

Figure 1.8 Stock of Net Borrowing of Irish Resident Credit Institutions from Abroad [68]

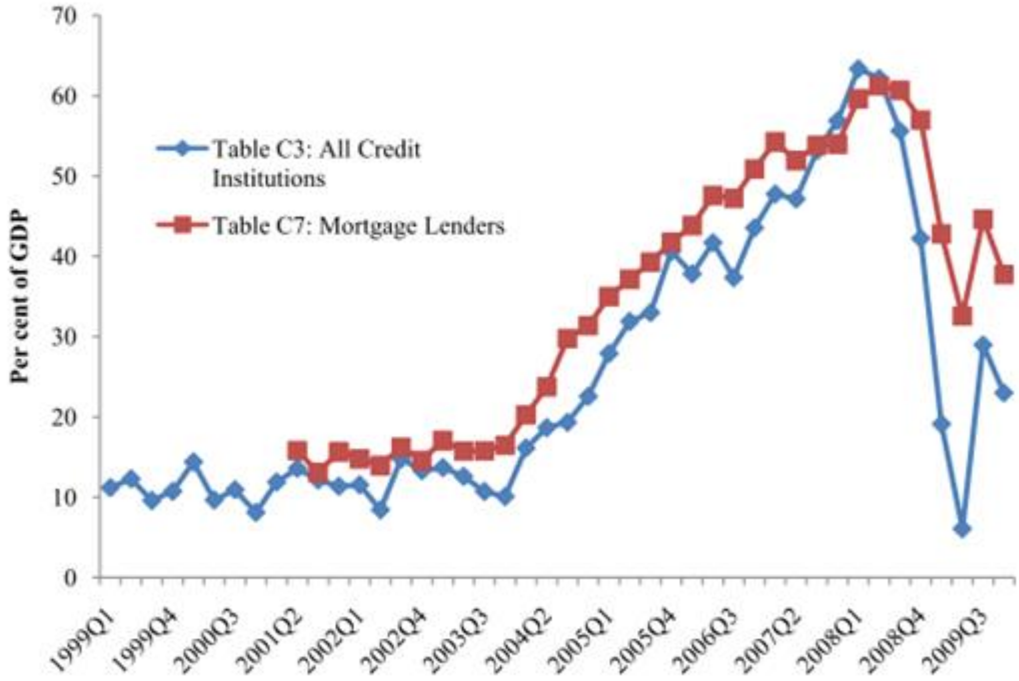


Four years later in his report on the crash, Honohan showed how much worse the situation had become (Figure 1.9)[69]. The head of the IMF's mission to Ireland, Craig Beaumont, confirmed this in his written statement, quoting a 2012 IMF staff report:

> "The integration of the Irish financial system into the broader euro area financial landscape…gave Irish banks unfettered access to wholesale funding that turbocharged their asset expansion**.** In the five years to mid-2008 the net foreign liabilities of the Irish banking system jumped from about 20 percent to about 70 percent of GDP, and wholesale funding rose to 55 percent of assets."[70]

[68] Ibid., 70.
[69] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 27.
[70] quoted in "Written Statement of Craig Beaumont," 27.

Figure 1.9 Stock of Net Borrowing of Irish Resident Credit Institutions from Abroad, 1999Q1 to 2009Q4[71]



Source: Table C3, 7 of the Central Bank Monthly Statistics, and the CSO's Quarterly National Accounts.
Note: GDP are annualised from quarterly data.

As we shall see, this external dependence of the Irish banks was an important part of the reason private banking debt was so quickly converted into sovereign debt once the crisis hit. On the one hand, this reflected the neo-colonial relationship between Ireland and the bigger EU powers, who enforced the interests of their own banks and bondholders over those of the weaker Irish capitalist class in ensuring they got their money back. On the other, it meant the dominant banking and property sections of the Irish capitalist class, who had enriched themselves by their irresponsible borrowing and lending during the bubble, were able to socialise the vast majority of those gambling losses by passing them on to the Irish population as a whole in the form of national debt. So although the crisis was obviously a very negative event from the perspective of Irish and European elites and temporarily wiped out the fortunes of some wealthy individuals, *its resolution* ended up being a win-win for both the Irish and European ruling classes.

The threat that growing external funding dependency posed to the Irish banking system was raised in the Central Bank's 2005 *Financial Stability Report,* which warned that the 'increased reliance of the Irish banking sector on international funding' 'exposes it to risks of a possible drying-up of liquidity, if a shock were to hit the system'[72]. The head of Financial Stability at the Central Bank,

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[71] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 27.
[72] Central Bank, "Financial Stability Report 2005," 2006, 91, http://www.centralbank.ie/publications/Documents/Part%201%20-%20Financial%20Stability%20Report%202005.pdf.

Frank Browne, had been highlighting this liquidity risk since at least 2004[73] but his suggestion that it should be the subject of the main 'thematic paper' in the 2005 *Financial Stability Report* was rejected by senior management. According to Browne's statement to the Inquiry[74], the then Chairman of the Central Bank's Financial Stability Committee, Liam Barron,

> raised issues about the paper saying that it was "tricky stuff" and "political"…He referred to the paper in what I thought were quite disparaging terms saying that my analysis implied that the world was now "riddled with bubbles" and that central banks had "mucked it up".

Barron disputes many aspects of Browne's evidence but conceded he had repeatedly raised concerns over liquidity. However, Barron claimed that 'given that the Central Bank had no control over liquidity what could be done in practice from a financial stability prospective [sic].'[75] This statement is misleading as the Central Bank could have directed the Financial Regulator to limit banks' loan-to-deposit ratios to stop them from borrowing so much from abroad. This is confirmed by the Honohan report, which states that 'A ceiling or penalty on very high loan-to-deposit ratios for banks would…have been effective'[76] and 'could have had a decisive and early effect in restraining the bubble before it really got under way.' However, Honohan adds that 'it would have been vigorously resisted'[77]. He doesn't say by who but it's clear that banks, big commercial borrowers (and the establishment political parties that represent their interests) would have been up in arms about any regulation that could infringe on their profits.

This highlights how financialisation, in increasing the dependence of the capitalist economic system on the financial sector for profits, increases the political power of banks and other financial actors. The financial and insurance sectors are the most common source of wealth on *The Forbes List* of billionaires[78] and in the US, the Finance/Insurance/Real Estate (FIRE) sector gives by far the most corporate donations to both the Republicans and the Democrats. In the EU, according to research by the independent watchdog organisation, Corporate Europe Observatory, over 1,700 finance industry lobbyists spend €120 million a year on lobbying EU institutions[79]. The current EC Director for Regulation and Supervision of Financial Institutions, Mario Nava, made no attempt to challenge these findings when put to him by Joe Higgins during the Inquiry[80]. Corporate Europe Observatory's conclusion that 'as far as financial regulation is concerned, lobbyists are besieging the Commission –

[73] "Witness Statement of Frank Browne," 38.
[74] Ibid., 49.
[75] "Section 24 Statement from Liam Barron," November 2015, 20, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/11/Material-Clarification-Liam-Barron.pdf.
[76] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 17.
[77] Ibid., 106.
[78] Oxfam, "Even It Up: Time to End Extreme Inequality," 2014, 5, http://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/cr-even-it-up-extreme-inequality-291014-en.pdf.
[79] Corporate Europe Observatory, "Regulating Finance: A Necessary but 'up-Hill' Battle," *Corporate Europe Observatory*, September 24, 2014, http://corporateeurope.org/financial-lobby/2014/09/regulating-finance-necessary-hill-battle.
[80] "Transcript of Mario Nava Hearing," 312.

which has an open door policy towards them'[81] would also seem to be confirmed by Charlie McCreevy who told the Inquiry that:

> one of the great things in Europe, I'll have to say, is that as a Commissioner, you are encouraged to meet all types of lobbyists at all times. And it's all there to meet…and you can bring in everyone you like or don't like, whatever the case may be, and there's never a comment in the wide earthly world[82].

McCreevy's successor as EU Commissioner with responsibility for financial responsibility, Jonathan Hill, is a former financial lobbyist[83]. His appointment was warmly welcomed by the head of the British Bankers' Association who praised Claude Juncker for entrusting "key Commission portfolios to people with the right experience", saying it would "unlock the flow of finance"[84]. Under these conditions, it's no wonder the EU has consistently set minimal regulatory standards for banks and continues to bend over backwards to accommodate them, even after they caused the worst financial crisis since the Great Depression. The same applies in Ireland where the banks that wrecked the economy were handed a Guarantee of all their gambling debts, bailed out with billions of euro, and now the government's main concern is to re-privatise them so the process can start all over again. The role of lobbying and the power of bankers and property developers in all this will be examined in subsequent chapters.

Increasing Inequality

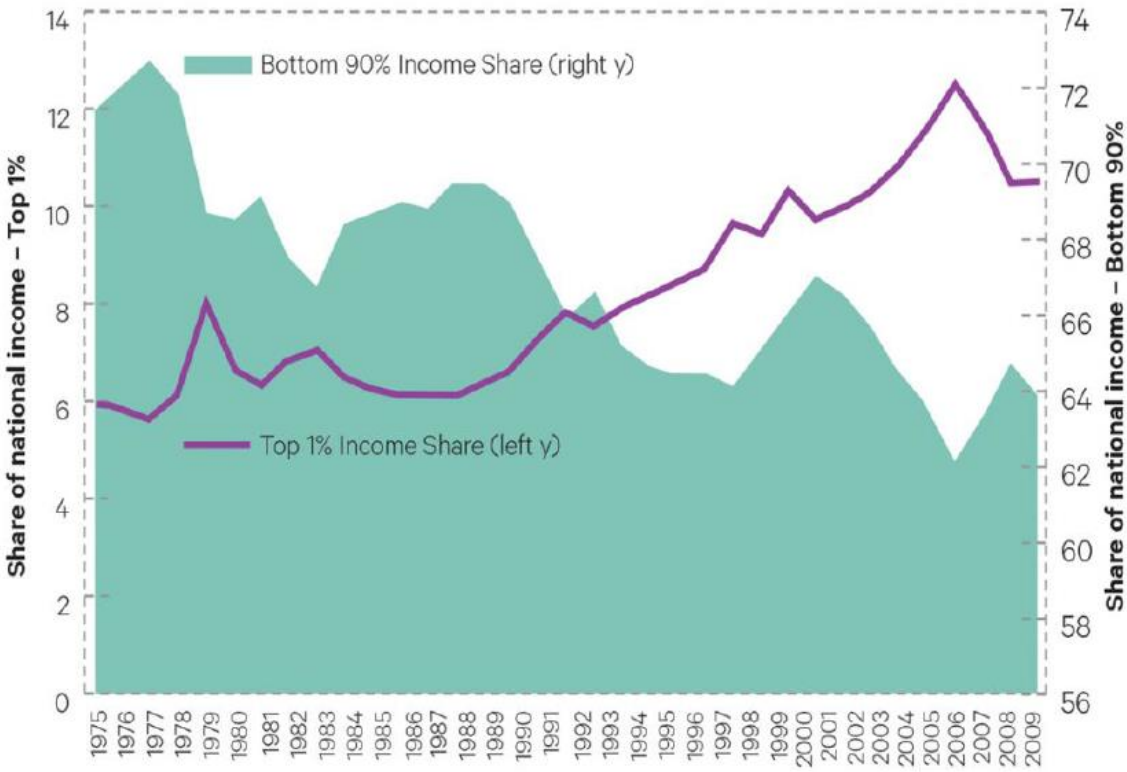
Another core element of global neoliberalism is increasing inequality. Professor McDonagh linked this to 'the erosion of the power of labour to defend its organizations, its working conditions and its standard of living.'[85] The inevitable outcome was a massive transfer of wealth from working people to the elites, now often referred to as the 1%. According to Oxfam, "Around the world, ordinary workers are taking home an ever-dwindling slice of the pie, while those at the top take more and more" [86]. By 2007, the 80 richest people owned about 48% of world wealth. Prior to the crisis, this phenomenon was most obvious in the US, where 'Labour's loss of bargaining power led to the stagnation of real median family income'[87].

In Ireland, the labour share of national income, which is the share of GDP or national output going to workers in the form of wages, fell from 71% in 1980 to 45% in 2002. According to Professor McDonough, this was 'the sharpest drop of anywhere' [88]. It automatically meant a corresponding increase in the profit share taken by business owners or capitalists, from 29% to 55%. Although the profit share was artificially inflated by multinationals booking profits here that were really made elsewhere in order to avoid tax, its growing size also reflected profiteering by domestic businesses, off the backs of their own workforce and also of the working class as a whole through spiralling consumer prices. The first form of profiteering is confirmed by a 2008 EC study, which found that in Ireland, 'the real wage…decreased at an average annual rate of 2.62%' from 1981-2006, 'The

[81] Corporate Europe Observatory, "Regulating Finance."
[82] "Transcript of Charlie McCreevy Hearing," 145.
[83] Corporate Europe Observatory, "Regulating Finance."
[84] quoted in ibid.
[85] McDonough, "Opening Statement to the Banking Inquiry," 2.
[86] Oxfam, "Even It Up: Time to End Extreme Inequality," 15.
[87] McDonough, "Opening Statement to the Banking Inquiry," 3.
[88] "Transcript of Terrence McDonough Hearing," February 26, 2015, 552–553.

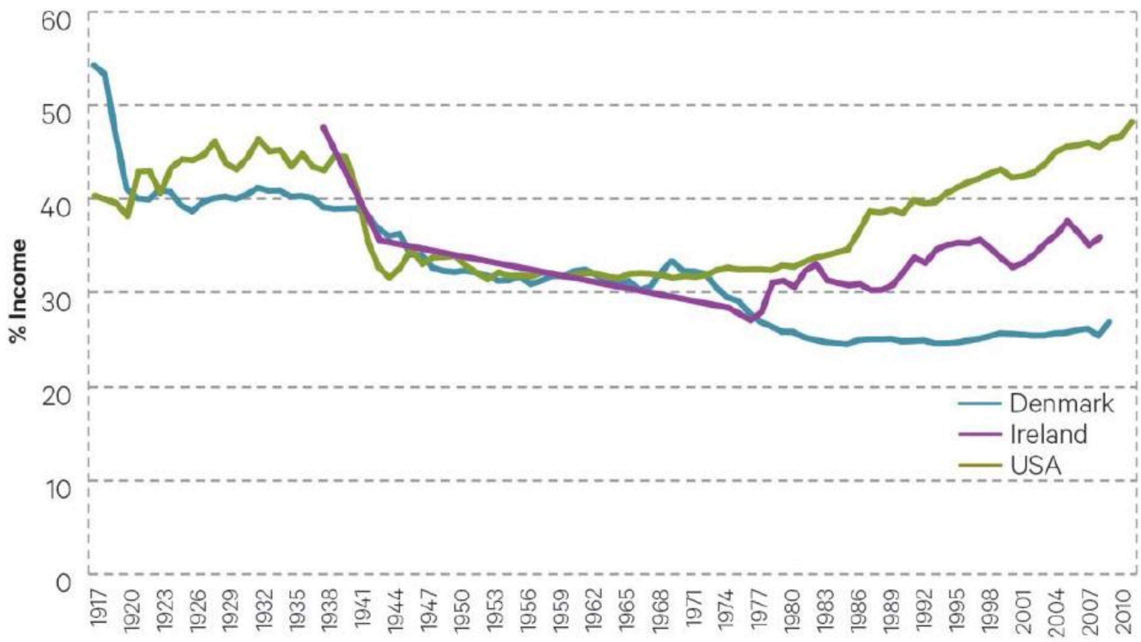
strongest negative growth' in the EU-15[89]. Figure 1.10 shows how this has led to a growing share of national income for the top 1%[90].

Figure 1.10 Share of income before taxes and transfers of top 1% and Bottom 90%[91]



[89] EC, "The Labour Income Share in the European Union," in *Employment in Europe 2007*, 2008, 244.
[90] Cormac Staunton, "Cherishing All Equally – Economic Inequality in Ireland," June 19, 2015, 4, http://www.tasc.ie/download/pdf/cormac_staunton_inequality_ireland_june15.pdf.
[91] Ibid.

Figure 1.11 Share of income before taxes and transfers of top 10% - Denmark, Ireland & US[92]



Until the crash, this increasing inequality was masked by the trade union leadership's trading of wage increases in line with profit or productivity growth for income tax cuts. In the words of Rob Wright, the right wing Canadian civil servant hired by the government to assess the Department of Finance's role in the crisis, 'in the 1990s, the most important change was a breakthrough, through the social partnership, to say "let's reduce wages substantially and reduce taxes"'[93] . So if workers felt better off, it was primarily due to lower income tax not wage increases. Wages fell behind profits, leading to a declining labour share, a rising profit share and rising inequality. Meanwhile, demobilised by social partnership, trade union membership halved in percentage terms[94], which reinforced the downward spiral.

As the bubble inflated, more and more workers began to feel *worse off* due to rampant inflation, caused by a level of profiteering/price gouging that even income tax cuts and moderate wage increases couldn't compensate for. Prices in general rose 38% from 2000-2008, meaning something that cost €100 in 2000 cost €138 in 2008[95]. Meanwhile, from 1993-2007, house prices quadrupled; a rate of inflation 'among the highest of any advanced economies', according to EC Director-General for Economic and Financial Affairs, Marco Buti[96]. That's why the RTE programme, *Rip Off Republic*, was such a ratings success in 2005, and why there was a real *need* for wage increases in the public

[92] Ibid., 6.
[93] "Transcript of Rob Wright Hearing," December 18, 2014, 53, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2014/12/18122014_Wright_vol1.pdf.
[94] "Transcript of Terrence McDonough Hearing," 553.
[95] inflation.eu, "Historic Inflation Ireland – Historic CPI Inflation Ireland," 2015, http://www.inflation.eu/inflation-rates/ireland/historic-inflation/cpi-inflation-ireland.aspx.
[96] "Transcipt of 1st Marco Buti Hearing," February 18, 2015, 380.

and private sectors. As Joe Higgins said to Rob Wright, who was critical of wage increases for workers *and* removing workers on the minimum wage from the tax net:

> What else would young nurses, teachers and public servants – many of whom are on low or middle incomes – have done but seek wage increases when their accommodation costs were going through the roof? It was a case of their seeking wage increases or living in tents…[97]

This reality of rising living costs has been obscured by right wing economists and politicians who have focused on wage increases in isolation from the profit share and often while misleadingly comparing them to European countries that had higher wage levels to begin with in order to portray Irish wage increases as excessive. This has enabled them to claim that wage inflation was a *cause* of the crash through a loss of 'competitiveness'.

What was really happening was profiteering by capitalists, on the one hand through price gouging and on the other by taking an ever-increasing *profit share* of output/income. This enabled supernormal amounts of profits to be maintained at a time when *rates* of profit were low or decreasing (the reasons rates of profit fell are explained later). The result was a massive accumulation of profit and wealth for the richest in society and a widening chasm with those at the bottom. Newspaper 'Rich Lists' show that in 1998, the wealthiest 100 people in Ireland were worth €10.8bn[98] whereas by March 2008 just the richest *50* had €35bn[99].

What was happening in Ireland was part of a global phenomenon. Along with the liberalisation of global financial markets and the increased leverage allowed under lax financial regulation, rising wealth inequality fuelled a tsunami of money flooding the financial markets before the tide turned with the credit crunch. This coincided with low interest rates[100], which accelerated a worldwide 'search for yield' by the rich and further financialisation through inventing exotic financial products to satisfy it.

Joe Higgins put this analysis to the current Governor of the Central Bank, Professor Philip Lane, pointing out that according to Oxfam, 'in 2007, at the beginning of the crash, the 80 richest billionaires had $1.5 trillion in the markets'[101] – which was roughly equivalent to China's cash reserves[102]. Lane replied:

> That is definitely a big part of the mechanics of what went on. Let us remember that the reason that the frenetic innovation was taking place was that interest rates were so low that many investors in order for them to be able to offer a reasonable return had to do

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[97] "Transcript of Rob Wright Hearing," 94.

[98] Ken Foxe, "MEET THE RICHEST 100 PEOPLE IN IRELAND WORTH POUNDS 8.5 BILLION; 100 RICHEST PEOPLE IN IRELAND," *Irish Daily Mirror*, March 20, 1998.

[99] "The Rich List Top 100," *Sunday Independent*, March 30, 2008.

[100] The superficial explanation in mainstream monetarist economic theory is that the price of money falls when there is more of it around. Frank Browne expresses this view in his written statement: 'Persistent excess liquidity tends to lower the actual real interest rate relative to its equilibrium (or natural) level.' "Witness Statement of Frank Browne," 83.

[101] "Transcript of Philip Lane Hearing," January 21, 2015, 205–206, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/01/21012015_philliplane_vol1.pdf.

[102] Lapavitsas, *Profiting without Producing*, chap. 8 Table 1 Reserves of emerging and developing countries, US $bn.

> something different…All of these new types of products were being driven by a "search for yield". How in this environment can investment make a bit extra? The ideal is to find something that makes a bit extra but looks safe. This is the reason for securitisations - trying to come up with AAA, which was not safe.

Joe Higgins then asked:

> With that increasing share to profit, interest and rent and less for working people, does Professor Lane see that as a background to working people being forced to borrow more to buy the products that they could not afford from their ordinary wages and then on the other hand these funds that we have been talking about lending to them to try to boost their profits?

Lane responded:

> I think that is a really important part of what went on. That is one consequence of the decline in the labour share. One of the puzzles since the late 1990s is that profits have been relatively high but firms have not invested so much. Increasingly firms sit on a great deal of cash…On the other side of that is the fact that labour incomes in many countries were stagnating…the high increase in household debt was, at least in part, being driven by the stagnation of wages.

Essentially, Lane was agreeing here with one of the better known Marxist or Keynesian explanations of economic crises – namely that inequality leads to crises. When the majority of workers don't earn enough to buy the goods capitalists produce – and they can't keep borrowing forever – the market for those goods will eventually collapse. The most obvious example is the housing bubble. With house prices having increased by the equivalent of the average industrial wage every year for ten years and mortgage debt also rising exponentially faster than wages, a tipping point was reached where houses were no longer affordable and the market collapsed. The same happened with consumer goods in general, as evidenced by the high rate of inflation before the crash and the collapse of domestic demand afterward.

Joe Higgins questioned Professor Lane further on this point:

> Why were countless billions of euro and dollars cascading around the financial markets in this way and why were so many exotic products developed? Why was the money in question not invested in manufacturing, for example, particularly in view of the fact that 25 million people in the European Union were unemployed? Why were billions poured into property speculation in Ireland at a time when, by common consent, broadband infrastructure and water infrastructure were in desperate need of investment?

Lane's response was:

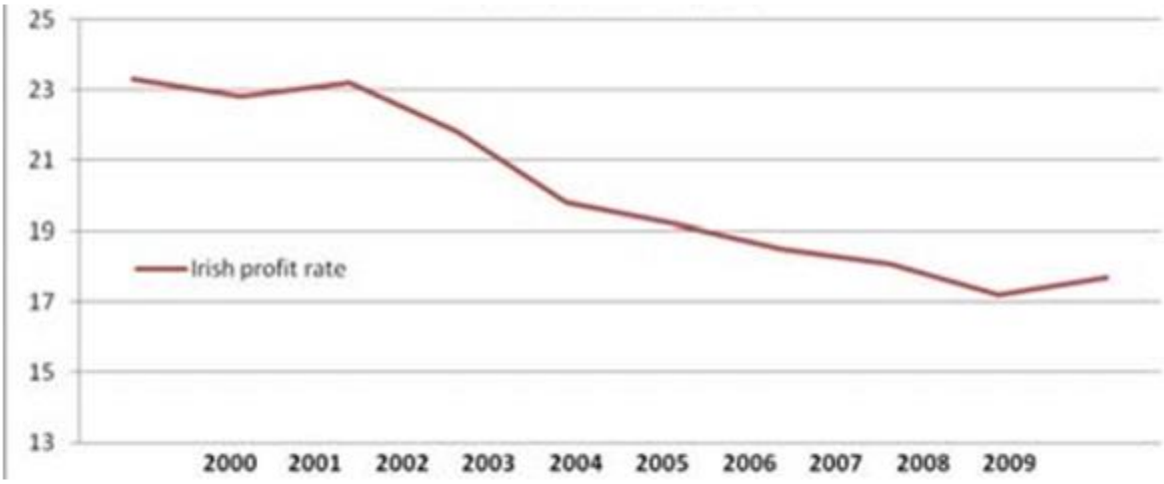
> There is a global issue here. Investment rates, in terms of the real or productive economy, have been low in Asia and in the advanced economies. Some of the stories people tell essentially revolve around competition. With the rise of new competitors from the emerging world, it is not super-clear what is the right investment strategy for many corporations…I

agree that the fact so much was invested in property reflects some kind of distortion in how the world economy works.

Falling rate of profit prompts financial speculation by major profit seekers

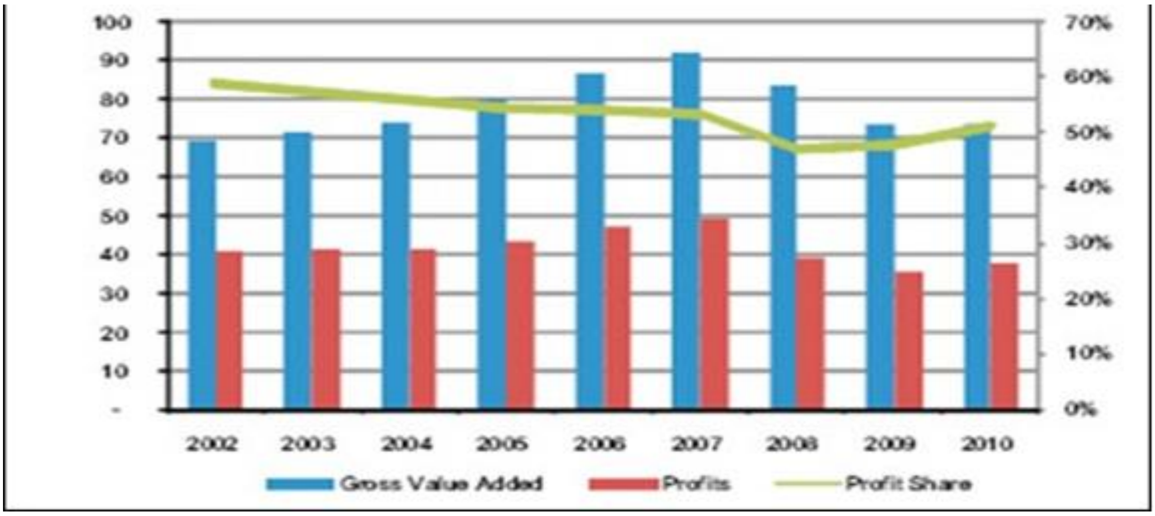
Professor Lane's 'puzzle' – i.e. 'that profits have been relatively high but firms have not invested so much' – may be explained in terms of Marx's law of the tendency of the *rate* of profit to fall. It's not possible to elaborate here in great detail but a brief examination is necessary to complete the explanation as to why trillions, instead of going into research and the development of new products, were, instead, moving around the world's financial markets as if they were a global casino. Economist, Michael Burke, has shown how, in line with global trends, the *rate* of profit was falling in Ireland in the run-up to the crash even as the *amount* of profits was still rising (Figures 1.12 and 1.13).

Figure 1.12 Irish rate of profit 2000-2009[103]



[103] Michael Burke, "The Causes of the Irish Depression," *The Citizen*, no. 4 (September 2011), http://www.theirelandinstitute.com/citizen/c04-burke-page.html.

Figure 1.13 Amount of Profits and Profit Share of Gross Value Added of Non-Financial Corporations 2002-2010[104]



Marx's explanation was that, over time, the capital investment firms need to compete, in terms of technology etc., tend to increase, which lowers the rate of profit. Another process inherent to capitalism that can have a similar effect is competition, or the 'race to the bottom' dynamic, which tends towards lower prices and lower profit margins.

There are four main ways capitalists can counteract this:

1) sell more to compensate for a lower margin per product
2) move into areas of business with a higher margin
3) cut costs – by cutting wages and/or jobs and making remaining employees work harder (i.e. reduce the labour share); or lowering other costs, for instance through lobbying for lower taxes and less regulation, or slashing health and safety standards
4) increase productivity through innovation or upskilling. This can temporarily give an innovative company an edge but ultimately increases investment costs for everyone, starting the cycle all over again.

All the above happened in the Irish economy in general and Irish banking in particular in the run-up to the crash. Due to low rates of profit in the global and Irish economies generally, capitalists increasingly moved out of long-term productive activities like manufacturing and into speculative areas like property and finance where they could (temporarily) achieve higher rates of profit. Yet even in banking, competitive pressures increasingly cut into profit margins as foreign banks entered the Irish market and lowered interest rates. Irish banks responded by: massively expanding lending to compensate for falling margins, particularly increasing high risk commercial property lending to developers and property speculators that attracted higher rates of interest; cutting credit standards and staff numbers; and dabbling in new forms of financial engineering like securitisation that also enabled them to lend more.

[104] Michael Burke, "The Relation of Profits and 'Austerity,'" *Socialist Economic Bulletin*, October 25, 2011, http://socialisteconomicbulletin.blogspot.ie/2011/10/relation-of-profits-and-austerity.html.

Professor David Harvey, who was invited to appear before the Inquiry as an expert witness but was unfortunately unavailable to attend, explains how low rates of profit can lead to financial speculation being seen an easier, less risky option than productive investment[105] :

> During these past years, monetary authorities such as the International Monetary Fund have frequently commented that the "world is awash with surplus liquidity", that is, there is an increasing mass of money looking for something profitable to engage in…Less and less of the surplus capital has been absorbed into production (in spite of everything that has happened in China) because global profit margins began to fall after a brief revival in the 1980s…in spite of an abundance of low-wage labour. Low wages and low profits are a peculiar combination. As a result, more and more money went into speculation on asset values because that was where the profits were to be had. Why invest in low-profit production when you can borrow in Japan at a zero rate of interest and invest in London at 7 per cent while hedging your bets on a possible deleterious shift in the yen-sterling exchange rate? And in any case, it was right around this time that the debt explosion and the new derivatives market took off…Who needed to bother with investing in production when all this was going on? This was the moment when the financialisation of capitalism's crisis tendencies truly began[106].

As a globalised, financialised tax and regulatory haven, Ireland sucked in huge amounts of this foreign capital seeking a higher after tax rate of profit and a 'Wild West' for financial speculation free from interference. Whereas the response globally to falling rates of profit has been to resort to financial engineering (much of it ultimately based in property via mortgage securitisation), Ireland's indigenous capitalists largely just resorted to 'a plain vanilla property bubble'[107].

Neoliberal ideology

Underpinning the thrust toward globalisation, financialisation, rising inequality, and the pushing downwards of workers' rights, conditions and wages, was the spread of a neoliberal ideology of market fundamentalism that supports and justifies it. Its basic tenets are that left to themselves markets are rational, efficient and self-regulating and governments should only intervene to promote them, for instance by weakening regulation, abolishing barriers to trade and encouraging competition. As Nyberg[108] put it in his report:

> For several years before the banking crisis, the authorities operated under the assumption that financial markets generally were efficient and self-regulating; this was generally considered as the modern and reasonable approach both in Ireland and abroad.

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[105] Harvey, *The Enigma of Capital and the Crises of Capitalism*, 28–29.
[106] Explanations of crisis the tendency of the rate of profit to fall and based on repression of labour/inequality are often portrayed as conflicting but they can also be compatible if the repression of labour and resulting under-consumption was a response to a fall in the underlying rate of profit, rather than just something capitalists always do to maximise their profits whether they are falling or not. The two theories also have in common the identification of vast stores of profit or wealth as a problem for global capitalism rather than merely a result of its 'success' – albeit for different reasons.
[107] Regling and Watson, "A Preliminary Report on the Sources of Ireland's Banking Crisis," 6.
[108] "Nyberg Report," 59.

This analysis was confirmed by a procession of different witnesses. The EC Director-General for Economic and Financial Affairs, Marco Buti[109], told the Inquiry that

> The financial sector was thought to simply channel funds in an efficient manner to where the real economy needed them. Dangerous excesses were thought to originate only in monetary and fiscal policy making.

This encapsulates another core aspect of the neoliberal ideology – that only the state is capable of making mistakes and that 'the market' is possessed of infinite wisdom and foresight. Pressed by Joe Higgins on how it was possible to persist in this belief in light of 'housing property bubbles in Finland in the 1970s and in the Netherlands in the 1980s which crashed and caused havoc' and another 'few dozen OECD countries' with 'housing bubbles which had a similar effect over the previous 20 years', Buti replied, 'this was the paradigm at the time. It was shared by the EU institutions, the IMF, the OECD and so forth.'[110] He also pointed out that 'The line-up of guests which has preceded me has indicated that they were in a sense clouded by the same type of views'[111]

The former Chair of the Financial Regulator, Brian Patterson, confirmed the dominance of neoliberal ideology among the people supposedly charged with regulating the banks[112]:

> In an era of de-regulation and belief in free-market policies, principles-based regulation was based on the belief that:
>
> - The market should be allowed to operate freely; the Regulator should not interfere in product design or pricing…

This dogma was conveniently compatible with marketing Ireland as a regulatory haven and so guarded against any discomfiting cognitive dissonance for regulators that weren't doing any regulating. The only exception to this policy of non-interference was efforts to make the market even *more* competitive, accelerating an already self-destructive 'race to the bottom'. Neoliberal ideology was so internalised that competition itself was seen as a 'natural' form of regulation intrinsic to markets and so self-evidently superior to anything that could be clumsily devised by states. This self-limiting creed leaps out of the Financial Regulator's *2006 Annual Report*, which manages to reference competition twice in the title and a hundred times in the report. It preaches to the 'consumers' of Ireland:

> When consumers exercise choice, this fosters competition - which in turn increases value to the consumer. So we foster competition between the providers of financial services. We work constructively with them on competitiveness and innovation. So, we have placed the consumer at the heart of financial regulation…

A few pages later, another reading from the Gospel according to Milton Friedman is delivered:

> We strive to facilitate competition in the financial services market. Markets only work well if both sides of the market are functioning properly - the suppliers and the buyers. If

[109] Buti, "Transcipt of 1st Marco Buti Hearing," 382–383.
[110] Ibid., 396.
[111] Ibid., 390–391.
[112] Patterson, "Opening Statement to the Banking Inquiry," 5.

> consumers use their buying power they can effect real change in the level of competition in the financial services market[113].

Joe Higgins questioned Patrick Honohan about the role of this free market ideology in the crash:

> Some people would feel that…in trying to get to this mystery of why there was not an intervention to stop the property bubble being blown up, there is too much tiptoeing through the tulips and that we can get to a very fundamental reason. Is it the case that the property bubble was blown to extremes by this scramble for super-profits by banks, developers and bondholders, that this is what the capitalist financial markets are all about, that this ideology is shared by Government, the majority of the Legislature in this State and by much of the media, and also that the regulatory authorities, most of whom came through that system, share that and that the prevailing spirit is, "Don't separate the lion from its prey. That is what they do. Let them at it"?

Honohan replied simply: 'That is right.'[114]

Although witness after witness attested to the dominance of neoliberal free market ideology as a cause of the crash, what they generally failed to mention is that it remains the dominant ideology in Ireland and internationally. In many respects, it has emerged even stronger from the crisis with only lip-service now paid to the need for stronger financial regulation, even as forty Irish bankers and more than 3,000 across the EU continue to rake in over a million euros a year in 'compensation'[115]. To explain its persistence despite its having been utterly intellectually discredited by the crash requires examining the elephant in the room. It was not so much ideology as profit and collective self-interest that blinded the ruling class, in Ireland and internationally, to the dangers of what was going on.

[113] Financial Regulator, "Consumer Protection with Innovation, Competitiveness and Competition: 2006 Annual Report of the Financial Regulator," 6; 10.
[114] "Transcript of First Honohan Hearing," 141.
[115] European Banking Authority, "Benchmarking of Remuneration Practices at Union Level and Data on High Earners," September 2015, http://www.eba.europa.eu/documents/10180/950548/Report+on+Benchmarking+of+Remuneration+and+on+High+Earners+2013.pdf.

Chapter 2 – The Bubble and the Banks

Introduction

From the late 1990s to the crash, a 'world-beating property bubble'[116] was blown up in Ireland based on an enormous expansion of credit, particularly from 2003-2008 (Figures 2.1 & 2.2), and growing inequality of wealth. The one and only motive for this lending growth was profit. According to the Nyberg Report:

> High profit growth was the primary strategic focus of the covered banks…Since the potential for high growth (in assets) and resultant profitability in Ireland were to be found primarily in the property market, bank lending became increasingly concentrated there[117].

Within property lending, it was *commercial property lending*[118] to builders, developers, landowners, commercial landlords and other property investors that caused the banks to fail. By 2008, the banks had given out an incredible €158bn in commercial property loans[119] – equivalent to Ireland's entire Gross National Income in 2008[120]. Traditionally, mortgage lending had been the largest activity for Irish banks but by 2008, commercial property lending had become predominant (Figures 2.3-2.6)[121]. This was where the vast majority of the banks' losses came from and where the vast majority of the bank bailout went. The banks with the most commercial property loans made the biggest losses and got the biggest bailouts (Figure 2.7)

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116 Patrick Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," May 31, 2010, 19.
117 Peter Nyberg, "Misjuding Risk - Causes of the Systemic Banking Crisis in Ireland: Report of the Commission of Investigation into the Banking Sector In Ireland," March 2011, 49.
118 The phrase 'commercial property' is used here to refer to all loans to builders, developers and other property investors for residential or non-residential property development/acquisition/investment/construction, whose purpose is to make a profit, excluding Buy-To-Let mortgages. See Glossary for definitions of the terms used in this report.
119 Brendan McDonagh, "NAMA Update," 2014, 5.
120 CSO, "Ireland: GDP and GNI, 2003-2012," in *Measuring Ireland's Progress 2012*, 2012, http://www.cso.ie/en/releasesandpublications/ep/p-mip/measuringirelandsprogress2012/economy/economy-finance/.
121 Five years earlier, the banks had

Figure 2.1 Lending by the Six Irish Banks 2002-2008

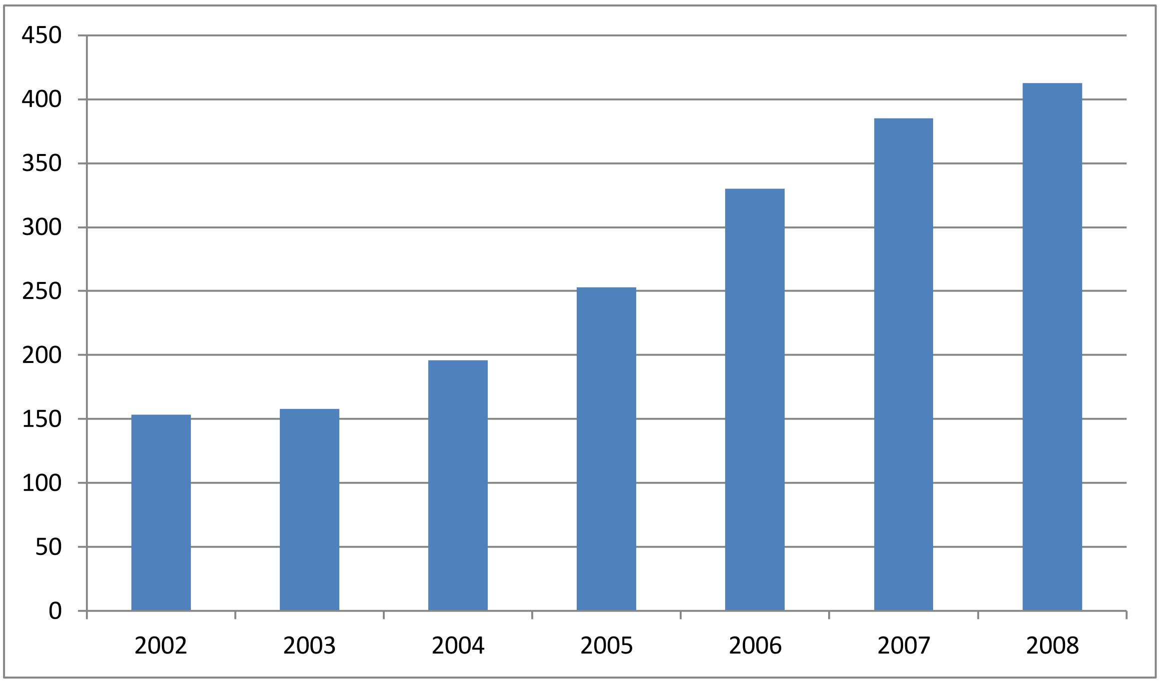
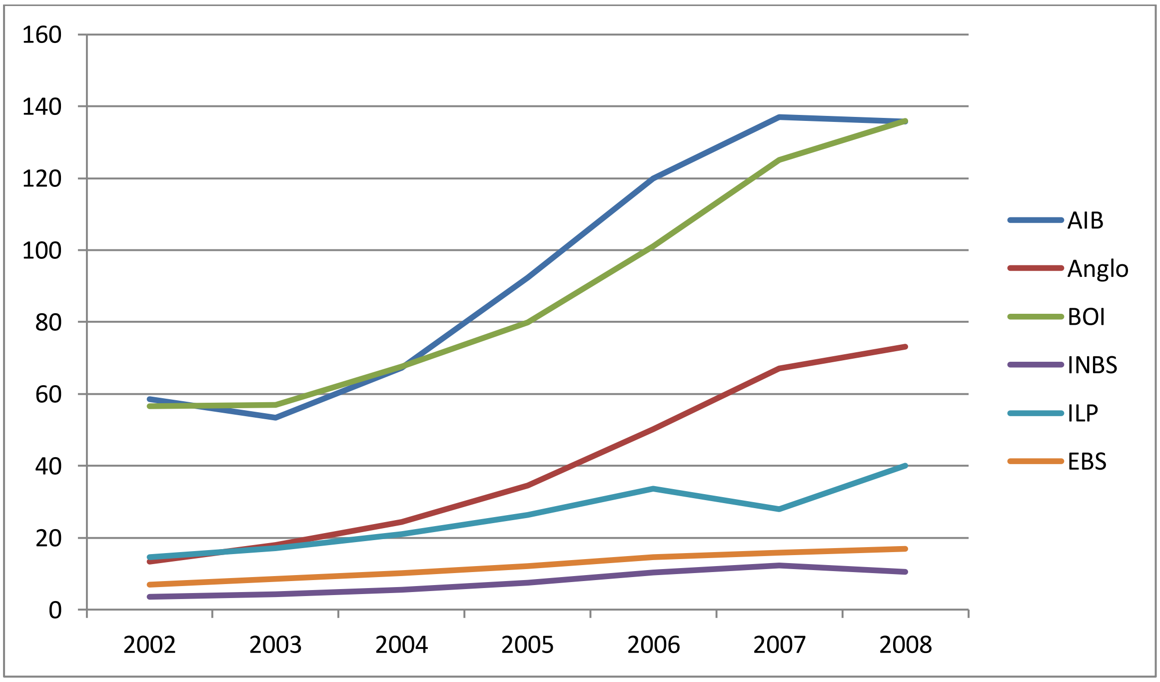


Figure 2.2 Lending by Bank 2002-2008[122]



[122] Based on banks' Annual Reports.

Figure 2.3 Irish Banks' Commercial Property & Mortgage Lending 2003-2008 €bn[123]

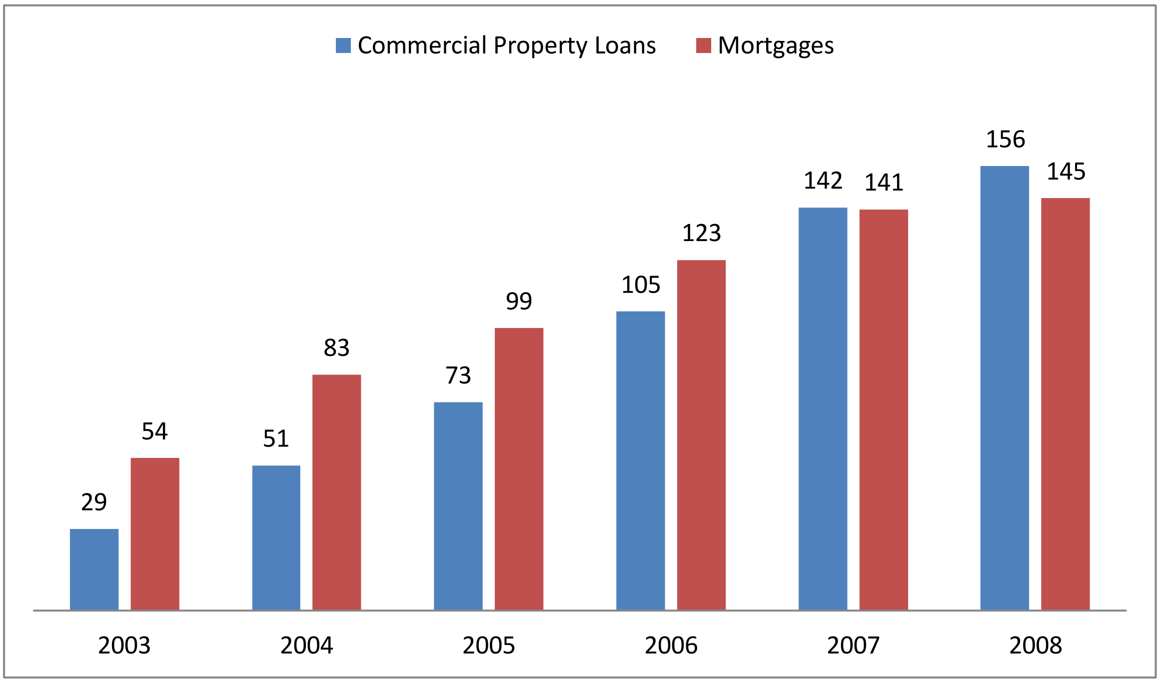


Figure 2.4 Commercial Property Lending by Bank 2003-2008[124]

[123] NAMA, "Supplementary Documentation," September 19, 2009, https://www.nama.ie/fileadmin/user_upload/Supplementary_Documentation.pdf.. There is a discrepancy of €2bn between the figure of €156bn in total commercial property loans provided by NAMA in 2009 and the €158bn figure later cited by Brendan McDonagh, which may be due to the reclassification of some loans McDonagh, "NAMA Update," 5.

[124] NAMA, "Supplementary Documentation," 65. Anglo figures based on NAMA estimate that 84% of its loans in 2008 were for commercial property.

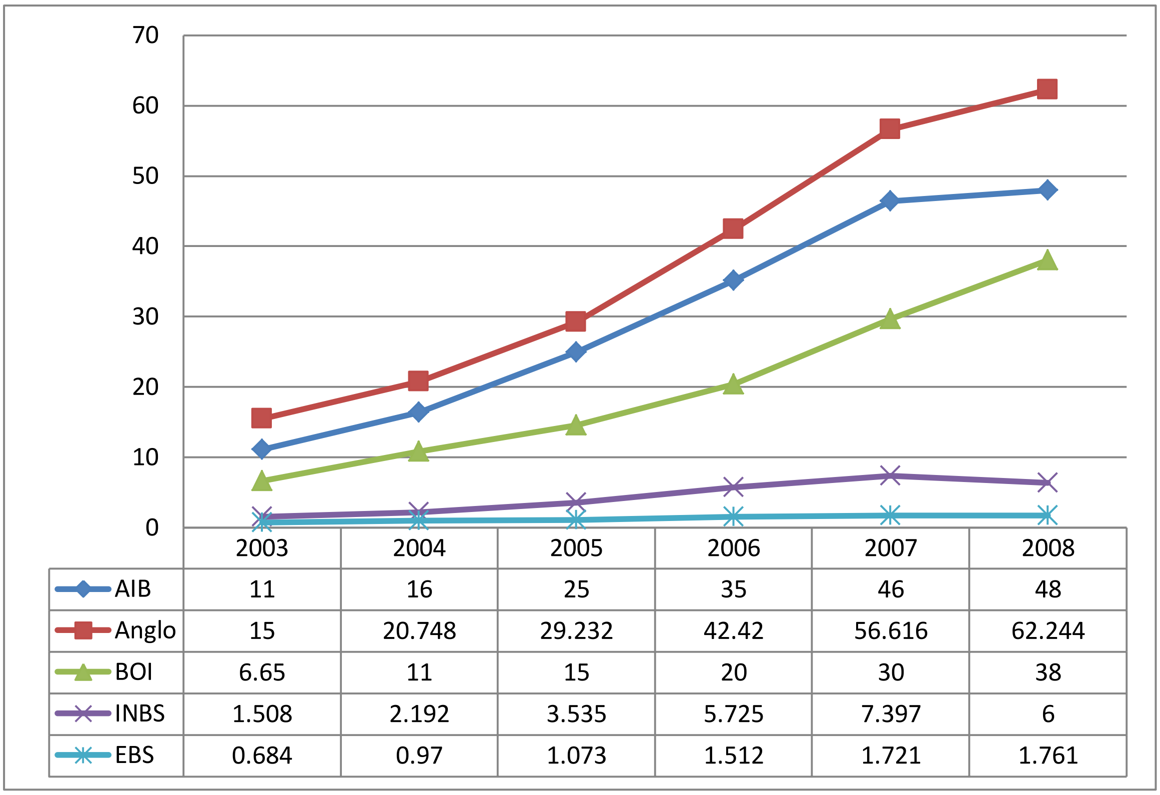


Table 2.1 Annual Growth Rate of Commercial Property Lending by Bank 2004-2008

	2004	2005	2006	2007	2008
AIB	45%	56%	40%	31%	7%
Anglo	38%	41%	45%	33%	10%
BOI	65%	36%	33%	50%	27%
INBS	45%	61%	62%	29%	-19%
EBS	29%	11%	29%	14%	2%

Figure 2.5 Breakdown of the Six Banks' Loan Books 2008[125]

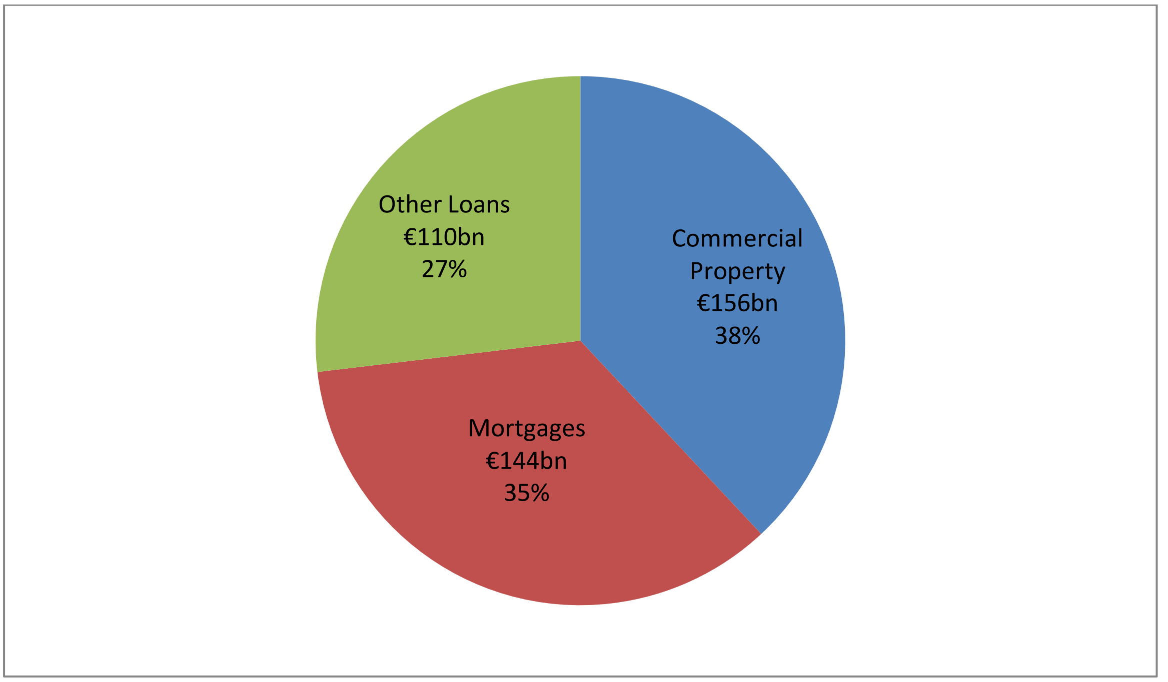
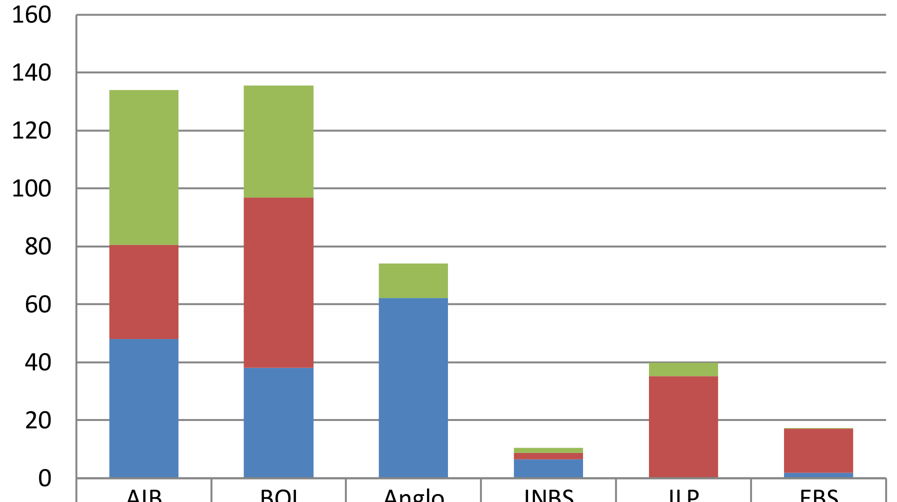


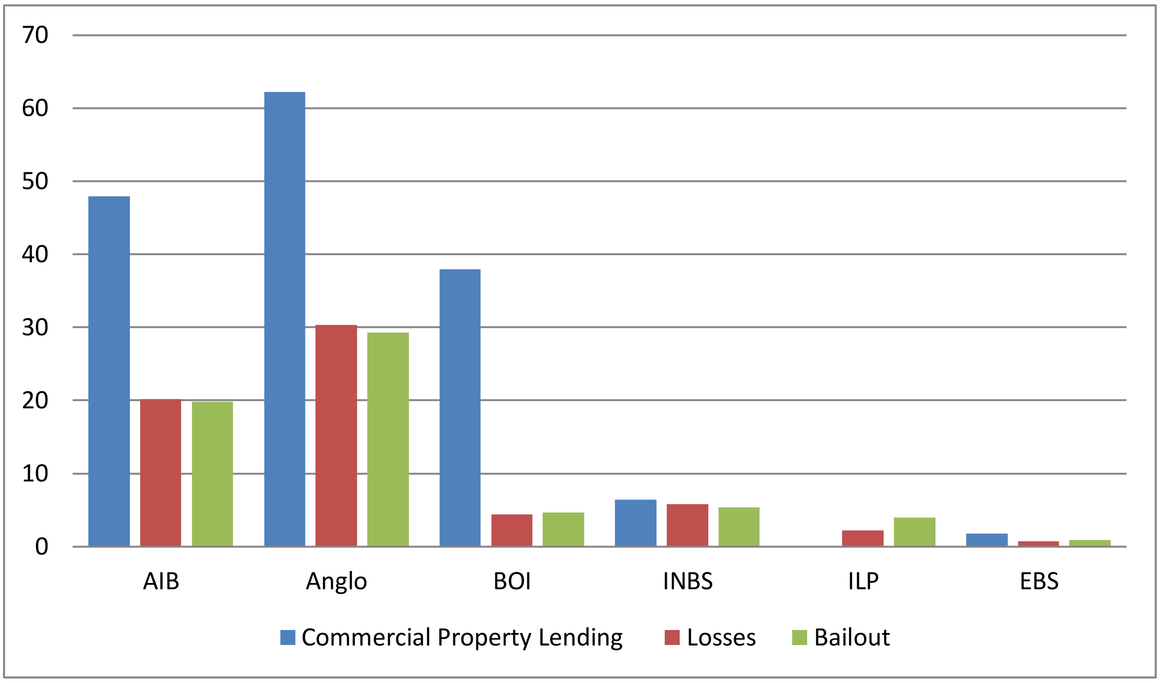
Figure 2.6 Breakdown of the Banks' Loan Books by Bank €bn 2008[126]



	AIB	BOI	Anglo	INBS	ILP	EBS
Other Loans	53	39	12	2	5	0
Mortgages	33	59	0	2	35	15
Commercial Property	48	38	62	6	0	2

[125] NAMA, "Supplementary Documentation."
[126] Ibid.

Figure 2.7 Commercial Property Lending vs. Losses & Bailouts €bn



This crucial fact can get drowned out in the propaganda from the media and establishment politicians that "we all partied" and are somehow all to blame, just because some of us bought houses to live in. As the former Central Bank Governor, Patrick Honohan, told the Inquiry:

> had there been no losses on [the commercial property loans transferred to NAMA], the net fiscal cost of the assumption of banking liabilities would have been small. In other words, the main banks had enough pre-crisis capital…to absorb the actual and prospective losses on residential mortgages'[127].

Likewise, the first official report on the banking crisis by Regling and Watson[128] found that 'By far the most serious macrofinancial flaw was the over-exposure of institutions to commercial property, with this vulnerability being heightened by a high concentration of lending to a small number of borrowers'.

From 2009-2013, the banks lost €65bn and received a €64bn bailout from the state. €42bn of this came from losses on the €74bn in commercial property loans to developers and property speculators that were transferred to NAMA[129]. Losses on the remaining €82bn in commercial

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[127] Patrick Honohan, "STATEMENT BY PATRICK HONOHAN TO THE BANKING INQUIRY 'Nexus Phase,'" May 28, 2015, 8.

[128] Klaus Regling and Maxwell Watson, "A Preliminary Report on the Sources of Ireland's Banking Crisis," 2010, 40, http://www.betterregulation.com/external/A%20Preliminary%20Report%20on%20The%20Sources%20of%20Irelands%20Banking%20Crisis.pdf.

[129] NAMA acquired loans with a face value of €74bn and paid €32bn for them, crystallising a €42bn loss.

property loans left on the banks' books[130] made up much of the rest. Another major contributing factor was buy-to-let loans to landlords, which made up nearly a quarter of all Irish mortgages[131]. Around €21bn of this was lent by Irish banks to landlords in Ireland[132] although Irish banks also had significant amounts of buy-to-let lending in the UK. Buy-to-lets have been a slower burning fuse on the banks' balance sheets but have also caused billions in losses. They have now also become one of the main causes of homelessness, as repossessions by the banks are throwing tenants out onto the streets into the worst housing crisis in over 50 years. Commercial property and buy-to-let loans are still causing the biggest losses even now when the banks' owner-occupier mortgage books are much larger[133]. This is because ordinary mortgage holders have been hounded to the ends of the earth for their mortgage arrears while speculators have had their gambling debts written off at our expense[134].

Bill Black's Recipe: How Banks Make Profits and Bankers Get Rich

To understand how this disaster for ordinary people came about, we have to go back to the 'boom' years when the bubble was being inflated. US regulator, Bill Black, appeared before the Inquiry as an expert witness and outlined a 'recipe' banks follow which 'produces the worst losses, is most likely to cause hyperinflated bubbles, is most likely to cause catastrophic individual losses, and is most likely to cause future crises'. The first ingredient is to 'grow like crazy'; the second is to 'make terrible quality loans'[135]. Consciously or not, all the Irish banks followed this recipe in the run-up to the crash and Black's three 'sure things' resulted: 'record profits', 'Under modern executive compensation the senior leadership [was] promptly…made wealthy' and 'catastrophic losses'[136] . This was entirely

[130] At AIB and BOI, only the debts of commercial property borrowers who owed more than €20m were transferred to NAMA, leaving lots of smaller loans in place Comptroller and Auditor General, "National Asset Management Agency Progress Report 2010 - 2012," Comptroller and Auditor General Special Report, (April 2014), 19. By 2013, AIB still had €19.7bn of commercial property loans on its balance sheet. AIB, "Annual Report 2013," 2014, 95, http://investorrelations.aib.ie/content/dam/aib/investorrelations/docs/resultscentre/annualreport/annual-report-2013.pdf. BOI had €16.8bn BOI, "Annual Report 2013," 2014, 80, http://www.bankofireland.com/mwg-internal/de5fs23hu73ds/progress?id=o4K41RXtm8kzG6_O24yAr7LKzumY0z_qjvfgM39sX9E,&dl..

[131] Central Bank, "Sectoral Developments in Private-Sector Credit - December 2007," 2008, 6, http://www.centralbank.ie/press-area/press-releases/Documents/Sectoral%20Developments%20in%20Private-Sector%20Credit%20-%20December%202007.pdf.

[132] Nyberg, "Nyberg Report," 16; Central Bank, "Sectoral Developments in Private-Sector Credit - December 2007," 6.

[133] For instance, AIB wrote off over €4bn in commercial property loans from January 2014-end June 2015 AIB, "Half Yearly Financial Report 2015," August 6, 2015, 71, https://investorrelations.aib.ie/content/dam/aib/investorrelations/docs/resultscentre/resultspresentation/aib-half-yearly-financial-report-2015.pdf., compared to €823m on all mortgages, including BTLs. despite the fact that it has 2¾ times as much mortgage loans. Moreover, 40% of its BTL book is impaired, compared to 15% of its owner-occupier mortgages so the majority of the €823m will have been for BTLs. Likewise, at Irish Life & Permanent(ILP)/PTSB, two-thirds of its impairment charges in 2012 (which was the year it lost the most money) originated from commercial property loans and buy-to-lets even though these only made up a quarter of its loan book PTSB, "Annual Report 2012," 2013, 5; 7, http://www.permanenttsbgroup.ie/~/media/Files/I/Irish-Life-And-Permanent/Attachments/pdf/2012/310-annual-report-ptsb.pdf?

[134] PTSB, "Annual Report 2012," 5; 7.

[135] Bill Black, "Transcript of Bill Black Hearing," February 5, 2015, 261.

[136] Ibid.

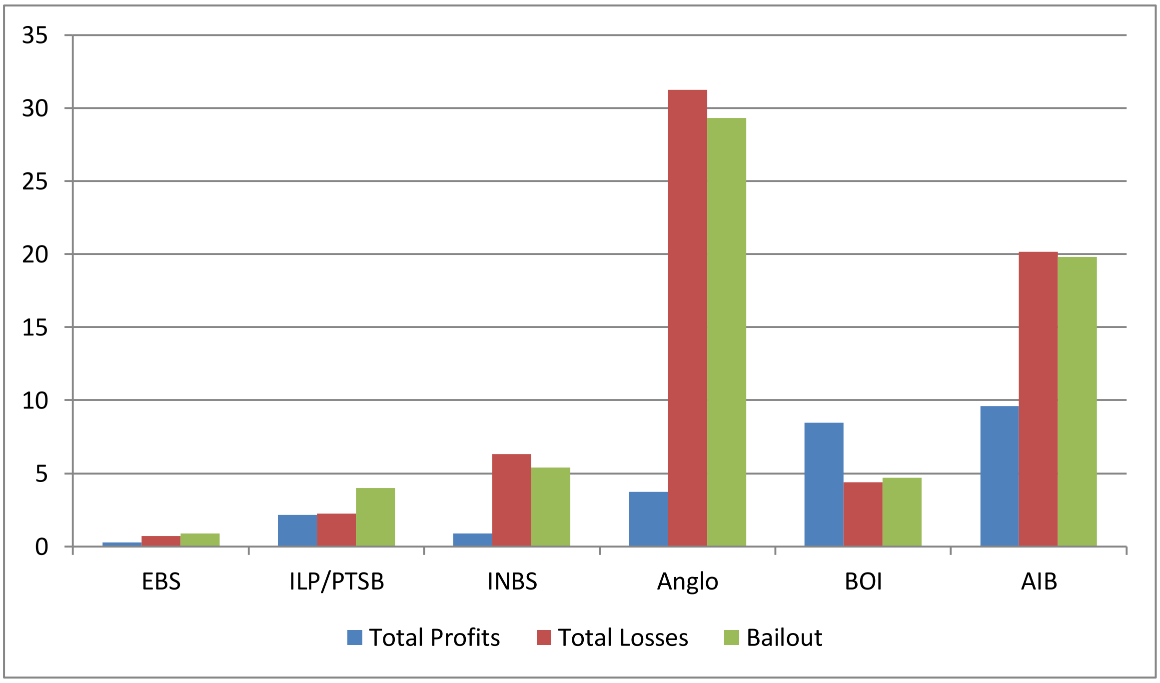
predictable as the recipe is the fastest way to make profits and profit-making is the *raison d'être* of banks – and all other capitalist enterprises.

In the context of a neoliberal ideology of free markets and Ireland's victory in the EU's regulatory race to the bottom, there was nothing stopping them. Far from it, regulators and establishment politicians bent over backwards to help them follow the recipe, right up until September 2008 when they obligingly guaranteed all the losses caused by their mega-profits. As Minister for Finance, Brian Cowen, fawned to the Institute of Bankers in November 2006:

> you are players on the field and I'm just an ardent supporter on the sidelines. I will continue to wear your colours. Well done on yet another very successful year for your sector – I hope you have a most enjoyable evening[137].

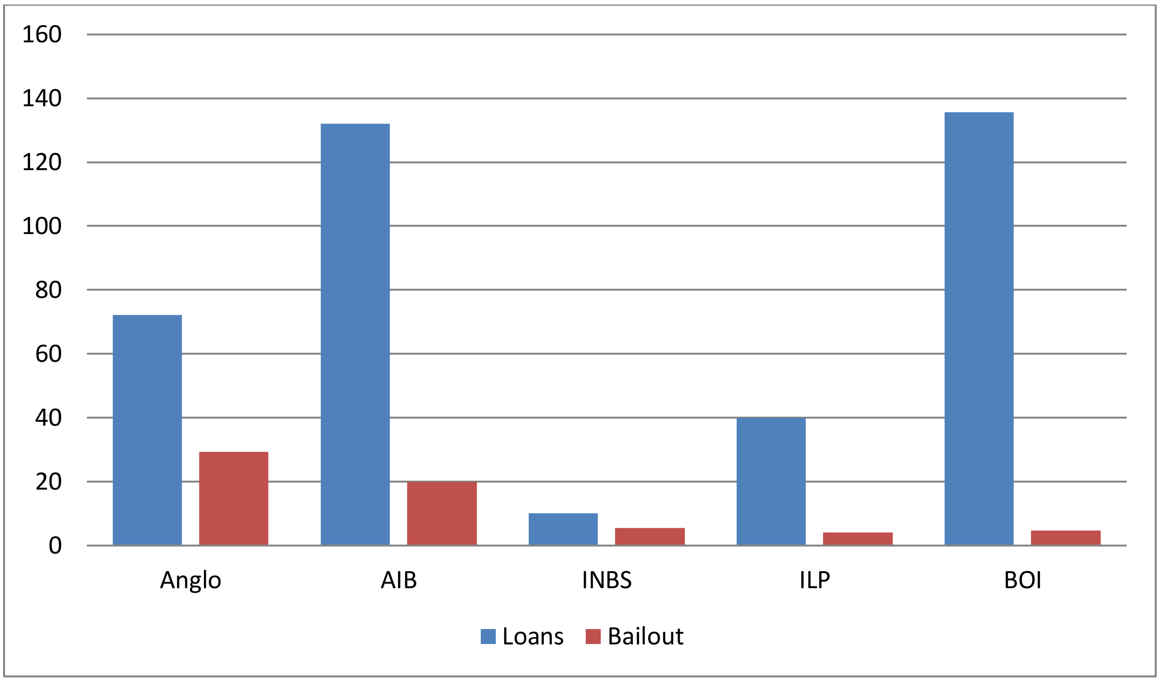
That same year, the IMF reported 'Irish banking sector profits are currently amongst the highest in western Europe'[138] . In total, from 2002-8, the banks' reported profits of €25bn.The biggest profits before the crash corresponded to the biggest losses after it and the biggest bailouts from all of us (Figure 2.8).

Figure 2.8 Profits[139] vs. Losses by Bank 2002-2014 €bn



[137] Brian Cowen, "Address by the Minister for Finance, Brian Cowen, TD, to the Institute of Bankers in Ireland Annual Dinner - 2 November 2006.," November 2, 2006, http://oldwww.finance.gov.ie/viewdoc.asp?DocID=4325.
[138] quoted in Craig Beaumont, "Written Statement of Craig Beaumont," October 2015, 25.
[139] after tax

Figure 2.9 Size of Loan Book (2008) vs. Bailout



Throughout this report, there will be a particular focus on Anglo and AIB, which between them did well over three-quarters of the damage, and INBS, which performed even worse than Anglo relative to its size. The INBS bailout equated to an incredible 54% of its 2008 loan book, compared to 40.6% for Anglo, 15% for AIB, 10% for ILP and 3.5% for BOI (Figure 2.9).

The massive increase in bank profits in the 2000s had been consciously strategised for by bank management. For instance, AIB had set itself the goal to 'double pre-tax profits' between 2000-2005[140] and its Senior Management Conference in 2004 cited Anglo's 30% growth in Earnings per Share as a benchmark for its own target of "double digit growth"[141]. The result across the banks, as the Irish Bank Officials' Union (IBOA) warned the Oireachtas Finance Committee back in 2004, was "a dominant culture emanating from the top down of profit before everything. Profit comes before service and the customer, before ethics and the highest standards and profit comes before the welfare of staff."[142] The head of the IBOA, Larry Broderick, elaborated on this in his statement, arguing that

> one of the major contributory factors in the virtual collapse of the banking sector was the transformation of its prevailing culture…to one dictated by sales targets driven by the demand at Board level for shareholder value to be maximised. These targets were pursued ruthlessly and relentlessly through a policy of short-term profit-taking directed by senior executives who stood, at the time, to be rewarded by remuneration packages which were…extremely generous even by international standards[143].

Simon Carswell corroborated this, explaining to Joe Higgins that:

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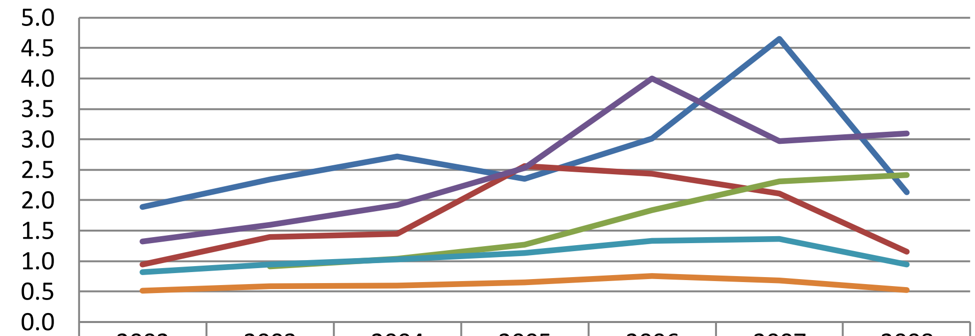
[140] AIB, "Why Has the Credit Crisis Hit AIB so Hard? - Board Seminar," April 29, 2009, 29.
[141] Ibid., 30.
[142] quoted in Larry Broderick, "Witness Statement of Larry Broderick to the Oireachtas Banking Inquiry," August 2015, 6.
[143] Ibid., 8.

> there was a switch in the 1980s to performance related pay and that that is really what drove this activity by the banks - the desire to maximise earnings. It was always about beating the previous year's profits and bankers being set higher targets to meet goals, not just by their own institutions but also by the market. They wanted to see the share price go in one particular way[144].

Between them, the six CEOs of the Irish banks netted approximately €71m from 2002-8 in pay alone and CEOs' annual pay more than doubled between 2002 and 2007 (Figure 2.10). The year before the crash, they went home with over €14m.

Figure 2.10 Bank CEO Pay 2002-2008 €m



	2002	2003	2004	2005	2006	2007	2008
Anglo	1.9	2.3	2.7	2.4	3.0	4.7	2.1
AIB	0.9	1.4	1.4	2.6	2.4	2.1	1.2
INBS		0.9	1.0	1.3	1.8	2.3	2.4
BOI	1.3	1.6	1.9	2.5	4.0	3.0	3.1
ILP	0.8	0.9	1.0	1.1	1.3	1.4	0.9
EBS	0.5	0.6	0.6	0.7	0.8	0.7	0.5

Former Anglo director, Gary McGann, who sat on the Remuneration Committee that approved David Drumm's pay, defended paying him €4.66m in 2007[145]. When asked why Drumm's pay package was the largest of all the bank CEOs, McGann said Anglo 'was the highest-performing bank for the last 25 or...25-odd years. That's well recognised' and claimed Drumm's 'short-term salary had been based on market competition' with 'bonuses based on targets to be achieved and long-term incentives based on sustainable profitability' (!)[146]. Joe Higgins then asked him if he thought ordinary workers, such as postmen and women who perform 'a very important social function...should...be entitled to a bonus of €2 million or €1 million?'. McGann responded:

> With the greatest of respect, Deputy Higgins, we're talking about apples and oranges here. The international banking world, the international plc world has norms and structures around how remuneration takes place...

Joe Higgins replied:

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[144] Simon Carswell, "Transcript of Simon Carswell Hearing," March 10, 2015, 649.
[145] Gary McGann, "Transcript of Gary McGann (Anglo) Hearing," September 3, 2015, 7, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/09/03092015_McGann_vol1.pdf.
[146] Ibid.

> Mr. McGann, if I could ask with the great respect to yourself as well, no postman and woman cost the taxpayers of this country €32 billion, which the management of Anglo Irish Bank did. How can you justify those levels of bonus for activities that led to, by any standards, a catastrophe for the taxpayer and the social situation of many people in this country?

McGann answered: ‘I think the correlation may be invidious’[147]. Given the context, he seems to have meant Joe’s comparison was in some way ‘unjust’ to himself or David Drumm, rather than the alternative, more appropriate meaning of ‘invidious’ as ‘likely to arouse or incur resentment or anger’.

Former AIB CEO Eugene Sheehy, who was paid €7.6 million from 2005-2009, felt that ‘At the time you could have made a case for it’, although at another point during his hearing he agreed that his pay levels ‘were not justifiable, period, okay, no matter what time you’re looking at it…there’s no way you could tell anybody in the street that these were acceptable levels of pay’[148]. Armed with the ‘benefit of hindsight’ he hasn’t been so quick to hand the money back; Sheehy confirmed to Joe Higgins that he has not made any contribution from the €7.6 million towards the €20bn cost of AIB’s bailout[149]. His predecessor, Michael Buckley, who also oversaw exponential lending growth while he was CEO refused to disclose his pension. ‘I honestly don’t feel any obligation to do so’[150], he said. The pension pot of former INBS CEO, Michael Fingleton, has been valued by the Central Bank at approximately €30m[151].

Bank CEOs and senior management also had large shareholdings in their own banks, netting handsome dividends and accumulating an ever-growing pile of wealth, until the whole house of cards collapsed. From 2000-2007, the market capitalisation of AIB, BOI and ILP more than doubled and Anglo’s increased ‘over 2,000% from €0.6bn in 2000 to a peak of €13.3bn’. The same would have gone for the bankers’ own shareholdings[152]. It was customary at Anglo for executives to invest in their own bank. Anglo’s 2007 *Risk Appetite Statement* portrayed this as a positive, stating that ‘the fact that almost 90% of employees own shares in the Group underlines the close alignment between their interests and those of the Group’. Likewise, AIB’s annual reports show that while Sheehy was CEO from 2005-7, the value of his shares increased by approximately €2.7m to over €4m and he would also have been getting regular dividends. Sheehy defended the board’s decision to pay themselves one last dividend in July 2008, which was paid out on September 26th, three days before the Guarantee[153]. On top of all this, directors had the economic benefit of large loans from their own bank. Directors’ loans from AIB increased from €2.6m to €14.4m from 2005-2007.

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147 Ibid.
148 Eugene Sheehy, “Transcript of Eugene Sheehy and Michael Buckley (AIB) Hearing,” April 29, 2015, 15–16, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/04/29042015_Sheehy_vol1.pdf.
149 Ibid., 37.
150 Ibid., 64.
151 Aodhan O’Faolain and Ray Managh, “Michael Fingleton Fails in Attempt to Stop Central Bank Inquiry,” *TheJournal.ie*, January 4, 2016, http://www.thejournal.ie/michael-fingleton-central-bank-inquiry-2530223-Jan2016/.
152 Nyberg, “Nyberg Report,” 14.
153 Sheehy, “Transcript of Eugene Sheehy and Michael Buckley (AIB) Hearing,” 22.

Whether derived from performance-related pay or shareholdings, the ultimate source of bankers' wealth was bank profits – and maximising those drove everything the banks did. Fundamentally, the main source of bank profits is the difference between the interest banks charge on loans and the interest they pay on deposits or wholesale funding. Bankers call this the 'Net Interest Margin'. It means there are three main ways a bank can increase profits: lend more; lend to riskier areas that attract a higher rate of interest; or cut costs. Or as Bill Black's recipe puts it: 'Grow like Crazy!', 'Make Terrible Quality Loans', and use 'pathetic underwriting'[154]. The Irish banks excelled at all three.

Grow like Crazy!

Black is certainly not the only regulator to recognise that fast growth is dangerous for banks. As the future Central Bank Governor, Patrick Honohan[155], wrote in 2009:

> A very simple warning sign used by most regulators to identify a bank exposed to increased risk is rapid balance sheet growth. An annual real growth rate of 20 per cent is often taken as the trigger.

Likewise, the Nyberg Report[156] highlights how Irish bank lending grew from '€120bn in 2000 to almost €400bn by 2007', with loans 'growing at a compound rate of almost 28% per annum from 2004-2006' and 'more than doubling overall' in just three years. In what must rank as an understatement of the century, Nyberg[157] comments: 'As all banks had effectively adopted high-growth strategies…the aggregate increase in credit available could not be fully absorbed by good quality loan demand'. As Honohan pointed out in an article he wrote in 2009,

> Each of the locally-controlled banks had at least one year in which this threshold was triggered. One of them, Anglo Irish Bank, crossed it in eight of nine years, and indeed its average annual rate of growth 1998-2007 was 36 per cent. Another, Irish Nationwide, crossed the line six out of the nine years, for an average rate of growth over the nine years of just above 20 per cent[158].

AIB was the next worst offender[159], growing by over 20% in 1999, 2004 and 2005 – which it saw as a 'strong competitive performance'. Internal documents from November 2006 show it projecting annual ROI lending growth of 32% and crowing: 'AIB on the offensive...Setting the agenda…High confidence across the network'[160]. The source of this self-satisfaction is evident in an internal presentation to the board after the crash. Under the heading 'The Good Times - AIB (1998-2007)', it reads:

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[154] Black, "Transcript of Bill Black Hearing," 261–262. Two other ingredients in Black's recipe are 'employing extreme leverage, which means a whole lot of debt compared to equity' and 'setting aside no meaningful loss reserves for the inevitable catastrophic losses which will follow'. The banks did these things too but for simplicity's sake the focus in this chapter is on the first two ingredients, which are sufficient in themselves to wreck a bank.

[155] Patrick Honohan, "Resolving Ireland's Banking Crisis," *The Economic and Social Review,* 40, no. 2 (Summer 2009): 217.

[156] Nyberg, "Nyberg Report," 12.

[157] Ibid., 34.

[158] Honohan, "Resolving Ireland?," 218.

[159] EBS also grew by more than 20% in 2002, 2004 and 2005 but was much smaller and cost ordinary people much less. Accordingly, this chapter will mainly deal with the other five banks.

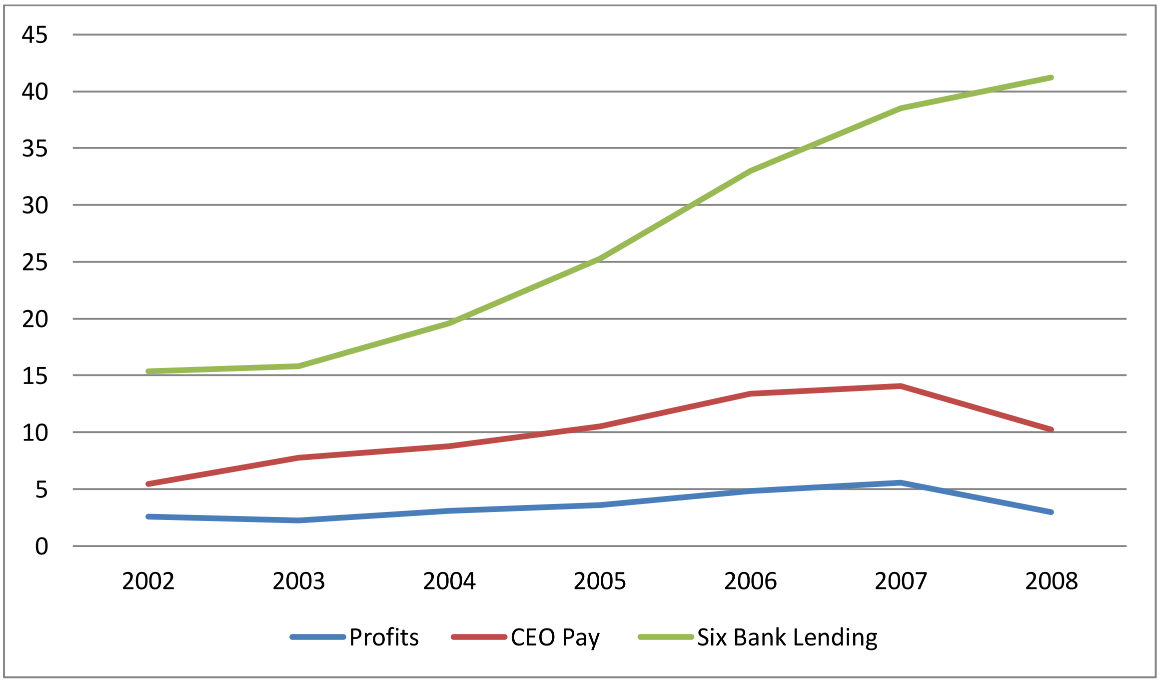
[160] AIB, "Review of Strategic and Competitive Issues - Board Meeting Agenda Item No. 5.1," November 9, 2006, 2.

330% (Increase in Loans and Advances)

191% (Increase in Earnings)[161]

Another internal post-mortem concluded that 'the main thrust of the Business in ROI was to focus on volume/market share-driven loan origination'. According to former Anglo executive, Matt Moran, 'the focus of all banks [was] on growth'[162]. The IMF agrees, reporting that across the banks, 'profitability was maintained through large lending volumes'[163]. Figure 2.11 shows the strong correlation of lending growth, profits and CEO pay for all the banks and belies bankers' attempts to imply that exorbitant pay and lending growth were not connected. Nyberg came to the same conclusion, finding that 'rapid loan asset growth was extensively and significantly rewarded at executive and other senior levels in most banks'[164].

Figure 2.11 Loan Books (€10bn) vs. Profits (€bn) vs. CEO Pay (€m)



All Anglo's former head of Irish lending, Tom Browne, said about pay in his opening statement was that 'There was no link between incentive and remuneration arrangements and loan growth for individual lenders as this for any bank would have been highly imprudent and dangerous'[165]. Eugene Sheehy similarly told the Inquiry that 'there was no relationship, none whatsoever, between my salary and the size of the bank's balance sheet. That's a fact.'[166] This is sophistry, especially as Sheehy himself had explained in his opening statement that 'Variable compensation was linked to achievement of planned profit objectives…Our preference was to grow income by margin management rather than volume growth. However, our growth came from increased volumes at

[161] AIB, "Why Has the Credit Crisis Hit AIB so Hard? - Board Seminar," 17.
[162] Matt Moran, "Opening Statement to the Inquiry," September 3, 2015, 11.
[163] quoted in Beaumont, "Written Statement of Craig Beaumont," 26.
[164] Nyberg, "Nyberg Report," 30.
[165] Tom Browne, "Opening Statement of Tom Browne (Anglo)," September 9, 2015, 5.
[166] Sheehy in Sheehy, "Transcript of Eugene Sheehy and Michael Buckley (AIB) Hearing," 37.

declining margins'[167]. Moreover, an internal AIB review released to the Inquiry states that 'Significant emphasis on lending growth as a means of achieving earnings growth… manifested itself into fairly blunt volume and earnings targets at business unit / branch level. This resulted in significant advances growth throughout RoI and NI.'[168]

Browne oversaw growth in Anglo's Irish loan book from €13bn to €38bn from 2005-7. During that time, he was awarded a salary of €4.483m and bonuses of €2.7m[169]. His shares were worth €11.5m when he left the bank and he also received a €3.75m golden handshake. Asked if he stood over that payment he replied:

> When I left the bank in 2007 I felt I'd done a good job and I felt I left behind a bank that there was no undue stress when I was walking out the door...I was leaving, my race was run. And, you know, the board decided that they were going to actually recognise my efforts over the previous 15 or 16 years[170].

While they feasted on its fruits, all the bank witnesses claimed not to have understood the risks of rapid growth. A memo from Matt Moran to the Anglo board in January 2007[171] suggests a somewhat different story, however. Under the heading 'Banks & High Growth - not always a happy marriage', it reads:

> "High growth banks seldom die of old age!" (Mohammad Rhostom, Portfolio Manager, Brown Brother Harriman, referring to our growth). Clearly growth implies risk for a bank- more so than for other sectors given the risk is maintained on your balance sheet for years following the inception of a loan. A key balancing act for us to impress upon the market is that Anglo's growth is delivered in a measured and conservative manner, without loosening our credit standards[172].

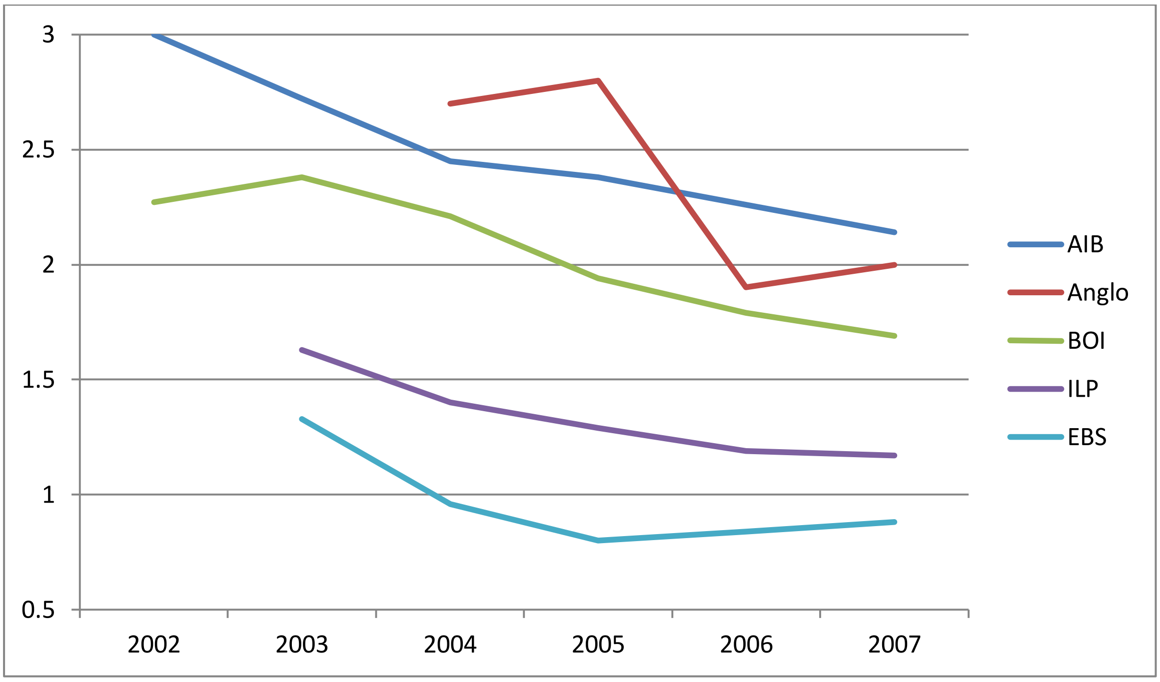
In reality, Anglo had been loosening its credit standards for years and had grown so recklessly that within two years it had racked up the worst losses of any bank in the world[173]. Asked if he felt he personally had done anything to contribute to the billions Anglo lost, Browne looked blank. 'I don't understand your question' [174], he said.

One plausible reason the banks gave for their insatiable pursuit of lending growth was that their Net Interest Margins – *rates* of profit – were falling (Figure 2.12) even as their *amount* of profit scaled new heights (Figure 2.13). This was partly due to financial globalisation and the single EU financial market, which encouraged foreign banks to enter the Irish market. The large overseas operations of banks like Ulster Bank/RBS and Bank of Scotland meant they could afford to temporarily make a loss

[167] Eugene Sheehy, "Opening Statement to the Banking Inquiry," April 29, 2015, 7.
[168] AIB, "Why Has the Credit Crisis Hit AIB so Hard? - Board Seminar," 53.
[169] Anglo Annual Reports
[170] Tom Browne, "Transcript of Tom Browne (Anglo) Hearing," September 9, 2015, 171–172.
[171] Matt Moran, "Transcript of Matt Moran (Anglo) Hearing," September 3, 2015, 82–83.
[172] Anglo Irish Bank, "Board Memo Re: Perception of Anglo Irish Bank in Equity Markets and Rating of Onr Stock," January 30, 2007, 3.
[173] Emmet Oliver, "Bailed-out Anglo Racks up Worst Losses in World," *Irish Independent*, July 1, 2010, http://www.independent.ie/business/irish/bailedout-anglo-racks-up-worst-losses-in-world-26663473.html.
[174] Browne, "Transcript of Tom Browne (Anglo) Hearing," 173.

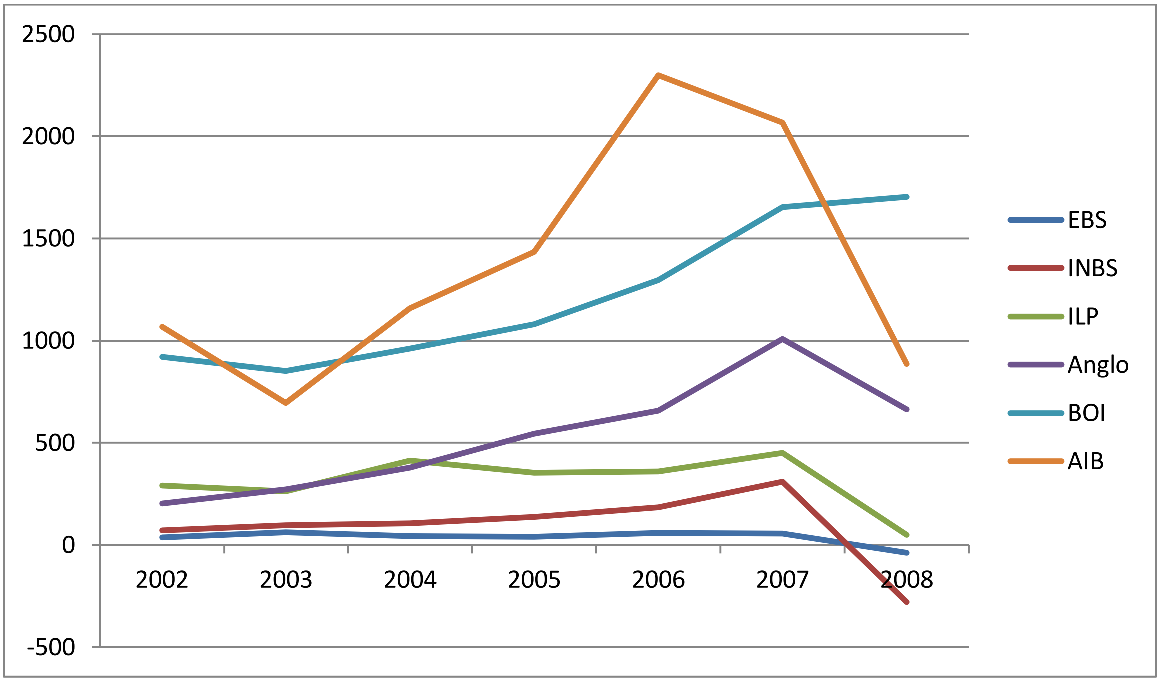
here by undercutting the Irish banks to win market share[175]. According to Carswell, 'In the period from 2004-07 in particular, there was a marked increase in competition between the banks and the foreign lenders were very actively becoming involved in the property development'[176]. The domestic banks compensated for lower profit margins per loan by lending more. BOI's 'Analysis of the Reasons Why the Institution Ran Into Difficulty' concluded that 'BOI's response to competition was overly dependant [sic] on volume to compensate for product margin erosion'[177] Eugene Sheehy also cited 'the long-term linear decline in net interest margin' and noted a particularly sharp decline from 2003 to 2007, which he said 'was driven by competition'[178] . He went on to explain that faced with this situation – and the banks' incessant pursuit of more profits – 'our growth came from increased volumes at declining margins'[179]. The outcome for the banking system as a whole was that because all the banks simultaneously lent more, lending and profits ballooned but the market shares of individual banks stayed much the same. Ulster Bank's CEO at the time, Cormac McCarthy, commented on this in his opening statement, noting that 'the Bank's competitive position at the end of this period was, in reality, no different to that which it found itself in at the start'[180].

Figure 2.12 Net Interest Margins 2002-2008[181]



[175] Broderick, "Witness Statement of Larry Broderick to the Oireachtas Banking Inquiry," 7.
[176] Carswell, "Transcript of Simon Carswell Hearing," 653.
[177] BOI, "Part 3: Analysis of the Reasons Why the Institution Ran Into Difficulty," in *EU Plan*, 2011.
[178] Sheehy, "Opening Statement to the Banking Inquiry," 2–3.
[179] Ibid., 7.
[180] Cormac McCarthy, "Opening Statement to the Banking Inquiry," May 6, 2015, 4.
[181] Taken from Banks' Annual Reports

Figure 2.13 After-Tax Bank Profits 2002-2007 €m



Central to this race to the bottom, as NAMA CEO, Brendan McDonagh, and Nyberg pointed out, was that 'institutions perceived lending as a sales activity'[182] and 'Lending was seen (and rewarded) as selling a loan or service rather than as acquiring a risky asset.' The result was that 'Banks' management and boards embraced a lending sales culture at the expense of prudence and risk management'[183]. This was also criticised by IBOA General Secretary, Larry Broderick, who told the Inquiry that 'The key objective in the financial services sector became the selling of "products"' so that 'From 2001 onwards…the pivotal measure used for the calculation of performance-related pay for individual employees was the achievement of sales-related targets'[184]. The IBOA had highlighted the stress this was causing ordinary bank workers to the Oireachtas Finance Committee in 2004:

> "The emphasis and obsession with selling more and more (financial) products to make even more profits, creates a very pressurised and stressful workplace. As a trade union, we have had to deal with a twenty-fold increase in stress-related problems in the last five years alone." [185]

At Anglo, this sales culture produced the type of 'credit approval process' described in the book *Anglo Republic* by Simon Carswell:

> "It was a bear pit," says a former senior lender at Anglo. "If you didn't get your loans approved over a few weeks in a row, they would move you off to another area such as treasury or wealth management if you couldn't hack it."

[182] Brendan McDonagh, "Opening Statement by Mr. Brendan McDonagh, Chief Executive of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," April 22, 2015, 12.
[183] Nyberg, "Nyberg Report," 95–96.
[184] Broderick, "Witness Statement of Larry Broderick to the Oireachtas Banking Inquiry," 6; 10.
[185] quoted in ibid., 13.

> …"It was a cross between a Nuremberg rally and the half-time talk to an American football team," says one ex-Anglo manager. "There were between fifty and sixty people in the room …No one was going to dissent in that atmosphere"[186].

This macho atmosphere was a direct result of the drive for lending and profit growth above all else. Anglo's Chairman and former CEO, Sean Fitzpatrick has described the bank's attitude to lending/sales as follows:

> The bank was about lending...The lending guys were all about Lionel Messi. They were all strikers. They were the pop stars. They were the guys who were making the f-ing money. They didn't worry about how the money was got to give to them. As far as they were concerned they were the guys lending money and that was where it all was. That was where the culture was as well.[187]

The CEO of EBS, Fergus Murphy alluded to how all this was fuelled by the never-ending supply of liquidity on the international wholesale markets:

> the focus was on profit before tax…And so that meant institutions were typically building the balance sheet… the organisation and the operating environment in the organisation, and the control environment in the organisation, and the banking operations, and the things that need to take place, like validating income or making a payment or ensuring affordability, were struggling, creaking at the edges to keep up with the origination machine that was being fuelled by the easy liquidity…[188]

Increasing lending also reinforced the *other* main reason banks' Net Interest Margins were falling. As the IMF pointed out in a report on Ireland in 2005, 'net interest margins have declined as reliance on more expensive wholesale funding has increased'[189]. And the reason wholesale funding increased was so banks could increase lending faster than their deposits. And the reason they couldn't get in more deposits was that businesses and the wealthy were borrowing more and saving less.

…through property lending

The vast majority of the banks' increased lending was for property rather than productive economic investments. This reflected the historic under-productiveness of the domestic Irish economy, the roots of which stretch all the way back to Ireland's economic peripherality as an agricultural colony of Britain. Nearly a century on from 1916, the domestic Irish economy largely consisted of services, much of it in unproductive areas like finance. The non-service parts were still dominated by agriculture and food[190] and by property and construction – all of which are relatively unproductive activities based on land ownership. As economist Michael Taft[191] puts it, Ireland has 'an under-performing indigenous sector, historically grounded in property-related activities'. By contrast,

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[186] Simon Carswell, *Anglo Republic*, 2011, 47–53.
[187] Tom Lyons and Brian Carey, *The FitzPatrick Tapes: The Rise and Fall of One Man, One Bank, and One Country* (Penguin UK, 2011).
[188] Fergus Murphy, "Transcript of Fergus Murphy (EBS) Hearing," July 22, 2015, 81.
[189] quoted in Beaumont, "Written Statement of Craig Beaumont," 21.
[190] The food and drink sector is Ireland's strongest native industry. Michael Taft, "Business in Ireland Is Too Important to Be Left to Irish Business," in *Ireland under Austerity: Neoliberal Crisis, Neoliberal Solutions*, ed. Colin Coulter (Manchester University Press, 2015), 274.
[191] Ibid.

manufacturing and IT remain dominated by FDI, attracted to the haven Ireland offers capital from tax and regulation.

In 2007, construction employment peaked at over 276,000, or 13% of total employment, with another 100,000, or 5%, employed in finance, insurance and real estate. Between them, these two bubble-related sectors accounted for more jobs than either industry or trade![192] Public and private investment in construction peaked at 20.6% of GDP in 2006, compared to 12% across the EU[193]. In GNP terms (which are more accurate given the level of FDI and tax haven activity), the numbers are even starker: construction activity grew from 16% of GNP in 2000 to 25.6% in 2006[194] and the total value of Irish construction activity from 2000-8 came to an incredible €254bn. This was bankrolled by a massive increase in property lending – by foreign as well as Irish banks. It grew 'from under 45% of total credit in December 2002 to over 60% in December 2008'[195] so that property lending represented '80% of all growth in credit' and increased by 'almost €200bn'[196] in just six years. Within this, the six Irish banks increased their domestic property lending by €122bn from 2002 to 2007, growing it from €46bn to €168bn[197]. To put that in perspective, if FG-Labour are re-elected they plan to invest €27bn over the next six years across *all* areas of the economy. Clearly, this vast misallocation of resources by the banks dwarfs any 'public sector waste'. AIB's Group Chief Credit Officer, Kieran Bennett outlined how this expansion of property lending was consciously planned by the AIB leadership but much the same could be said about all the banks:

> the prevailing strategy of AIB at that time…was centred on earnings growth…The vehicle for earnings growth was asset growth and mainly property asset growth. The AIB Group plan for 2007 approved by the Board in January 2007 was for profit growth of 12% and asset growth of 16%. Property growth was to an extent reverse engineered from the budgetary process[198].

'Make Terrible Quality Loans'

The Growth of Commercial Property Lending

As well as lending more, banks further boosted their Net Interest Margin by concentrating on riskier areas where they could charge more interest. Commercial property lending, and to a lesser extent buy-to-lets, fit the bill because they have significantly higher margins than owner-occupier mortgages, which are the lowest earning because they are the lowest risk. The most intense phase of commercial property lending growth was from 2003-2008, when it increased more than five-fold from €29bn to €156bn (Figure 2.3). According to the CEO of NAMA, Brendan McDonagh, lending to developers 'was seen as a profitable business due to larger lending margins and relatively low

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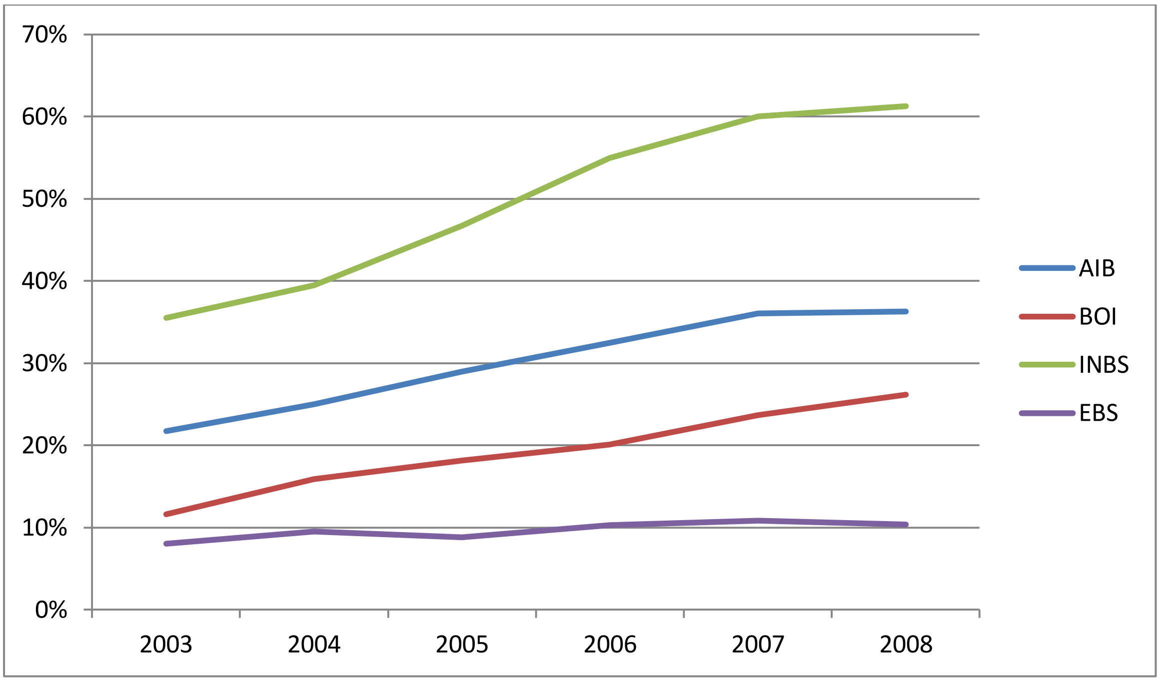
192 CSO, "Total Numbers in Employment by Quarter & Sector 1997-2014," 2015, http://www.cso.ie/px/pxeirestat/statire/SelectVarVal/saveselections.asp.
193 Eurostat figures on Gross fixed capital formation by AN_F6 asset type http://ec.europa.eu/eurostat/web/prohducts-datasets/-/nama_10_an6
194 Tom Parlon, "Opening Statement to the Banking Inquiry," April 22, 2015, 10.
195 Nyberg, "Nyberg Report," 14.
196 Ibid.
197 Ibid., 16.
198 Kieran Bennett, "Witness Statement of Kieran Bennett," 2015, 3, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/08/Kieran-Bennett-WSW.pdf. €76bn of this was for commercial property lending and the remaining €91bn for mortgages, of which about €21bn was buy-to-lets.

operating costs'[199]. This was confirmed by the former Chair of INBS, Michael Walsh, who told the Inquiry that whereas 'In 2000, there was an equal split between commercial and residential. We had taken very clear decisions in terms of not pursuing certain markets - i.e. a residential market that was overall competitive and with a very low margin'[200]. According to an internal AIB post-mortem, 'Short-Term' earnings targets necessitated rapid asset growth and [commercial] property was the fastest growing sector in Ireland. A growing concentration to [commercial] property was thus an inevitable consequence of the strategy being pursued'[201]. It goes on to explain: '[Commercial] Property had relatively high margins/fees which allied with significant market demand drove eps [earnings per share] growth faster than other segments'[202]. The outcome was a massive increase in the concentration (Figure 2.14) and quantity (Figure 2.3) of commercial property lending across all the banks apart from ILP, which specialised in mortgage lending and Anglo which consistently had a concentration of over 80%.

Figure 2.14 Commercial Property Concentration 2003-2008



According to AIB, 'Between 2004-2007, 46% of the increase in Group advances was [commercial] property-related' and in its main ROI division, '[commercial] property lending grew from €10.1 billion in 2004 to €33.3 billion (2008), a compound annual rate of growth of 35%.'[203] . The same happened at INBS. A 2007 KPMG due diligence report noted: 'The Society's loan book has trebled from FY01 (€3.4bn) and FY06 (€10.7bn), with the increase driven by commercial lending', which had 'increased €3.5 billion from €2.1 billion in December 2004 to €5.6 billion in December 2005'.

[199] McDonagh, "Opening Statement by Mr. Brendan McDonagh, Chief Executive of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," 12.
[200] Michael Walsh, "Transcript of Michael Walsh (INBS) Hearing," September 2, 2015, 81.
[201] AIB, "Why Has the Credit Crisis Hit AIB so Hard? - Board Seminar," 2.
[202] Ibid., 33.
[203] Ibid., 36.

Nyberg concluded that ‘The willingness of banks to accept higher risks by providing more and shockingly larger loans primarily for commercial property deals was an important reason for the gradual increase in financial fragility in Ireland’[204]. He also emphasised that ‘Anglo was essentially a monoline bank focused almost exclusively on commercial property lending’[205] and said that ‘strategies in both bigger banks [AIB and BOI] evolved to allow increased exposure to the commercial property market as this was a sector that could provide for the significant loan growth required to meet earnings targets’[206]. Simon Carswell’s less tactful description was that ‘Anglo Irish Bank was the one-trick pony in a frenetic land grab, leading a poorly regulated and highly competitive race for market share and profit’[207]. He said this involved ‘a marked shift by the other banks, once they saw how much money Anglo was making… The sheer scale of the profits made at Anglo was too tempting for the other banks – they really had to try and get a slice of the action’[208]

The boards and management of all the banks obviously knew how concentrated their banks were on commercial property, and so did the Financial Regulator. INBS Chair, Michael Walsh confirmed to Joe Higgins that ‘By definition, the board was fully aware of these’[209]. Likewise, when asked what percentage of Anglo’s loan book was property-related, former director, Fintan Drury, replied: ‘clearly it was a monoline bank, that’s what it did…I would’ve said somewhere between 80% and 90%’[210]. The riskiness of this was also well known. A January 2007 memo to Anglo’s Board by Matt Moran states ‘Our less diversified business adds additional inherent risk versus a universal player ’[211]. Similarly, in a ‘Review of Strategic and Competitive Issues’ presented to AIB’s board in November 2006 it says:

> We are at a point when we need to manage our loan book tightly and we are rightly concerned about the concentration of exposure to Property and Construction. However this needs to be balanced with…the appetite of Bank of Ireland and Ulster Bank in particular to exploit any more restrictive approach by AIB to the big players in Property and Construction.

A handwritten note beside it says: ‘P & C [Property & Construction] that's where the bus. is. If step back, difficult to recover’[212]. According to AIB’s Group Chief Credit Officer, Kieran Bennett, he warned the Board in April 2007 that ‘Concern was beginning to be expressed by the Rating Agencies in relation to AIBs property concentration’ but there was still no move by the board to limit, or even define, the bank’s ‘risk appetite’ even though the ‘Lack of Group-wide credit risk strategy and risk appetite’ had been raised as a problem by Group Internal Audit in early 2005[213].

…especially development lending

Within commercial property lending, there was an increasing concentration on development lending, which is higher risk because it is mainly based on capital gains. The attraction, according to

[204] Nyberg, “Nyberg Report,” ii.
[205] Ibid., 32.
[206] Ibid., 25.
[207] Simon Carswell, “Opening Statement to the Banking Inquiry,” March 9, 2015, 2.
[208] Carswell, “Transcript of Simon Carswell Hearing,” 638.
[209] Walsh, “Transcript of Michael Walsh (INBS) Hearing,” 84.
[210] Fintan Drury, “Transcript of Fintan Drury Hearing,” July 30, 2015, 94.
[211] Anglo Irish Bank, “Board Memo Re: Perception of Anglo Irish Bank in Equity Markets and Rating of Onr Stock,” 1.
[212] AIB, “Review of Strategic and Competitive Issues - Board Meeting Agenda Item No. 5.1,” 3.
[213] Bennett, “Witness Statement of Kieran Bennett,” 4; 6; 13.

Anglo executive, Matt Moran, was that ‘Development related lending assumes greater risk and hence attracted higher returns’[214]. Likewise, Michael Walsh, wrote in a letter to the Financial Regulator in February 2005 that ‘We decided to diversify into non-home lending particularly in the housing development market where we would obtain better margins’. Nyberg summarises that ‘banks accumulated large portfolios of increasingly risky loan assets in the property development sector. This was the riskiest but also (temporarily) the easiest and quickest route to achieve profit growth.’ [215]

Development loans typically involved ‘interest roll-up’ whereby all the interest accrued over the course of the loan would be paid in one go at the end, for instance when a piece of land was flipped to a new buyer after getting planning permission; the original loan was re-financed by someone else; or a commercial or housing development was completed and sold on. Investment property lending is seen as lower risk by comparison because it is more based on rental yields. An example would be an investor borrowing to buy an office block to rent to corporate tenants.

A March 2007 inspection of Anglo’s commercial property lending by the Financial Regulator found development lending accounted for a quarter of its loan book[216]. AIB by 2008 wasn’t far off, at 18%. A whopping 9% of this, or €12bn, was loans to buy land – the riskiest of all forms of property lending[217]. Overall, by September 2008, the Irish banks had run up €63bn in land and development loans. AIB had the most at €23.7bn, followed by Anglo with €19.7bn, BOI with €13.6bn and INBS with €5.6bn[218]. However, INBS had the highest land and development concentration of them all. KPMG found that in 2006 ‘Development finance issued on speculative property investments is the main form of lending issued to commercial customers in Ireland. Within Ireland this sector has grown at a CAGR [Compound Annual Growth Rate] of 53% from €0.7 billion in FY04 to €1.7 billion in FY06…’[219]. By the time of the Guarantee, development loans accounted for €8.5bn of INBS’ €12bn loan book – more than 70%[220].

An added attraction of development lending was profit-share agreements with developers involving ‘supplemental arrangement fees’. These were a particular specialty of INBS, whose business model was described by Nyberg as ‘in some ways closer to that of a venture-capital financier than that of typical banks’[221]. Michael Walsh outlined this model in his opening statement:

> The loans would typically be provided on a short term basis, with many of them being repayable often within as little as eighteen months. The borrower was expected to enhance the project and then refinance the loans elsewhere with larger institutions. To optimise the return on capital the Society structured many of its loans with normal market interest

214 Moran, “Opening Statement to the Inquiry,” 11.
215 Nyberg, “Nyberg Report,” 50.
216 cited by Deputy Eoghan Murphy in Moran, “Transcript of Matt Moran (Anglo) Hearing,” 81.
217 AIB, “Why Has the Credit Crisis Hit AIB so Hard? - Board Seminar,” 38.
218 PWC, “Project Atlas II Volume 1 Overview Working Draft,” November 17, 2008.
219 KPMG, “Project Harmony Due Diligence Report 20 June 2007,” June 2007.
220 Michael Fingleton, “Transcript of Michael Fingleton Hearing,” September 2, 2015, 14, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/09/02092015_Fingleton_vol1.pdf.
221 Nyberg, “Nyberg Report,” 23–24.

> charges but with a right to participate in any profits on the subsequent development which would be funded elsewhere[222].

Nyberg explained in his report how risky this was:

> Security generally comprised the property asset only (i.e. without recourse to guarantees or cross security), while interest, fees and associated costs were frequently added to the loan (i.e. interest and/or fees roll-up). When planning permission, which generally increased the value of the site, was attained it was intended that another bank would refinance the loan and INBS would be repaid. Loan contracts tended to include profit share agreements, with INBS receiving typically between 25% and 50% of the profit if and when a project was concluded successfully…. This business model was in principle and in practice risky because of the planning permission risks involved and because of the reliance on the refinancing of borrowers by other banks[223]

By 2006, according to KMPG's vendor due diligence report for INBS, profit share arrangements were providing almost half its profits. INBS also entered into joint ventures with developers, beginning in 1992 with Gerry Gannon and Sean Mulryan[224]. As we shall see, this led to very close relationships – and enormous debts – between INBS and its biggest borrowers.

A final point to make about how risky all this development lending relates to the relatively low rates of interest banks were charging on these high risk loans. Developers are currently charged interest rates of 10-15% on development loans[225] but during the bubble they were getting them for far less than that as developers played the banks off against each other to get a lower price. Developer, Gerry Gannon, told the Inquiry: 'I expanded my banking relationships beyond Anglo with a view to introducing an element of competition and reducing the cost of finance'[226]. Likewise, Sean Mulryan wrote of 'Presenting opportunities to several providers seeking the most competitive commercial terms'[227]. This competitive race to the bottom spurred the banks to slash interest rates even on high risk development loans, driving down Net Interest Margins – and rates of profit – and further reinforcing the urge to 'Grow Like Crazy!' to compensate. On top of this, development loans generally deferred even the interest payments until the end of the loan term, when the project would supposedly be finished and the developer would supposedly sell it off. According to the Chair of NAMA, Frank Daly, this meant 'banks were taking high equity-grade risk for low debt-grade returns – and, in fact, even those low debt returns were often not realised but rather accrued as rolled-up interest booked as income in bank financial statements.'[228] This all worked fine until the

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222 Michael Walsh, "Opening Statement to the Inquiry of Michael Walsh (INBS)," September 2, 2015, 20.
223 Nyberg, "Nyberg Report," 23–24.
224 Michael Fingleton, "Opening Statement of Michael Fingleton the Banking Inquiry," September 2, 2015, 2; Sean Mulryan, "Transcript of Sean Mulryan Hearing," July 22, 2015, 9.
225 Peter Stafford, "Introduction - the Developer Perspective" (Financing for Property Development Conference, The Marker Hotel, Grand Canal Square, Dublin 2, 2015), 8.
226 Gerard Gannon, "Gerard Gannon Statement," June 10, 2015, 2, https://inquiries.oireachtas.local/banking/participant/GGA/EvidenceDocuments/GGA01B01/Gerard%20Gannon%20Statement%20to%20the%20Joint%20Committee%20of%20Inquir%20(renamed).pdf.
227 Sean Mulryan, "Opening Statement to the Inquiry," July 22, 2015, 9.
228 Frank Daly, "Opening Statement by Mr. Frank Daly, Chairman of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," April 22, 2015, 2–3.

bubble burst, stranding developers with their pants down in empty fields, vacant shopping centres or ghost estates and the banks with €9bn just in 'interest roll up'[229].

In light of all this, it's no wonder that when the crash hit, it was the banks with the most commercial property lending that booked the biggest losses and got the biggest bailouts (Figure 2.7). Little INBS is particularly spectacular in this respect: its super-concentration in commercial property lending meant it leapfrogged the losses of three much bigger banks, including BOI whose loan book was 13 times larger (Figure 2.9). By 2008, 86% of Anglo's total loan book was commercial property lending. A mere 3% of that was for industrial property and only another 12% was for non-property-related business lending[230]. In a way, Anglo was a grotesque but not inaccurate caricature of the unproductive nature of the Irish economy as whole.

Use Pathetic Underwriting! Cut costs & credit standards

The third ingredient in Bill Black's recipe for mega profits, mega-rich bankers and catastrophic losses is 'pathetic underwriting'. According to the CEO of NAMA, Brendan McDonagh, 'The impact of greater competition amongst lenders was to increase risky and imprudent lending', while Nyberg concluded that 'Because lending growth, in practice, became prioritised over credit and risk management, checks and balances in the banks were weakened even though the formal structures remained.'[231] In other words, the insatiable greed for more profits led to credit controls being cut.

Simon Carswell linked this not only to competition and greed for profit among banks but also to competition among developers. Asked 'why the banks became so careless in the way they allowed loans to be made?' he replied:

> It was so profitable because the property market was rising and they wanted to get the money out as quickly as possible…The key was getting the money out as quickly as possible. Many rival developers were bidding for the same land and each developer may have been backed by a different bank. It was the competitive race to buy the land which drove this process[232].

This slashing of credit standards is euphemistically referred to by bankers as 'relaxation of credit policy' and 'exceptions'. The Public Accounts Committee found 'Anglo relaxed its credit policy three times between 2005 and 2007'[233] and whereas credit policies are supposed to generally be followed, and exceptions are meant to actually be exceptional, NAMA told the Inquiry that 92% by value of the Anglo loans transferred to it represented 'exceptions' to credit policy. In cash terms, this amounted to €32bn[234]. Similarly at AIB, according to its Group Chief Credit Officer, Kieran Bennett, 'Limits set in the GLEP [Group Large Exposures Policy] were essentially soft rather than hard in that breaches were almost always sanctioned. As a result, this allowed for almost unfettered growth in property'[235]. This is confirmed by an April 2009 internal AIB review released to the Inquiry. It states that previously any

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229 NAMA, "Supplementary Documentation," 3.
230 AIB, "Board Meeting Minute Item 2- Project Omega," November 28, 2008, 19.
231 Nyberg, "Nyberg Report," 28.
232 Carswell, "Transcript of Simon Carswell Hearing," 651.
233 Public Accounts Committee, "Report on the Crisis in the Domestic Banking Sector: A Preliminary Analysis and a Framework for a Banking Inquiry," July 2012, http://www.oireachtas.ie/parliament/media/committees/pac/PAC-Report---FINAL.pdf.
234 NAMA, "Exceptions to Credit Policy for Anglo Loans Transferred to NAMA," 2015.
235 Bennett, "Witness Statement of Kieran Bennett," 6.

individual exposures over €250m had to be referred to the Board under the Group Large Exposure Policy (GLEP), but those limits were increased in October 2006. It comments: 'In practice, the GLEP was more an escalation mechanism for approval of exposures beyond this amount'. The result was that by 2008, 49 of the top 50 exposures, amounting to €18.8bn, were 'in excess of the GLEP.' [236] A similar dynamic developed to a lesser extent at BOI. For example, after introducing land bank loans limits in 2006[237], documents released to the Inquiry show that the board increased them in August 2007 and again in August 2008.

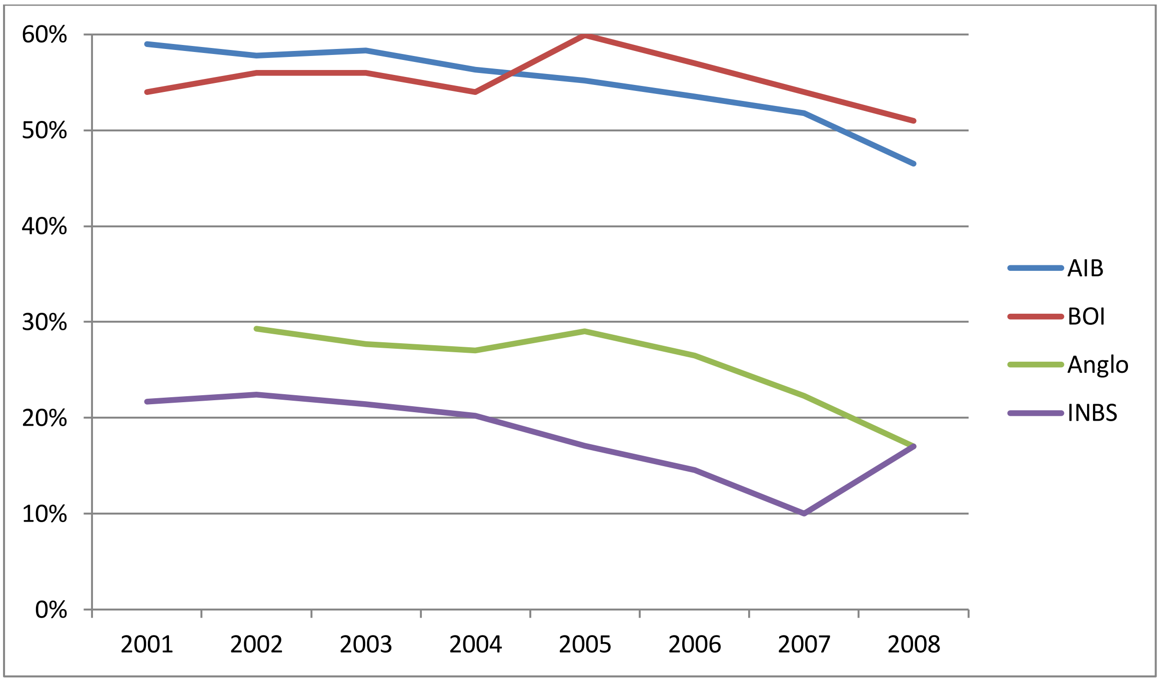
In a 'sales' culture like Anglo's, credit control and risk management were always going to be regarded as an irritant but when growing at 36% they became impossible. In *Anglo Republic,* a senior executive is quoted as saying*:* "It became too busy and loans did not get the same level of discussion when the loan growth really started taking off…We kidded ourselves that this system really worked – we just didn't have the time" [238]. This certainly seems like a more plausible account of what was going on than Tom Browne's assertion that 'the system allowed for early identification of problems in the loan book'[239]. Kieran Bennett identified the same problems in AIB:

> when the main driver was growth, the fundamentals of credit oversight and control were much weakened….It was ironic that it was almost impossible to get skilled internal resources released from the business due to growth demands…the organisational response was to suck it up and get on with it.[240]

This highlights how loosening credit policy was reinforced by the banks' incessant cost-cutting (Figure 2.15) – which is also the third and final way banks can increase their profits. From their profit-obsessed neoliberal perspective, this must have seemed like a virtuous rather than a vicious circle as it doubly boosted profits by simultaneously cutting costs and facilitating greater lending. For neoliberals, fewer staff and lower costs always equals greater 'efficiency', 'competitiveness' and profits, rather than the actual outcome of catastrophic incompetence and devastating losses. As Figure 2.15 shows, the scale of cost-cutting by AIB, Anglo and INBS in the run-up to the crash was so severe it could be compared to asset-stripping, especially as senior management were simultaneously paying themselves huge salaries, bonuses and dividend payments.

[236] AIB, "Why Has the Credit Crisis Hit AIB so Hard? - Board Seminar," 47–48.
[237] Ronan Murphy, "Written Statement of Ronan Murphy (BOI)," October 2015, 3.
[238] Carswell, *Anglo Republic*, 47–53.
[239] Browne, "Opening Statement of Tom Browne (Anglo)," 4.
[240] Bennett, "Witness Statement of Kieran Bennett," 4.

Figure 2.15 Cost/Income Ratios 2001-2008



The main metric banks use to measure their costs is the 'cost-income ratio' and pushing this down as far as possible was their constant goal. IBOA General Secretary, Broderick explained how:

> Even before the crash in 2008, banking employees had faced demands for major restructuring – involving significant levels of redundancies as well as some outsourcing – on the grounds that this would secure the viability of the institution by improving competitiveness – when, of course, it is clear that the real purpose of these measures was to maximise profits in already highly profitable entities in order to enhance shareholder value…For example, in 2005, Bank of Ireland Group launched its Cost and Capability programme to reduce its staff complement by 2,100 through a combination of voluntary redundancy and early retirement over a four-year period…While AIB did not engage in a major programme of job losses during the 2000s, it had already undergone a substantial restructuring involving 1,100 voluntary redundancies in the late 1990s[241].

Notwithstanding this, AIB board minutes from July 2006 list 'Cost/income ratio down by 2.7% to 52.4%' as one of the 'key highlights' of the previous six months[242] A 'Review of Strategic and Competitive Issues' four months later notes, 'Branch resources are stretched, reflecting continuous growth in business volumes'. However, it concludes that this points 'to the need for a changed operating model which centralizes all activities other than customer sales and service'[243] rather than more staff. By 2008, the cost-income ratio had been driven down even further, to 46.5%. AIB's 2008 Annual Report described this cannibalisation of the bank in glowing terms:

> In this climate of slower revenue growth, swift action and aggressive management of our cost base yielded a 6% reduction in costs in 2008 generating a reduction in the cost income

[241] Broderick, "Witness Statement of Larry Broderick to the Oireachtas Banking Inquiry," 10.
[242] AIB, "Board Minutes - AIB July 27th 2006," July 27, 2006, 3.
[243] AIB, "Review of Strategic and Competitive Issues - Board Meeting Agenda Item No. 5.1," 3.

> ratio from 51.8% to a historic low of 46.5%.This positive income/cost growth position drove an 18% increase in operating profit before provisions to € 2.7 billion demonstrating AIB's efficiency, operating flexibility and recurring customer revenues[244].

AIB was still miles behind Anglo, which slashed its cost-income ratio from 29% to 17% from 2005-2008. This undoubtedly contributed to its huge losses as it meant fewer staff and resources for credit control, risk management and internal audit. The neoliberal mindset that lower costs equals bigger profits was evident in how former director, Matt Moran, cited Anglo's low cost-income ratio as one of the reasons management forecasted in November 2008 that it "will be the most profitable and capital generative of all publicly quoted financial institutions in Ireland" from 2009-2013. Moran explained that Anglo 'had a cost-to-income ratio that was very low, so it meant that for revenue generated in a period, a significant element of that would convert to profit'[245]. However, once the crisis hit, the realisation seems to have dawned on at least some of Anglo's *'Top Gun'* executives that proper underwriting might have been an idea after all. As one of them said to Simon Carswell, "If your army gets big enough, you need more cargo guys around to do the heavy lifting, not just the jet fighter pilots"[246].

INBS had the lowest cost-income ratio of them all – a ludicrous 10%, compared to an industry norm for UK building societies of 70%[247]. The Nyberg report commented that:

> As INBS neglected to build up robust organisational structures and risk management frameworks, it is not surprising that there was no evidence of even basic analysis or reporting of, for example, internal sector limits, concentration risk and the adequacy of security. The absence of such structures resulted in low overheads leading to a remarkably low cost-income ratio…[248]

Other implications were that INBS' overseas commercial loan book of €5.5bn was overseen by only two managers[249] while Internal Audit was described by INBS Internal Auditor, Eamonn Daly, as 'very under-resourced', especially as INBS had no Risk Unit or even a Risk Officer[250]. Daly added:

> if we compare the situation of INBS to EBS, while the latter building society had a less favourable cost income ratio and a lower profitability ratio, it also had significantly higher staff numbers – and ultimately, as is well-known, although EBS also required government assistance during the banking crisis it comprised a much lower % of its loan assets than INBS[251].

Daly went on to explain:

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244 AIB, "Annual Report 2008," 2009, 24, http://online.hemscottir.com/ir/aib/ar_2008/download/pdf/ar_2008.pdf.
245 Moran, "Transcript of Matt Moran (Anglo) Hearing," 95.
246 quoted in Carswell, *Anglo Republic*.
247 Nyberg, "Nyberg Report," 28.
248 Ibid.
249 Ibid., 33.
250 Eamonn Daly, "Section 25 Statement of Eamon-Daly (INBS)," October 2015, 6; 9.
251 Ibid., 17.

> there was an inappropriate strategic emphasis on the part of senior executive management of INBS on keeping the cost income ratio of INBS at a very competitive level compared to its peer group. In my view, this inappropriate focus fed directly into inappropriate under-resourcing in some key areas, and to many of the weaknesses in INBS identified by CBFR [Central Bank/Financial Regulator], EA [External Audit], and indeed IAD [Internal Audit Department] itself, in their respective reviews and reports. [252]

An exhaustive Central Bank investigation into INBS finally concluded shortly before Fingleton and Walsh were due to appear at the Inquiry. The Central Bank stated on its website that 'INBS's admitted failings amount to a consistent and, at times, wholesale disregard for its own policies and procedures'. Specifically, it said:

> INBS has admitted to breaching seven different aspects of its commercial lending and credit risk management processes, namely: 1. the initial loan application stage; 2. the loan approval process; 3.the taking of security, obtaining valuations and adherence to maximum Loan to Value ratios ("LTVs"); 4.the monitoring of commercial lending; 5. the role of INBS's Credit Committee; 6.reporting obligations to the Board of INBS relating to commercial lending; and 7.the requirement for a formal credit risk policy relating to the establishment of profit share agreements.

Despite all this, INBS' Chair, Michael Walsh, claimed INBS had 'a more prudent model than that adopted by many of its competitors'[253]. While this appears an outlandish claim at first glance, given there has been no comparable Central Bank investigation into any of the other banks we have no way of knowing for certain how much better or worse INBS was in any of the above areas. But on the basis of all the evidence presented to the Inquiry and the scale of the losses at the other banks, much of what the Central Bank found in relation to INBS could probably be said about the other banks.

The intense competition in Irish banking in the 2000s exacerbated all three ingredients of Bill Black's recipe for bank failure – Grow like Crazy! Make Terrible Quality Loans and Use Pathetic Underwriting. The outcome was a destructive race to the bottom. All the banks joined in, including BOI, which in its own words, 'explicitly and implicitly looked to relative profit performance targets vis-a-vis its peer group'[254]. Consequently, even the most 'conservative' of the major banks racked up €38bn in commercial property loans and €4.4bn in losses from 2009-2013 (Figure 2.7). As was outlined in Chapter 1, far from restraining this process, the dominant neoliberal philosophy meant the EU, Irish government and the Financial Regulator did all they could to encourage even *more* competition, in the mistaken belief markets could do no wrong and were inherently efficient and self-regulating.

An additional important ingredient of the toxic swill cooked up by the banks was extreme concentration to a small number of well-connected commercial property speculators. In his testimony to the Inquiry, Bill Black identified a high level of debtor concentration as a particularly efficient way to 'grow like crazy!' and make terrible quality loans:

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[252] Ibid.
[253] Walsh, "Opening Statement to the Inquiry of Michael Walsh (INBS)," 4.
[254] BOI, "Part 3: Analysis of the Reasons Why the Institution Ran Into Difficulty."

> Even if you were going to concentrate on commercial lending, you would never prudently concentrate in a small number of borrowers. The old joke they tell about banking is absolutely true. If you borrow $10,000 from a bank, the bank owns you but if you borrow $100 million from the bank, you own the bank. The banks will extend even bigger loans to you and, as long as new money is coming in, you can keep the thing alive a bit. That is always a bubble disaster. We have known this for many past crises. This was something that was easy for the bankers and for the regulators to figure out. [255]

This points to the relationships between the banks, the property sector and politics and is dealt with in the next chapter.

[255] Black, "Transcript of Bill Black Hearing," 273.

Chapter 3: The Relationships beneath the Bubble

During the Inquiry, Anglo's former head of Irish lending, Tom Browne was asked if the €25bn growth in Anglo's Irish loan book from 2004-7[256] was sustainable. He replied:

> It wasn't sustainable, it just happened, you know, in terms of, you know, you'd a very active client base in a very active market with a landscape that actually created those type of opportunities, and we had a client base that we continued to support and, as I said earlier on, we supported too strongly. [257]

Pressed on how Anglo's loan book got so out of control, he repeated the same line about a 'very active' 'client base' no fewer than eight times. Like a horror version of *Field of Dreams,* it seems if developers wanted to build it, Anglo would come. INBS's Finance Director, John Stanley Purcell, displayed a similar approach, explaining that the Society's loan book trebled from €3.4bn to €10.7bn in three years because 'Well, what we were doing was, we were doing loans, repeat business with people we knew'[258].

The former *Irish Times* environment correspondent, Frank McDonald, explained that this relationship worked both ways: 'Bankers also played a role of touts for developers. Frequently, it was the banks who spotted the potential of a well-located site and will then line up one of their client developers to run with it'[259]; 'banks and developers were working hand in glove in seeking out sites for development…'[260]. *Irish Times* journalist and author of *Anglo Republic*, Simon Carswell, similarly told the Inquiry that:

> There was a frenzy to lend to the developers…In some instances the banks would approach the borrower asking if he was interested in the land and, if so, the bank would help the borrower to buy it. The developer might be on the radar but may not have been interested until the bank raised the issue.[261]

These dynamics led to the banks' extremely high exposure to a small but powerful elite of property and construction tycoons who accumulated vast wealth during the bubble to become the largest cohort on Ireland's Rich List[262]. Sean Mulryan, Liam Carroll, Michael O'Flynn, Bernard McNamara, Derek Quinlan and Treasury Holdings' Ronan and Barrett became household names as they were fêted in the media as geniuses with the 'Midas Touch'[263]. As the banks' biggest customers, they seldom heard the word 'No'. Regulators displayed the same deference towards bankers, and politicians deferred to both bankers and developers, and all within a web of tight-knit elite relationships that Simon Carswell described as 'extremely cosy'[264]. The closeness of these

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[256] Browne was head of Irish lending from2005-2007.
[257] "Transcript of Tom Browne (Anglo) Hearing," September 9, 2015, 172.
[258] "Transcript of John Stanley Purcell (INBS) Hearing," September 2, 2015, 138.
[259] Frank McDonald, "Opening Statement to the Banking Inquiry," March 12, 2015, 3.
[260] Ibid., 775.
[261] "Transcript of Simon Carswell Hearing," March 10, 2015, 652–3.
[262] Brian Carey, "Ireland's Well-Heeled Enter Inner Sanctum of Global Rich; Today's Rich Supplement Shows the Combined Wealth of the Top 100 Has Risen to €25bn," *Sunday Tribune*, April 11, 2004. The percentages in 2007 were much the same Sunday Independent, "TheTop 100," *Sunday Independent*, March 18, 2007, 2007..
[263] Derek Quinlan, "High Rollers Back Quinlan Private's Midas Touch for Daring €1bn Property Deals," April 8, 2004; Martin Fitzpatrick, "Newcomers to the Financial Bigwig List," *Sunday Independent*, November 6, 2005.
[264] Simon Carswell, "Opening Statement to the Banking Inquiry," March 9, 2015, 2.

relationships and the pecking orders within them reflected the power structure in this country and the dominance within the Irish capitalist class of developers and financiers.

After the bubble burst, it emerged that the top 29 Irish bank borrowers accounted for €34bn of the €74bn in commercial property debt transferred to NAMA – an incredible 44%. The top 63 made up 61% and the top 145 made up 78%. The banks lost €42bn on the loans transferred to NAMA and were recapitalised for that through the bank bailout. So fewer than 150 property speculators cost us €33bn. To add insult to injury, many of those loans were for property speculation *overseas* and so contributed nothing whatsoever to the Irish economy. By September 2008, the Irish banks had lent €170bn outside of Ireland – 40% of their entire balance sheet[265]. NAMA initially estimated a third of its loans were for commercial property[266] outside Ireland; the final figure by value was 46%[267]. Yet the government put us on the hook for the lot.

Irish confidentiality laws prohibit disclosure of relationships between banks and their customers, even when the bank is NAMA and the customers in question have cost the population billions of euro. The Inquiry was fortunate some of these details had already been exposed in the media as it would otherwise have been unable to question the big borrowers about their business dealings at all – and in fact would have had no basis for even knowing who they were.

However, the legal advice which the majority on the Committee accepted frustrated any serious questioning of developers which was attempting to throw light on their dealing with public representatives. For example, the record shows that when Joe Higgins was attempting to question major developer Sean Mulryan on whether he had political assistance in assembling a very major land bank in Wicklow, the Chairman citing legal advice adamantly refused to allow the line of questioning. This was despite the Inquiry's Terms of Reference 3(b)(ii) stating that the Inquiry may inquire into "relationships between State authorities, political parties, elected representatives, supervisory authorities, banking institutions and the property sector.' Central to the property bubble and crash was the relationship between developers, bankers and establishment politicians and it is a measure of the chilling effect of the 2013 Act that members were not allowed to explore this in case of legal action being taken against the Committee.

Unsurprisingly, lending concentration was highest at the worst banks. Anglo's top 20 borrowers made up half of its €41.7bn Irish loan book[268], while 'The top fifty customers at AIB owed €19 billion, about 15 per cent of all its global lending'[269]. Asked about the level of debtor concentration at Anglo, Black said:

> I have never seen a concentration that high at any financial institution of any size anywhere in the world at any time in history. It is absolutely – no questions and no ifs, ands or buts –

[265] PWC, "Project Atlas II Volume 1 Overview Working Draft," November 17, 2008.
[266] NAMA, "Supplementary Documentation," September 19, 2009, 4, https://www.nama.ie/fileadmin/user_upload/Supplementary_Documentation.pdf.
[267] Comptroller and Auditor General, "National Asset Management Agency Progress Report 2010 - 2012," Comptroller and Auditor General Special Report, (April 2014), 53.
[268] Peter Nyberg, "Misjuding Risk - Causes of the Systemic Banking Crisis in Ireland: Report of the Commission of Investigation into the Banking Sector In Ireland," March 2011, 33.
[269] Matt Cooper, *Who Really Runs Ireland?* (Dublin: Penguin Ireland, 2009).

> utterly unsafe and unsound and I would have begun efforts to stop it immediately. At those levels we would have been gearing up for receivership[270].

The situation was similar at INBS where the top 30 commercial borrowers accounted for 41% of its total loan book in 2006[271] and the top six made up 15% in 2008[272]. According to Fingleton, 'The Society, at the end of 2007, had approximately 300 exposures, with the top 100 representing 80% of the commercial loan book.'[273]. In other words, 300 people racked up the debts that led to INBS' €5.4bn bailout – and 100 accounted for €4.3bn of it. The Financial Regulator was fully aware of these dangerous levels of debtor concentration; it got quarterly reports from each bank on their largest borrowers[274].

As well as dangerously concentrating risk, this meant the banks depended on a small 'golden circle' of property developers for a substantial portion of their profits and were very wary of losing their business to competitors. Nyberg concluded that 'Being a relationship lender, Anglo found it quite difficult to decline a loan to any of its traditional top customers' and that 'The lending culture was such that when applications were problematic, the mindset was "there is a 'yes' in there somewhere"'[275]. This was confirmed by Simon Carswell, who said:

> The Anglo credit and risk infrastructure or committees were set up to find a "Yes" in loans that came in from customers and loan proposals. It was almost regarded as a lender's failure to get a borrower's loan deal over the line. That was seen as a problem for the lender and not the borrower…that whole scenario was established to do whatever they possibly could to get that money to the borrower.[276]

This permissive posture prevailed across the banks. BOI's analysis afterwards was that its commercial property 'credit decisions were…subject to…intensive competitive pressures' while 'the implications of competitors' actions (particularly the quantum of exposures, large exposures, single customer concentrated exposures) were not always fully apparent'[277].

The Property Industry: Where did all the money come from and Who was Getting Rich?

The fact bank lending was so concentrated highlights how the bubble was fuelled not only by credit but the emergence of a wealthy elite of builders, developers and other 'high net worth individuals'. Towards the end of the first phase of Celtic Tiger in 1998 (which had been more exclusively based on foreign direct investment in line with Ireland's capital haven development strategy), newspaper 'Rich Lists' showed that the wealthiest 100 people in Ireland were worth €10.8bn[278]. By 2004 that

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270 "Transcript of Bill Black Hearing," February 5, 2015, 273.
271 cited by Joe Higgins in Michael Walsh, "Transcript of Michael Walsh (INBS) Hearing," September 2, 2015, 84.
272 "Letter from Yvonne Madden, Banking Supervision Department, Financial Regulator to Kevin Cardiff Re INBS," September 15, 2008.
273 "Opening Statement of Michael Fingleton the Banking Inquiry," September 2, 2015, 15.
274 Nyberg, "Nyberg Report," 95 n153.
275 Ibid., 32.
276 "Transcript of Simon Carswell Hearing," 648.
277 Internal document from 2011.
278 Ken Foxe, "MEET THE RICHEST 100 PEOPLE IN IRELAND WORTH POUNDS 8.5 BILLION; 100 RICHEST PEOPLE IN IRELAND," *Irish Daily Mirror*, March 20, 1998.

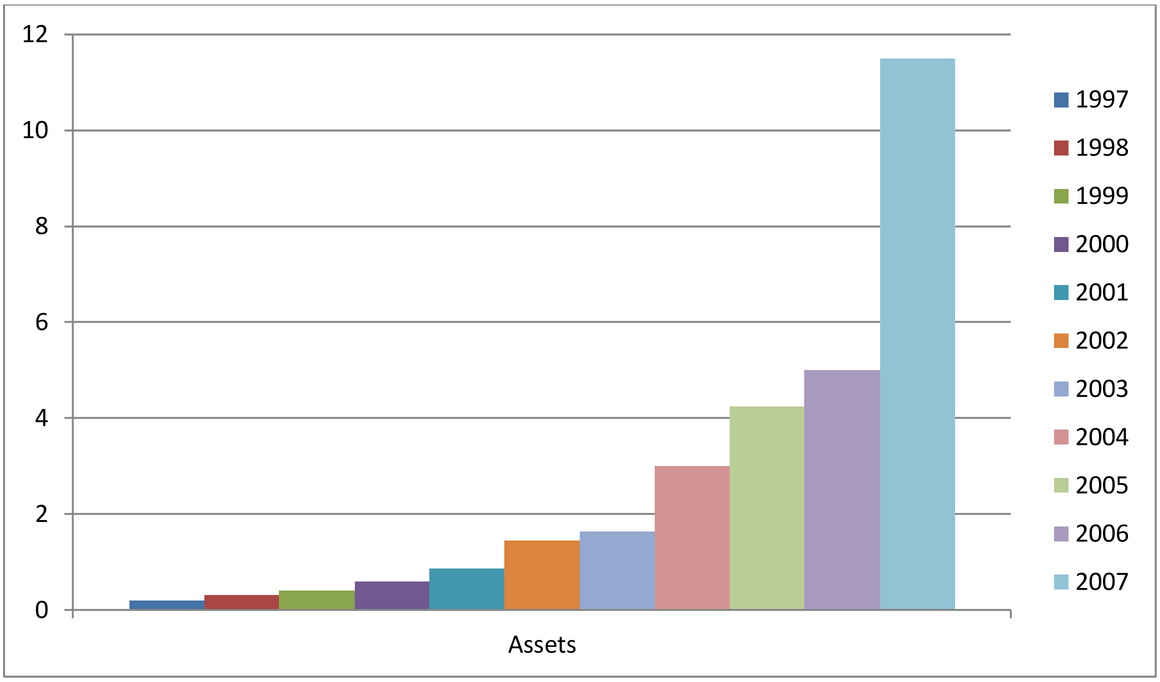
had risen to €25bn[279] and by 2007 to over €35bn. The *Sunday Independent*'s final pre-crash Rich List published in March 2008 showed that just the top 50 richest had €35bn[280], illustrating the enormous accumulation of wealth during the bubble and the growing inequality in Irish society. By far the largest cohort of the Rich List was made up of people whose fortunes flowed from property and construction. By 2004, this was already the largest source of wealth, at 30 of the top 100[281]. This meant that in Ireland as internationally, a 'wall of money' was flooding the market in search of the highest rate of profit. Or, as commercial estate agents, Jones Lang LaSalle, put it, 'The investment market was characterised by large volumes of money seeking product.'[282]

Land speculation is central to developers' profits

The source of these profits was speculation, particularly in land, and debt peonage for ordinary people trying to buy a home. Developers like banks are rentier capitalists in that the primary source of their profits is speculating *with* capital, rather than employing it productively themselves. The scale of accumulation involved is illustrated by Quinlan Private's asset growth, which shadowed that of the banks' balance sheets (Figure 3.1). Some 'developers', for example Derek Quinlan, were pure financiers[283], but even those who were also builders made much of their profits from speculation. Builder/developer, Michael O'Flynn, inadvertently alluded to this in explaining that 'access to finance is the lifeblood of developers in the way raw materials are to a manufacturer'[284]. Notwithstanding this, he denied being a 'land speculator' on the grounds that he only bought land to build on it, rather than just to sell it on[285]. However, this ignores the speculative gain that accrues to *all* developers based on the general increase in land prices between their buying land and selling it on with houses or offices on it. So even though they mightn't be *directly* speculating on land, it still gets included in the price they can charge for a house or an office block.

[279] Carey, "Ireland's Well-Heeled Enter Inner Sanctum of Global Rich; Today's Rich Supplement Shows the Combined Wealth of the Top 100 Has Risen to €25bn."
[280] Sunday Independent, "The Rich List Top 100," *Sunday Independent*, March 30, 2008.
[281] Carey, "Ireland's Well-Heeled Enter Inner Sanctum of Global Rich; Today's Rich Supplement Shows the Combined Wealth of the Top 100 Has Risen to €25bn." The percentages in 2007 were much the same Sunday Independent, "TheTop 100," 2007..
[282] John Moran, "Opening Statement to the Banking Inquiry: Issues Relating to the Nature and Functioning of the Commercial Real Estate Market in the Period prior to 2008 in the Context of the Banking Crisis in Ireland," April 2, 2015, 2.
[283] Derek Quinlan, "Opening Statement to the Banking Inquiry," July 9, 2015, 6.
[284] "Transcript of Michael O' Flynn Hearing," July 22, 2015, 131.
[285] Ibid., 151.

Figure 3.1 Asset Growth of Quinlan Private €bn*



*based on Quinlan's opening statement & media reports

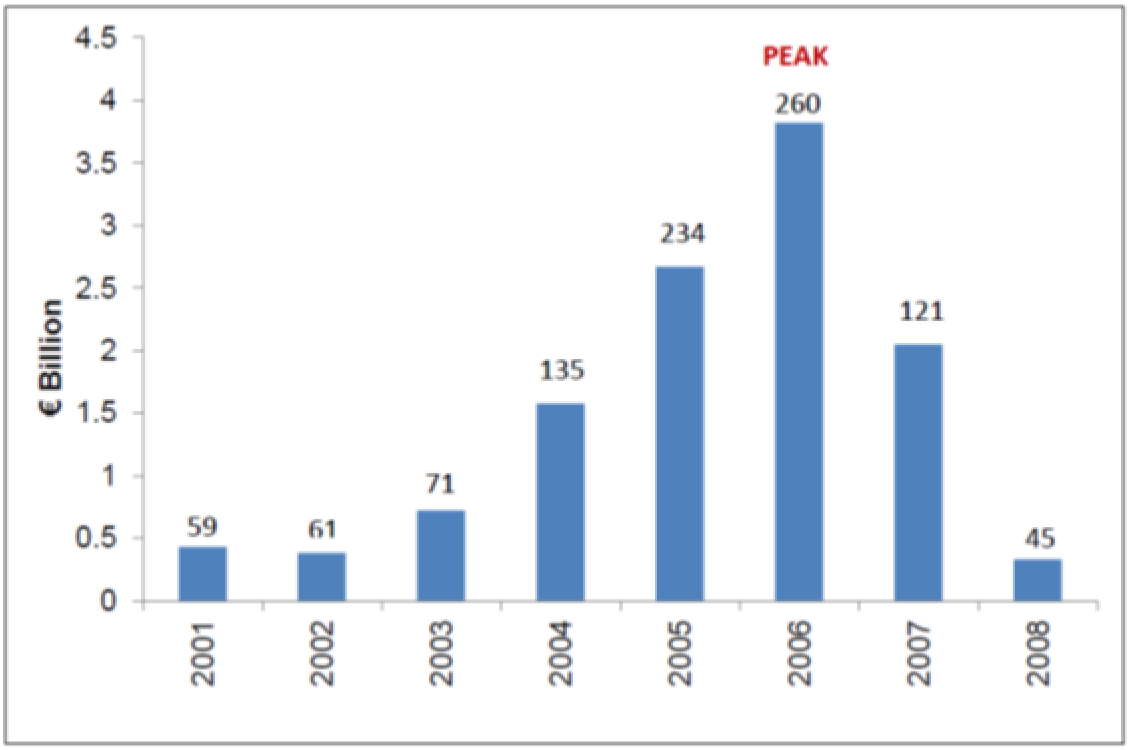
This is hugely significant in understanding how the whole property market works. As O'Flynn also explained to the Inquiry, 'Land drives the price of houses more than anything else'[286]. It's also the fundamental factor of production that links property prices of all types, whether it be zoned or unzoned land, the price of an office or apartment block for a commercial property investor, commercial rents paid by shopkeepers or restaurateurs, or house prices or rents for ordinary workers. Between the early 1990s and the mid-2000s, the percentage of average house prices made up by land costs increased from around 15% – the norm across the EU – to 40-50%[287]. This price gouging was widely recognised at the time. Taoiseach Bertie Ahern openly acknowledged that "what makes houses so dear is the land value" and the then Assistant Director General of the Central Bank, Michael Casey, also highlighted how inflated site costs were escalating housing costs.[288]

The result for workers buying a home was that by 2007, up to eight years of the repayments on a 25-year mortgage were going on 'the excess in the price of the site', amounting to an annual wealth transfer to landowners of €6.6bn[289]. The same dynamic applied across the economy. Spiralling land prices drove up commercial rents and consumer prices and with them the *Rip Off Republic* of the bubble. Towards the end, it also meant developers 'had to' cream off huge profits from their

[286] Ibid., 137.
[287] Fearghal O'Connor, "Is Dublin's Land Being Hoarded," *Business & Finance Magazine*, August 12, 2004; Eamon Gilmore, "Private Members' Business. - Planning and Development (Acquisition of Development Land) (Assessment of Compensation) Bill, 2003: Second Stage.," October 7, 2003, http://oireachtasdebates.oireachtas.ie/Debates%20Authoring/DebatesWebPack.nsf/takes/dail200310070002 0#N17; Irish Council for Social Housing 2006, cited in Michael Hennigan, "Dysfunctional Development Land Systems in UK and Ireland - Part 2," *Finfacts Ireland*, October 8, 2014, http://www.finfacts.ie/irishfinancenews/article_1028286.shtml.
[288] quoted in Gilmore, "Private Members' Business. - Planning and Development (Acquisition of Development Land) (Assessment of Compensation) Bill, 2003: Second Stage."
[289] quoted in O'Connor, "Is Dublin's Land Being Hoarded."

developments in order to fund further speculative land purchases. Michael O'Flynn explained: 'we were making larger profits, but those profits were necessary to replace land because the land cost was going up so much'[290]. According to Marie Hunt of CBRE, €12.5bn was invested in development land in Ireland from 2001-8, with annual investment growing from less than €0.5bn in 2001 to a peak of €4bn in 2006[291] (Figure 3.2). One of the main causes of spiralling land costs was the control of development land, including 'land suitable for housing…by a relatively small number of landowners and developers'. In Fingal, around 25 big developers controlled more than half of land suitable for housing, giving them 'a monopoly-type influence on the availability and price of land and, as a result, the price of housing'[292]. This was enormously profitable for landowners and developers and incentivised the vast amount of planning corruption exposed by the various tribunals.

Figure 3.2 Irish Investment in Development Land 2001-2008[293]



Marie Hunt of commercial estate agents, CBRE, illustrated how small the commercial property speculating elite was when she told the Inquiry that only 50-60 Irish investors accounted for the entire investment in non-residential income-generating commercial property[294] in Ireland each year. Also, unlike other areas of the Irish economy that are dominated by foreign investment, this was one area domestic capitalists had sole domain because deals here were seen as too small for foreign investors to bother with[295]. This meant a very small number of people accounted for that entire

[290] "Transcript of Michael O' Flynn Hearing," 137.
[291] "Marie Hunt Opening Statement to Banking Inquiry," April 2, 2015, 7.
[292] P. J. Drudy, "Housing in Ireland: Philosophy, Affordability and Access," *Journal of the Statistical and Social Inquiry Society of Ireland* 36 (February 1, 2007): 98.
[293] Hunt, "Marie Hunt Opening Statement to Banking Inquiry," 7.
[294] Hunt used this rather complicated category to distinguish this area from residential property development and from development land that could be used for either residential or non-residential commercial property development.
[295] "Transcript of Marie Hunt (CBRE) Hearing," April 2, 2015, 1057.

market here and also the €46bn invested by Irish residents in that market in Ireland and overseas from 2001-8. More than three-quarters of this went outside the country[296] and by definition provided no benefit to anyone in Ireland – apart from the speculators borrowing billions from Irish banks to fund it.

Two of the largest NAMA debtors, Sean Mulryan and Derek Quinlan[297] had invested mainly overseas, with over €2bn of Mulryan's €2.4bn debt owed for property in the UK[298]. The €12.5bn invested in development land[299] and the billions that went into residential property development from 2001-8 were additional to the €46bn spent on non-residential commercial property. However, even at the peak of the bubble in 2006 when over 90,000 houses were built in Ireland, this still only accounted for 'about half of the total of construction output'[300], indicating the huge level of activity in other areas of commercial property, such as shopping centres, offices, hotels and so on.

The property investment pyramid scheme

Based on Irish non-residential commercial property returns from 2001-8[301], someone who invested €1m in 2001 would on average have ended up with an asset plus returns worth €2.41m by 2007 – an increase of 141% without doing anything whatsoever. The same investor would have subsequently suffered a 60-70% loss, bringing the value of his investment back down to €723,000-€964,000. At that stage, however, if he was lucky enough to be a big developer bailed out by NAMA, the taxpayer would have footed the difference by buying his loan off AIB or Anglo and then paying him to 'manage' it. In reality though, the investor need not even have had €1m of his own to invest in the first place, as the banks were routinely providing up to 80% funding[302]. So with €200,000 to invest in 2001, he could have made €2.21m by 2007 minus the €800,000 he borrowed from the bank, leaving him with a speculative gain of €1.61m, more than eight times his original investment – less whatever (increasingly) low rate of interest he had to pay banks competing for his money.

Developer/financier, Derek Quinlan explained to Joe Higgins the scale of increased profits made possible by this 'leveraging' process, even where a much lower level of borrowing (50%) was involved:

> you measure the return on an investment, on the amount of equity that is invested. So if you buy a property for €1 million and you invest €1 million in it so there is no borrowing and the property is producing, we will say, 7%, you're getting a 7% return on your €1 million. But if, in fact, you can gear that and put in half a million bank debt…then you are improving the return on your equity because after 12 months, if you sell the property, we'll say, for €1.1 million, then there is a much higher return on your equity because you have only €500,000 of equity in there. You're earning 20% on your equity in a year.[303]

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[296] "Marie Hunt Opening Statement to Banking Inquiry," 6.
[297] Quinlan, "Opening Statement to the Banking Inquiry," 3.
[298] Sean Mulryan, "Opening Statement to the Inquiry," July 22, 2015, 12.
[299] "Marie Hunt Opening Statement to Banking Inquiry," 7.
[300] Parlon in Tom Parlon and Liam Kelleher, "Transcript of Construction Industry Federation Hearing," May 13, 2015, 13.
[301] "Marie Hunt Opening Statement to Banking Inquiry," 3.
[302] "Transcript of Marie Hunt (CBRE) Hearing," 1059; Mulryan, "Opening Statement to the Inquiry," 16.
[303] "Transcript of Derek Quinlan Hearing," July 9, 2015, 40.

What many property speculators were doing as well was re-investing their speculative gain but without actually selling the original property on and realising it. So in effect they were using what NAMA CEO, Brendan McDonagh, called 'unrealised "paper" equity' to borrow more money to invest in more property and 'leverage' their original €200,000 or €500,000 even more. The Chair of NAMA, Frank Daly, explained how this worked:

> in many cases… a developer's equity contribution was in the form of a rolling-up of unrealised, paper profit from other developments i.e. unrealised equity positions levered by the developer to secure funding for new transactions… In effect, therefore, the banks were providing all of the real cash funding for both acquisitions and development…quite often the borrower's paper equity position never paid for an acre of land or concrete or scaffolding or a worker's wage…[304]

Sean Mulryan acknowledged using this 'unrealised equity' funding model but explained how at the time, he actually saw this as reflecting the success of his business: 'We'd a lot of equity in our business. We weren't taking money out of the business. We were reinvesting continuously. All our profits were going back in, and so they were happy with the situation at the time.' [305] From his perspective, this made perfect sense as reinvesting 'profits' is how capitalism works. As his fellow developer, Michael O'Flynn, put it: 'you don't make profit in business unless you invest in business'[306]. From this capitalist perspective , there's also no meaningful difference between realised and unrealised or 'paper' profit/equity – until the market collapses and exposes the unrealised 'profit' as fictitious. This was essentially what happened across the banks and the stockmarkets too, as the balance sheets and share prices of the banks all depended on fictitious property valuations that incorporated paper equity. The whole process represents a structural flaw inherent to capitalism. It's part of what makes it so crisis prone, and then so 'pro-cyclical' in a crisis.

To make matters worse, Simon Carswell explained that 'In some instances, the actual supposed equity or cash that was used in these deals would itself be borrowed so that in some transactions there would be debt on debt on debt and very little cash…'[307] Mulryan acknowledged using 100% bank funding, explaining that 'Ballymore …utilised a range of funding structures, from 100% equity funded, to 100% debt funded (when available) to a loan to value range of anywhere from 60% to 90%, with 80% being typically available.'[308]

This pyramid scheme could go on indefinitely – until it collapsed and caused the crash – and one reason property and credit bubbles so often go hand in hand. Bedazzled by the huge profits they were making, the banks ignored the huge risks involved. Or as NAMA's Frank Daly diplomatically phrased it, 'the banks were taking the type of risk normally the preserve of private equity/hedge fund providers without demanding the same level of rigorous analysis'[309]

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[304] "Opening Statement by Mr. Frank Daly, Chairman of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," April 22, 2015, 2.
[305] Sean Mulryan, "Transcript of Sean Mulryan Hearing," July 22, 2015, 92.
[306] "Transcript of Michael O' Flynn Hearing," 158.
[307] Carswell, "Transcript of Simon Carswell Hearing," 651.
[308] Mulryan, "Opening Statement to the Inquiry," 16.
[309] "Opening Statement by Mr. Frank Daly, Chairman of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," 4.

A landowner or developer could bag an even bigger windfall if tax incentives were involved, as Fianna Fáil ensured there usually were[310], or if he managed to 'persuade' local councillors to rezone his land. The scale of the cost-savings involved are evident from a Goodbody Economic Consultants report on area-based property tax reliefs commissioned by the Department of Finance. It found that 'tax costs represent up to 43 per cent of the building cost associated with developments undertaken as part of the Schemes.'[311] Planning corruption was equally lucrative. According to one property expert, writing in 2007, 'politicians are bribed to re-zone, being paid by the landowner from the added-value on re-zoning, which can be of the order of a factor of ten; this currently accrues to the landowner as a parasitic windfall.'[312]

Boom & Bust: The Capitalist Property Cycle

The speculative nature of the property industry has been widely recognised for decades. It's known to create periodic cycles of boom and bust that recur with even greater frequency than in other sectors of the capitalist economy. This was also explained by Hunt, who provided a diagram CBRE use of the commercial property cycle (Figure 3.3). She argued that 'Taking this pattern into account, an Irish commercial property correction was predictable in the period up to 2007'[313] but that the scale of it was not anticipated. She also told the Committee,

> Of course we are going to have another property bubble because we are in a cyclical market. If we look at where we stand today, relative to other peaks, we are probably mid-cycle again and it will always, invariably, follow the same pattern[314].

The snag, she explained, is that

> what one never knows is how quickly one will move around that cycle or how long one will be at any particular stage because in real estate things happen. It could be a geopolitical issue or a financial issue that will trigger the crash or downturn in each case but it usually follows this pattern.[315]

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[310] Property-related tax incentives are dealt with in detail later.

[311] Goodbody Economic Consultants, "Budget 2006: Review of Tax Schemes Volume II: Goodbody Review of Area-Based Tax Incentive Renewal Schemes" (Department of Finance, November 2005), ii, http://www.finance.gov.ie/sites/default/files/Taxrev2006vol2.pdf.

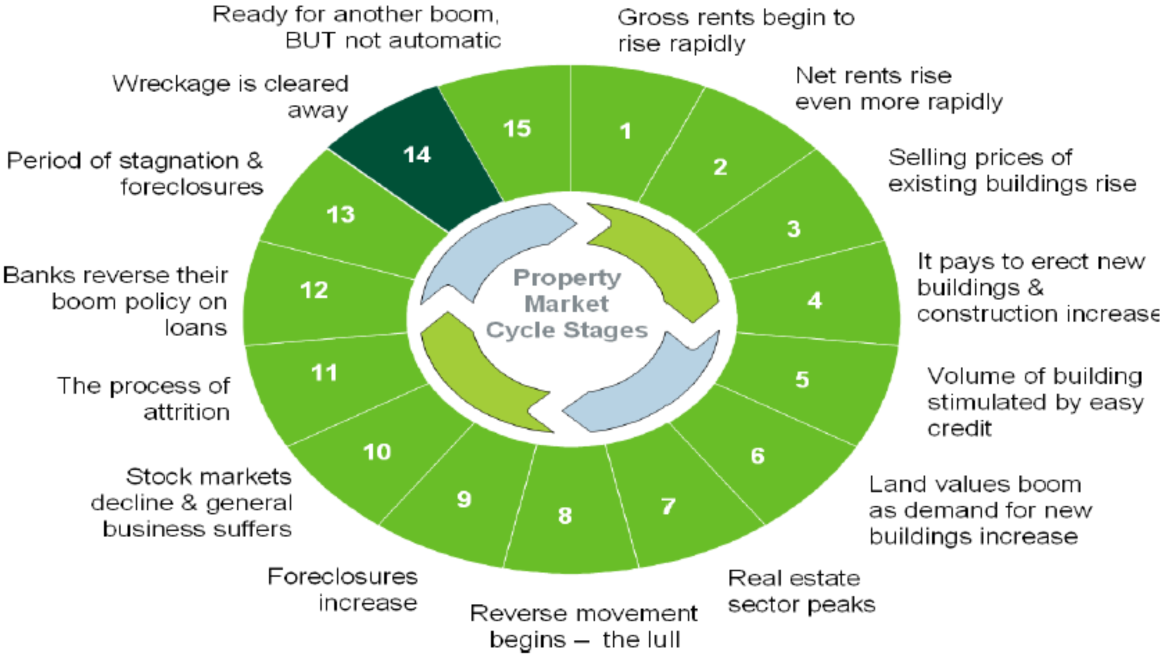
[312] Roy Johnston, "Comment from Roy Johnston, Techne Associates on Paper by P.J. Drudy," *Journal of the Statistical and Social Inquiry Society of Ireland* 36 (February 1, 2007): 125.

[313] "Marie Hunt Opening Statement to Banking Inquiry," 3.

[314] "Transcript of Marie Hunt (CBRE) Hearing," 1080.

[315] Ibid., 1078.

Figure 3.3 Stages of a Typical Property Market Cycle[316]



For many years before the crash, residential and non-residential property prices[317] had been rising in tandem, and before the crash, both of them clearly showed a bubble (Figures 3.4 & 3.5). The Central Bank included a paper in its 2006 *Financial Stability Report* demonstrating the correlation between different types of residential and non-residential property prices[318] (Figure 3.6). This might logically have created an expectation prices would fall together too, especially as residential and non-residential property prices depend on fundamentally the same land market, as well as being linked through general economic conditions. The former CEO of AIB, Eugene Sheehy, acknowledged this in his opening statement, commenting that 'Between 1995 and 2007 [non-residential] commercial property values increased by about 200% and residential by 180%'[319]. Yet despite this, Sheehy claimed not to have been aware of the close correlation between the prices of different types of property at the time. In fact, he said AIB had regarded its involvement in different parts of the property market as a way of protecting itself from risk[320]. Similar claims were made by other witnesses.

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316 "Marie Hunt Opening Statement to Banking Inquiry," 6.
317 Alan Kearns and Maria Woods, "The Concentration in Property-Related Lending — a Financial Stability Perspective," in *Financial Stability Report 2006* (Central Bank, 2006), 133–44, http://www.centralbank.ie/publications/Documents/Part%201%20-%20Financial%20Stability%20Report%202006.pdf.
318 Ibid.
319 Eugene Sheehy, "Opening Statement to the Banking Inquiry," April 29, 2015, 3.
320 Ibid., 4–5.

Figure 3.4 Average New House Prices vs. Average Annual Earnings[321], 1995-2007

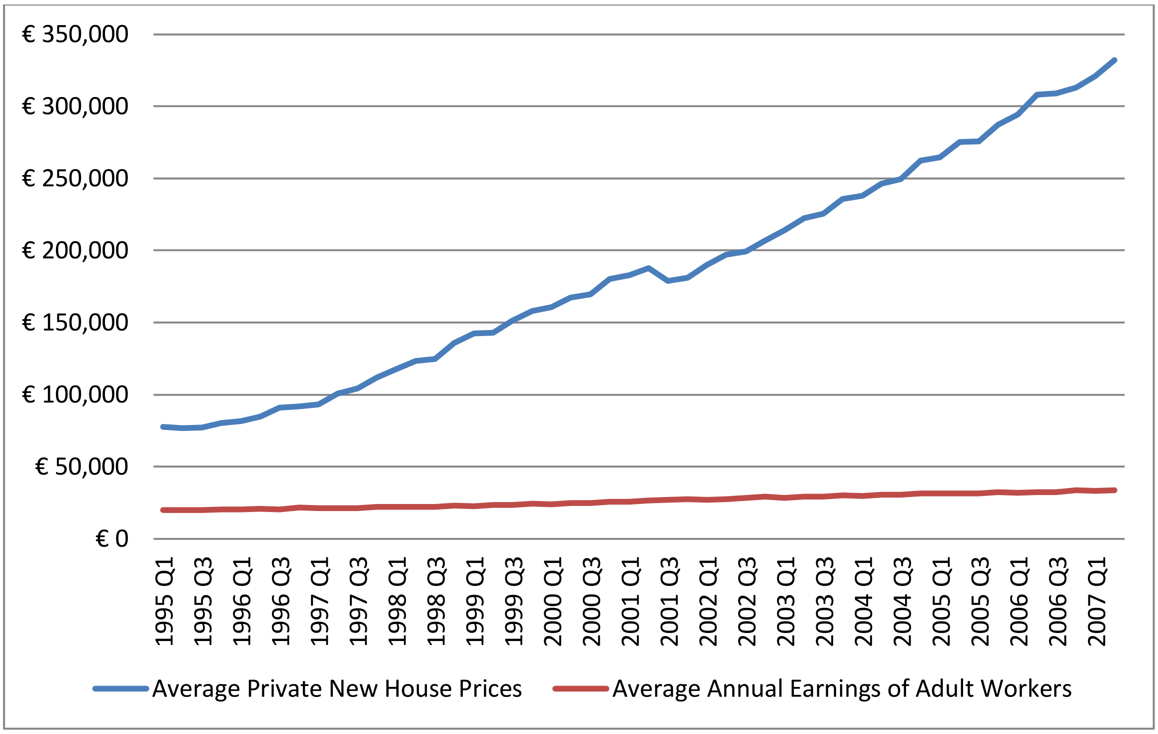
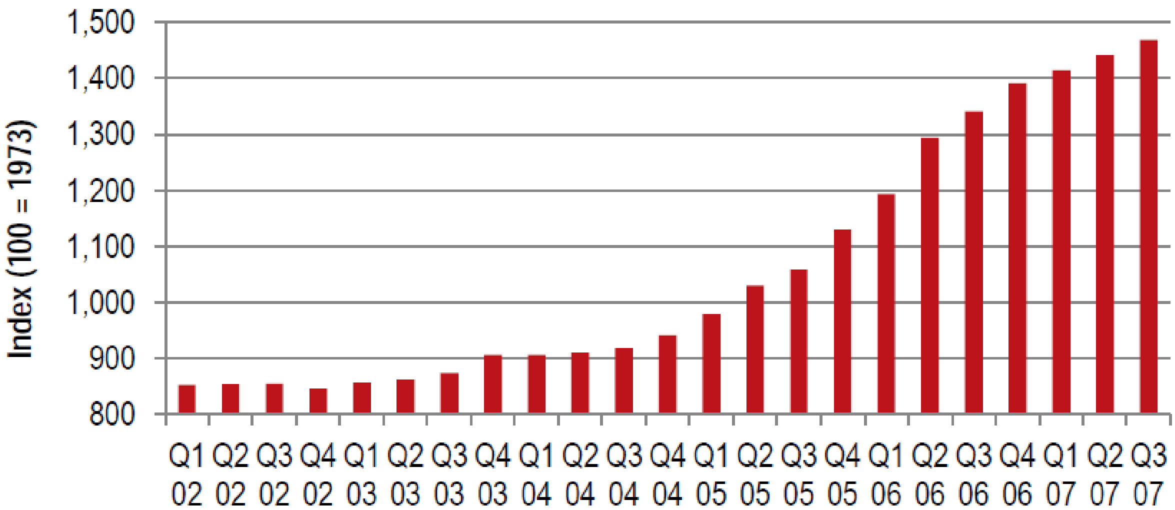


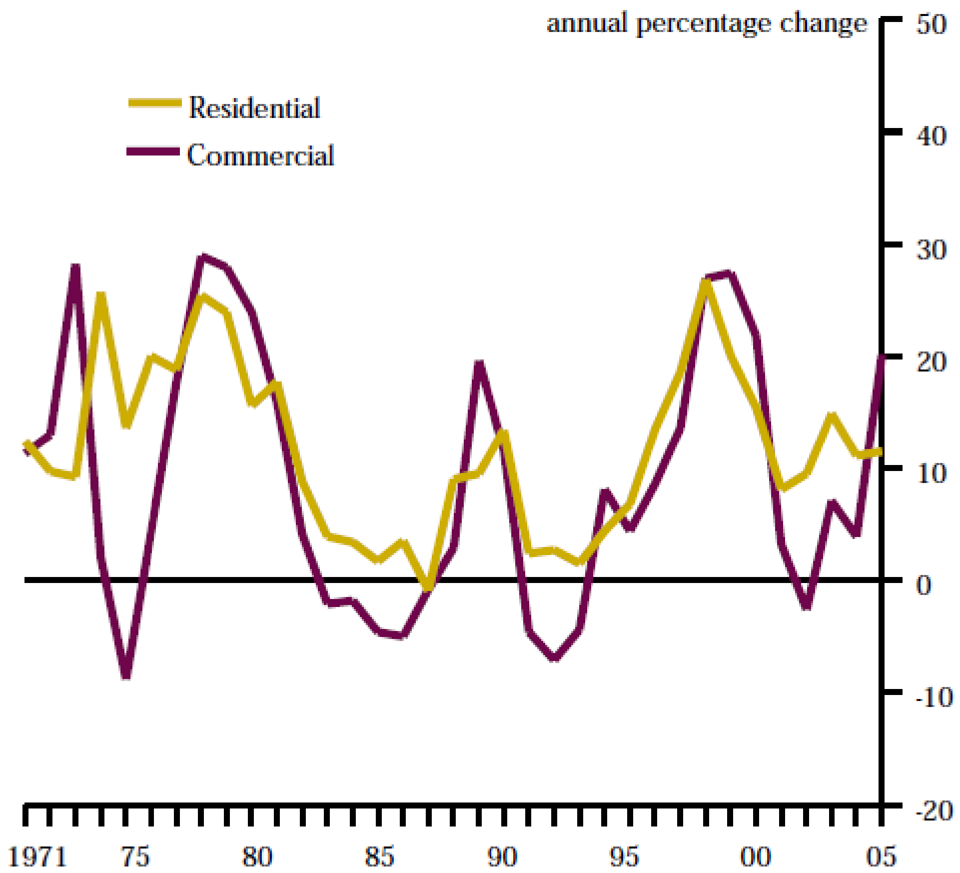
Figure 3.5 Jones Lang LaSalle Irish Non-Residential Property Index – Capital Values[322]



[321] Department of the Environment, Community & Local Governmen, "Housing Statistics: House Prices, Loans and Profile of Borrowers," July 7, 2014.

[322] Moran, "Opening Statement to the Banking Inquiry: Issues Relating to the Nature and Functioning of the Commercial Real Estate Market in the Period prior to 2008 in the Context of the Banking Crisis in Ireland," 1.

Figure 3.6 Correlation of Growth in Capital Values of Residential and Commercial Property[323]



Yet as soon as the market began to turn and developers, estate agents and banks were no longer blinded by all the money they were making, the realisation dawned that all elements of the property market are linked – on the way down as well as the way up. CBRE were certainly aware of this given how negatively they reacted to the April 2007 RTE documentary, *FutureShock*, which was about house prices, despite them being a purely non-residential property estate agent. Hunt explained their reasoning: 'The driving force was that even though we were not in the business of selling houses, we were in the business of commenting on what was happening with land and ultimately that is all related'[324]. The other non-residential estate agent who testified before the Inquiry, John Moran of Jones Lang LaSalle, agreed, stating that 'The underlying strength of the residential market also contributed significantly to the high levels of land value that pertained.'[325]

Too Blinded by Profit to See the Bubble

All of this highlights how the giant bubble blown up by inequality of wealth, easy credit, leverage and speculation should have been apparent to anyone with expertise in residential or non-residential

[323] Kearns and Woods, "The Concentration in Property-Related Lending — a Financial Stability Perspective," 40.
[324] "Transcript of Marie Hunt (CBRE) Hearing," 1087.
[325] Moran, "Opening Statement to the Banking Inquiry: Issues Relating to the Nature and Functioning of the Commercial Real Estate Market in the Period prior to 2008 in the Context of the Banking Crisis in Ireland," 4.

property, banking or economics. In practice, they were nearly all property speculator, Derek Quinlan like former finance professor and Chair of INBS, Michael Walsh, who told the Inquiry:

> I look back and say, "Why didn't I see it?" I suspect everybody who is in authority in any of the economic bodies now looks back and says "Why didn't they see it?" But the practical reality is that nobody saw it at the time[326].

What lay behind this apparent blindness, in Ireland as overseas, was that it suited the wealthy elites getting richer and richer speculating on the bubble – and their acolytes in the establishment parties, the toothless regulators they had appointed, and the entire mainstream media and economics profession – to ignore the bubble until it burst. As former Anglo director, PR consultant, property investor, and friend of Brian Cowen[327], Fintan Drury, admitted,

> We had gorged in the boom years and the banks had continued to feed our insatiable appetites. I know. I know because I was involved in both putting the menu on the table as a non-executive director of Anglo Irish Bank, and I know because I…sat there and ate more than I needed[328].

It was that type of repellent greed, combined with the incestuous relations of developers, bankers, politicians, state agencies and media, that explain why the banks apparently 'considered property lending to be almost a one-way bet, notwithstanding the well-established cyclical behaviour of property markets'[329] – and why nothing was done to stop them. As *Irish Times* journalist and author of *Anglo Republic*, Simon Carswell, told the Inquiry:

> I would characterise the relationship between the major players in the property sector and construction industry and government, certain elected representatives and the banks – as well as the relationship between the government, the banks and the financial supervisory authorities - as extremely cosy in the period leading up to the 2008 banking crash[330].

In addition, a significant supporting layer of other 'high net worth individuals' (HINWIs), including wealthy mainly self-employed professionals, such as lawyers, architects and accountants, aped the big capitalists by participating in syndicates, sheltering their income using property-related tax breaks, and taking out €21bn in buy-to-let mortgages.

Simon Carswell explained how Anglo used funds deposited by HINWIs in its 'wealth management' division to fund property deals the Bank was arranging with developers:

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326 "Transcript of Michael Walsh (INBS) Hearing," 83. Likewise, property speculator, Derek Quinlan claimed 'Nobody saw what was coming', Terence O'Rourke, an auditor for KPMG said that 'best information did not accurately predict the future. We had a very extreme event occurring which nobody foresaw, virtually nobody foresaw'; and Eugene Sheehy of AIB said they had faced one in a hundred year' event. "Transcript of Derek Quinlan Hearing," 67; "Transcript of Paul Dobey (KPMG) Hearing," May 14, 2015, 115, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/14052015_Dobey_vol1.pdf; "Transcript of Eugene Sheehy and Michael Buckley (AIB) Hearing," April 29, 2015, 8.

327 "Transcript of Fintan Drury Hearing," July 30, 2015, 14–17; "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," July 2, 2015, 66.

328 "Transcript of Fintan Drury Hearing," 6.

329 "Opening Statement by Mr. Brendan McDonagh, Chief Executive of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," April 22, 2015, 11.

330 Carswell, "Opening Statement to the Banking Inquiry," 2.

> Anglo Irish Bank had a wealth management division where many people had money on deposit, many of whom would also have been borrowers at the bank. When there were opportunities to do deals for the wealth management division, the bank used the pot of money already in the bank to help to buy these deals…In some instances, the actual supposed equity or cash that was used in these deals would itself be borrowed so that in some transactions there would be debt on debt on debt and very little cash in the transaction.[331]

According to Marie Hunt of CBRE, 56% of the Irish non-residential commercial property investment market was made up by 'developers' and 'private investors' , with syndicates of 'high net worth individuals' making up another 26%.[332] It was this relatively narrow social bloc that profited from the bubble and did everything they could to keep it going, and when that failed to pass the cost onto everyone else. In this regard, the personal involvement of establishment party politicians in the property industry and property investment deserves a special mention. In November 2007, RTÉ *Prime Time* reported that 22% of councillors dealt in or developed land through their day jobs as estate agents, landowners and builders. In Enda Kenny's home county of Mayo, that figure rose as high as 45%; in Brian Cowen's Offaly it was 44% and in eight other counties it was 33% or more.[333] Similarly, according to the 2007 Dáil Register of Interests, 39 of the 78 Fianna Fáil were landlords or owned some form of commercial or residential investment property. The percentages for Fine Gael were almost identical, at 25 out of their 51 TDs. In addition, 10 Fianna Fáil and 7 Fine Gael TDs had shares in property or construction companies and 3 TDs apiece were directors of property companies or auctioneering firms. The next most common investment category was bank shares which were held by 11 Fianna Fáil and 11 Fine Gael TDs, including Michael Noonan who in 2007 had shares in Anglo, but subsequently moved his money into German government bonds.

The Structural Influence of Elite Relationships

Although the web of relationships between all the various elites and its role in the bubble fell squarely within the terms of reference agreed by the Committee, it was difficult to question witnesses on these more political topics because of the legal strictures imposed on Members. Nonetheless, a recurrent theme was the close relationship between developers and the establishment parties, particularly Fianna Fáil as the historic party of government with their hands on the till. As dominant sections of the domestic economy and Irish capitalist class, the political influence of builders, developers, bankers and the property, construction and financial industries generally runs deep. It is evident in the revolving door between business and politics, the overlapping membership of state and corporate boards, the socialising and shared worldviews within the golden circle and the public clear statements of prominent politicians that their *raison d'etre* is to serve business interests – which it goes without saying are identical to the 'public interest'. Taoiseach Bertie Ahern told the Annual IBF/FIBI Lunch in March 2006:

> the Government is very conscious of its role in assisting you to maintain a healthy bottom line. I am confident that the partnership between Government and the banking community will continue to remain strong for the benefit of this country… there is a need to be more

331 "Transcript of Simon Carswell Hearing," 651.

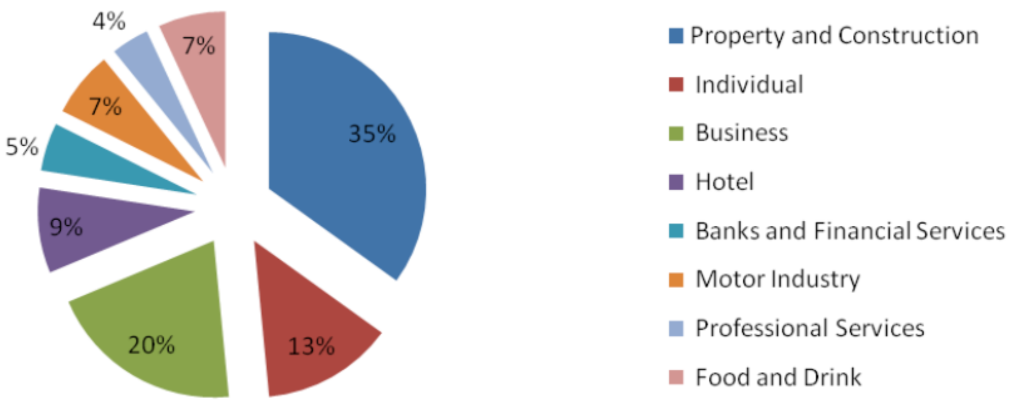
332 The remainder of both markets was made up of institutional investors, investment funds, occupiers etc. Outside of Ireland, there was a similar split, with 58% 'developers' and 'private investors' and 25% syndicates

333 Hennigan, "Dysfunctional Development Land Systems in UK and Ireland - Part 2."

balanced and less negative about the essential services you provide…Clearly a thriving banking community – both domestic and international – is good for the economy as a whole.[334]

Political donations were only the tip of the iceberg as the most obvious way 'Politics and business regularly overlapped'[335]. Nevertheless, the pattern of donations in the 1990s and 2000s gives an indication of what lay beneath. Evidence from Dr. Elaine Byrne, showed 35% of declared Fianna Fáil donations from 1997-2007 came from 'property and construction interests', with another 5% from banks and financial services (Figure 3.7).

Figure 3.7 Disclosed Donations of Fianna Fáil 1997-2007[336]



In line with what Byrne described as an apparently 'deliberate policy by political parties of soliciting donations below the disclosure thresholds', Fine Gael disclosed no donations at all from 2001-7[337]. However, there is no reason to believe their funding sources were any different from Fianna Fáil's. The current and former Director-Generals of the Construction Industry Federation confirmed that business people in general and builders and developers in particular supported either Fianna Fáil or Fine Gael:

> Tom Parlon: back in the day when I was running for election in 2002 in Laois-Offaly, you were either Fine Gael or you were Fianna Fáil…people that would have been in business at that time were one way or the other, and I'm sure they were approached and made their contributions…[338]

> Liam Kelleher: There were members who were close to Fianna Fáil, there were members who were close to Fine Gael[339]

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[334] Finfacts Team, "Taoiseach Praises Contribution of Banks," March 31, 2006, http://www.finfacts.ie/irelandbusinessnews/publish/article_10005395.shtml.
[335] Carswell, "Opening Statement to the Banking Inquiry," 3.
[336] Elaine Byrne, "Opening Statement to the Banking Inquiry," March 12, 2015, 11.
[337] Ibid., 4–5.
[338] Parlon in Parlon and Kelleher, "Transcript of Construction Industry Federation Hearing," 11.
[339] Ibid., 22.

All the big developers who answered the question admitted making political donations[340]. Joe O'Reilly disclosed €74,000 in political donations from 2002-8[341]. Despite finding it 'difficult to provide exhaustive detail', Peter Cosgrave disclosed just under €50,000 in donations, two-thirds of it to Fianna Fáil and around a fifth to Fine Gael [342]. O'Reilly and Gerard Barrett also said they had provided accommodation to political parties for electioneering, in Barrett's case to the Labour Party in Galway[343].

Dr. Byrne explained:

> when particular sectors have donated in such large amounts to political parties, it suggests they were doing so because they were seeking influence or they felt it was necessary…In the 1980s, the beef industry was donating to all political parties because beef was the biggest indigenous industry in Ireland at the time. In the 1990s and 2000s it was property, because property was fuelling the economy…Donations often reflect the make-up of the economy. Regarding the donations to Fianna Fáil, the property sector, auctioneers and solicitors were prominent donors, as were banks and the motor industry. They were the industries and sectors of the boom.[344]

This highlights, in a very real and direct way, how economic power translates into political power. Following on from this, Byrne was asked if 'those who are making the donations are seeking to influence those who hold the reins of power?', she simply answered 'yes'[345]. Byrne also advocated investigating 'soft' loans to politicians, which were reportedly given by Michael Fingleton to such prominent figures as Charlie McCreevy, Phil Hogan and Bertie Ahern's ex-partner, Celia Larkin. Fingleton's business partner in his personal property investments, Fianna Fáil Senator Francie

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[340] Bernard McNamara submitted an extremely short statement that failed to answer much of what he was asked. "Written Statement of Bernard McNamara," October 2015, https://inquiries.oireachtas.local/banking/participant/BMN/EvidenceDocuments/BMN01B01/Bernard%20McNamara%20Witness%20Statement.pdf. John Ronan said neither he nor Ronan Group Real Estate had made political donations from 2001-8 'As far as I can recall'. "Written Statement of John Ronan," September 2015, 16. However, SIPO records show he donated €1,000 each to Fianna Fail's Marian McGennis and Liam Cosgrave in 2002. He also donated €10,000 to Labour's Ruairi Quinn (then the outgoing Finance Minister) and €1,000 to Fianna Fail's David Andrews in 1997. Irish Times, "Quinn Was Biggest Recipient of Political Donations by Far," *Irish Times*, June 12, 1998, http://www.irishtimes.com/news/quinn-was-biggest-recipient-of-political-donations-by-far-1.162213.. His best well known property company, Treasury Holdings, was also one of a host of property and construction companies that took out advertisements in Fianna Fail's 75th anniversary brochure in 2001. Vincent Browne, "Inadequacy of Political Donations Legislation," *Irish Times*, May 5, 2010, http://www.irishtimes.com/opinion/inadequacy-of-political-donations-legislation-1.661225.

[341] "Opening Statement of Joe O'Reilly," July 23, 2015, 12.
[342] "Written Statement of Peter-Cosgrave," August 2015, 7–8.
[343] "Written Statement of Gerard Barrett," September 2015, 22.
[344] "Transcript of Elaine Byrne Hearing," March 12, 2015, 766.
[345] Ibid.

O'Brien, also had loans from INBS[346]. According to the Honohan Report, 'it was understood by all that [Michael Fingleton] was politically well-connected'[347].

Other indications of the closeness of the political system to the property and construction industry include the revolving door between the two. According to Simon Carswell, 'Individuals who worked in the political arena afterwards took up highly paid roles representing and lobbying on behalf of construction and financial industry groups, interacting with people they had previously worked closely with in politics'[348]. A case in point was Tom Parlon's transition from Minister of State for the OPW with responsibility for handing out state construction contracts to head of the Construction Industry Federation. According to an *Irish Independent* interviewer , he was 'completely unapologetic about using his political connections to up the odds, proudly describing how he's approached several ministers personally, including former PD colleague Mary Harney', but simultaneously 'rejecting the notion that there's anything "cosy" about the seepage between the lobbying and political scenes.' Parlon was quoted as saying: "I'm in and out of the Dáil every other day, any chance I get...everybody does it"[349]. When asked about this in the Inquiry, he answered:

> there's no doubt knowing how government works, or having an understanding of how government works is certainly a help…I had just lost my seat at the time in 2007…And I was approached about this job… I have no doubt that having the experience of being in government and so on was a help[350].

Records provided to the Inquiry by the Department of Finance showed 160 'solicited and unsolicited representations (in the form of minutes of meetings or formal written correspondence) made by representative bodies of valuers, auctioneers and the construction industry…regarding the importance of the property sector to the Irish economy' from 2001-2010 and a further 33 to the Department of Taoiseach. This *did not* include representations from individual developers, which the Inquiry was told were too numerous to count.

Interlocking board memberships, the hiring of consultants and experts by government agencies one day and property companies or banks, and shared social circles of elites, also reflect the symbiotic relationships between property, banking and politics.

The web around Sean Mulryan is just one example. The chief operations officer of Mulryan's company, Ballymore Properties from 2007, David Brophy, was on the board of INBS[351]. Ballymore was INBS's biggest borrower and had been involved in joint ventures with the specialist developers' bank since 1992. One of these, Clearstorm, had as a director the consultant, Peter Bacon, who produced a series of reports on the property market for the Fianna Fail-PD government in the late 1990s and early 2000s. Bacon was also European Director of Ballymore Properties from 2004 until

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346 William Nestor, "Newsmaker - Who Is Michael Fingleton?," *JOE.ie*, 2013, http://www.joe.ie/news/newsmaker-who-is-michael-fingleton/9982.

347 Patrick Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," May 31, 2010, 17 n12.

348 Carswell, "Opening Statement to the Banking Inquiry," 3.

349 Laura Noonan, "The Interview: Tom Parlon, CIF Chief," *Irish Independent*, October 28, 2010, http://www.independent.ie/business/irish/the-interview-tom-parlon-cif-chief-26693763.html.

350 Parlon and Kelleher, "Transcript of Construction Industry Federation Hearing," 23.

351 "Transcript of Michael Walsh (INBS) Hearing," 111; "Transcript of Michael Fingleton Hearing," September 2, 2015, 71, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/09/02092015_Fingleton_vol1.pdf.

the summer of 2008[352] and was described by Bertie Ahern in an interview with the *Irish Times* as "a good friend of mine". In late 2008-early 2009, he was chosen by Brian Lenihan to devise a model for a bad bank[353], which became NAMA and took over Sean Mulryan's debts and paid him a salary of over €200,000 a year[354]. Mulryan had longstanding connections to Fianna Fáil – lawyers for the Planning Tribunal revealed he had paid Liam Lawlor TD, the equivalent of €64,000 from 1994-1997.[355]

In July 2004, Mulryan had a private meeting with Taoiseach Bertie Ahern, Ken McDonald (Hooke & McDonald) and two other developers, Michael O'Flynn and Bernard McNamara[356]. The agenda included discussions on 'the amount of zoned land', 'the infrastructure/services required to service zoned land' and implementing the Part V social and affordable housing obligation after it has been watered down following earlier lobbying by developers. Mulryan disclosed over €128,000 in political donations from 2001-2007: 55.5% to Fianna Fáil, 19.5% to Fine Gael, and 8% to Labour[357]. He also knew government ministers personally. According to Fintan O'Toole's book *Ships of Fools, '*Seán Mulryan's annual Christmas parties at his Kildare stud farm, Ardenode, were just one of the social occasions when [Sean] Fitzpatrick [of Anglo] and his developer clients would have mingled intimately with Charlie McCreevy and Brian Cowen'[358] Mulryan was also one of 18 donors who paid €1,000 each to play golf with Brian Cowen to raise funds for his 2007 election campaign. He seems to have maintained his political connections despite the crash, travelling to China with Ahern several times in 2011 on trips organised by the Ireland China Co-operation Council. Cowen also acknowledged meeting him socially only a few days prior to Cowen's first appearance at the Inquiry[359].

Lobbying & Direct Policy Influence

Of course, it's usually impossible to prove that a particular relationship or 'business-friendly' attitude produced a particular policy outcome. All we can do is point out those relationships exist, that these interactions happen, and that politicians take decisions that benefit business elites they have 'relationships' with and speak supportively about. As Simon Carswell put it, 'Easy and ready access to politicians brought easy and ready access to policy and decision-making that drove the growth of the property and financial sectors'[360] .

The Influence of Banks

Despite the long history of banking scandals in Ireland, which included Ansbacher, DIRT, and the collapse of ICI to name but a few, the banks were encouraged to regulate themselves. They effectively wrote their own rules in 'consultation' with the Regulator, who then trusted them to

[352] Justine McCarthy, "Comment," *Sunday Times*, April 19, 2009.
[353] "Transcript of Peter Bacon Hearing," March 4, 2015, 577–578.
[354] Justine McCarthy, "Mahon Tribunal Drags on as Judges Can't Believe the Facts," September 11, 2011; naamawinelake, "Salaries of 168 NAMA Developers Published," *NAMA Wine Lake*, September 25, 2012, https://namawinelake.wordpress.com/2012/09/25/salaries-of-168-nama-developers-published/.
[355] Irish Times, "Flood Lawyers Reveal Payments of £400,000 to Liam Lawlor," *Irish Times*, January 28, 2002, http://www.irishtimes.com/news/flood-lawyers-reveal-payments-of-400-000-to-liam-lawlor-1.411739.
[356] Bertie Ahern, "Transcript of Bertie Ahern Hearing," July 16, 2015, 107.
[357] Mulryan, "Opening Statement to the Inquiry," 18.
[358] Fintan O'Toole, *Ship of Fools*, 2009.
[359] "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," 105.
[360] Carswell, "Opening Statement to the Banking Inquiry," 3–4.

abide by them. When Joe Higgins put this catalogue of banking scandals to Patrick Neary[361], the former CEO of the Financial Regulator basically reiterated his position in his opening statement that 'there was trust and reliance placed on the boards and management of the banks to conduct their affairs prudently and properly'[362]. The following extracts from the Financial Regulator's 2006 *Annual Report* illustrate this approach:

> A principles-led approach to regulation is the right model for Ireland …It both allows and requires financial service providers to manage themselves… We fully expect boards and senior management of all financial service providers operating in Ireland to adopt ethical behaviour and transparency in business dealings as key values. We do not examine each transaction or contract entered into by institutions to test compliance. Neither do we seek to interfere with the design of financial products…[363].
>
> …. We provide world-class service to financial institutions in all our dealings with them. [364].

One of several channels through which this consultative self-regulation operated was the Financial Services Consultative Industry Panel (FSCIP), which had been set up alongside the Financial Regulator under the 2003 Central Bank Act as a sort of watchdog. Section 57DF of the Act obliged the Regulator to consult with industry 'Before making or issuing a policy document or a regulatory document…unless that Authority believes that the document must be made or issued without delay' and it was also obliged to explain itself if it did anything against the banks' 'advice':

> …If the Regulatory Authority declines to give effect to any particular advice provided by the Panel, it shall provide the Panel with a written statement setting out its reasons for declining to give effect to the advice and shall, if the Panel so requires, publish the statement.

In case such 'moral suasion' proved insufficient, the FSCIP had the stick of providing 50% of the Regulator's funding and the statutory right to input into its annual budget. This clause also envisaged a role for the Minster for Finance, who was obliged to consult the banks before approving the state's budget for regulating them: 'The Minister shall consult each Consultative Panel before approving the Regulatory Authority's draft estimate of income and expenditure for a financial year.'

Some extracts from FSCIP's 2005 *Annual Report* give a flavour of the industry-regulator relationship. First from the Chairman's Statement by Former CEO of HSBC Ireland, James Deeny:

> Over-regulation and under-regulation create major inherent issues for any financial services market, and in seeking to achieve the right balance in the Irish market, there is absolutely no conflict between the Financial Regulator and the financial services industry.…Ireland is recognised as a well-regulated jurisdiction, but if regulations are broken, the answer is neither necessarily nor invariably extra regulation[365]

Later on, industry consultation on the Regulator's budget is summarised:

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[361] "Transcript of Neary Hearing," May 28, 2015, 59, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/28052015_Neary_vol1.pdf.
[362] Ibid., 9.
[363] Financial Regulator, "Annual Report of the Financial Regulator 2006," 2007, 12.
[364] Ibid.
[365] FSCIP, "Annual Report 2005," 2006, 20.

The Panel engaged in discussions with the Financial Regulator concerning its budgets for 2005 and 2006, and in accordance with its statutory mandate, responded to the Department of Finance on these budgets. The Panel expressed a number of concerns to the Department about the Financial Regulator's budget process and particularly the transparency of the basis on which the Budget proposals are formulated. Arising from this, it was agreed that commencing with Budget 2007, there would be active engagement by the Financial Regulator with the Panel throughout the entire budget cycle, involving nominated representatives from the Panel. [366]

Former Prudential Director of the Financial Regulator, Con Horan, confirmed that 'The budget and resources applied to supervision…was…an area where the FSICP had significant interest and influence'[367]. In addition, as of 2007, two of the three members of the Regulator's Budget and Remuneration Committee, which made 'recommendations to the Authority on the annual manpower and budgetary requirements of the Authority including levies on industry' were also capitalist representatives: the former Director-General of IBEC, John Dunne, and the former managing director of Standard Life Assurance, Alan Ashe[368] (who had also previously had a senior role in TSB)[369].

In light of all this, it's perhaps unsurprising that the Banking Supervision Department (BSD) was so ludicrously understaffed. Three people were responsible for supervising *both* Anglo and BOI and two to three for AIB and ILP. Bank assets also increased by 200% from 2003-8 while BSD staff increased by only 10%[370]. The predictable result was described by the Head of the BSD, Mary Burke, to Joe Higgins:

> If you are a team of three people and you have two of the major banks in the country and you are trying to supervise them through the worst financial crisis since nineteen twenty whatever, there was only so much those people could do…our ability to follow through, our ability to challenge, our ability to then enforce ... and there's not much point in…making a threat of following through if you know you can't ultimately do that. That was not there…I am crystal clear here. We did not have the resources that were needed to supervise these banks[371].

Burke's comments, along with the neoliberal philosophy of self-regulation, and the general power and political influence of banks, explain the apparent paradox whereby the Financial Regulator identified almost all the main issues in the banks – from excessive expansion of lending, especially to a small number of property developers, to the diminishing of credit standards and poor corporate governance – but did not take any conclusive action[372]. In the end, it was the structural power of

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[366] Ibid., 11.
[367] Con Horan, "Opening Statement to the Banking Inquiry," April 20, 2015, 6.
[368] Financial Regulator, "Annual Report of the Financial Regulator 2007," 2008, 81.The third member was a career civil servant and former board member of FAS, Dermot Quigley.
[369] progressive-economy@tasc, "IFSRA: The Financial Regulator Which Failed," *Progressive-Economy@tasc*, January 2, 2010, http://www.progressive-economy.ie/2010/01/ifsra-financial-regulator-which-failed.html.
[370] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 63–64; Mary Burke, "Opening Statement to the Banking Inquiry," April 29, 2015, 4.
[371] "Transcript of Mary Burke Hearing," May 27, 2015, 82–83.
[372] Nyberg, "Nyberg Report," 63.

finance capital that explains the 'pattern of inconclusive engagement' by the Financial Regulator with the banks identified by Honohan[373] - not the individual failings of men like Patrick Neary, who occupied they positions they did precisely because of their 'deference'[374] to the banks and reluctance to 'interfere'.

In the course of the Inquiry, a number of specific instances also came to light where banking interests clearly influenced policy and legislation in ways that inflated the bubble. The Irish Banking Federation (IBF) is always a very powerful lobby group but in the run-up crash had the added advantage of a President, Pat Farrell, who had formerly been General Secretary of Fianna Fáil and 'was believed to have the ear of the Minister for Finance'. One example was the April 2007 Asset Covered Securities (Amendment) Act. This allowed banks to use their commercial property loans as collateral to borrow even more money on wholesale markets, which could then be lent out again[375]. It 'was passed in the face of some opposition from the regulatory authorities[376] following intensive lobbying by the banks and a private dinner for Brian Cowen at BOI HQ. Its CEO, Brian Goggin [377] afterwards sent Cowen this thank you note:

> This particularly enlightened and innovative piece of legislation is a model for a number of significant stakeholders – political, public and private sectors – working constructively together to produce something that not just achieves its primary aim, but that also works to promote a very positive image of Ireland abroad…
>
> I can honestly say that I find it hard to remember when I have had as enjoyable, insightful and stimulating few hours discussion. You raised a particular interesting issue, indeed challenge, on the question of influencing or at least informing the debate on where and how we take forward this great project that is modern Ireland.[378]

Other examples of industry-friendly decisions made after lobbying by the banks included: the decision not to tax Contracts for Difference, which made Sean Quinn's amassing of a giant secret and destabilising shareholding in Anglo significantly more lucrative[379]; the demutualisation legislation passed in 2006 that incentivised INBS to blow up its balance sheet in anticipation of a trade sale[380]; and the discouragement of the Financial Regulator from proceeding with Directors' Compliance Statements [381]. These would have forced bankers to sign a statement confirming they were fully compliant with proper banking practices and made it easier to hold them personally liable for

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[373] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 9.
[374] Honohan uses this description numerous times in his report.
[375] Carswell, "Opening Statement to the Banking Inquiry," 4–5.
[376] "Transcript of Simon Carswell Hearing," 639; Senator Susan O'Keeffe in "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," 67.
[377] Simon Carswell, "BoI Chief Praised Cowen after Private Dinner," *The Irish Times*, February 12, 2011, http://www.irishtimes.com/business/financial-services/boi-chief-praised-cowen-after-private-dinner-1.570113.
[378] quoted in "Transcript of Simon Carswell Hearing," 644.
[379] Miriam Lord, "Cardiff's Intervention in Taxing Matter Saw His Stock Soar in 2006," *Irish Times*, November 26, 2011.
[380] "Nyberg Report," 24; Carswell, "Opening Statement to the Banking Inquiry," 5–6.
[381] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 50–51; "Transcript of Simon Carswell Hearing," 641; Horan, "Opening Statement to the Banking Inquiry," 3.

malpractice[382] . They were first proposed in by the Regulator in November 2004[383] but weren't in place before the crisis due to what the former Chair of the Financial Regulator, Brian Patterson, described as 'a barrage of resistance from the industry'[384]. According to Honohan, Brian Cowen also personally intervened on the side of the banks, writing to the Regulator that it was important to 'assess the competitiveness issue'[385]. Honohan testified that 'The Minister's letter would have been the end of it' and explained how this reflected 'a policy that the development of the financial sector is important and the Central Bank had to take account of the development of the financial sector.'[386] It also reflected the whole structure of self-regulation by banks and promotion of the industry established by Charlie McCreevy in the 2003 Central Bank Act and Brian Cowen's equally oleaginous approach to the banks. His speech to Financial Services Ireland in March 2006 is a case in point:

> …the work that has been carried out by both the industry - particularly through representative bodies like FSI - and the Financial Regulator in building-up an enhanced regulatory system for financial services in Ireland, will I am sure stand the test of time...A lynchpin of that approach is consultation… Again I would re-iterate how important it is that your industry is represented in the policy making process…[387]

This 'representation in the policy making process' would never prove more important than on the night of the Guarantee.

The Influence of the Property & Construction Sector

In property and construction, the two main examples of the political influence of the sector and its role in crash relate to planning decisions and property-related tax breaks and loopholes. The planning process and corruption was not examined by the Inquiry in any depth, both for legal reasons and because it had already been covered by various Tribunals. On a number of occasions when Joe Higgins tried to raise specific instances of apparent planning irregularities with developer witnesses he was cut off by the Chair, again illustrating the 'chilling effect' of the ludicrous legal constraints under which the Inquiry was operating and the structural power of the small elite wealthy enough to take legal actions against state bodies in the High Court.

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382 "Opening Statement of Liam O'Reilly (Financial Regulator) to the Banking Inquiry," May 14, 2015, 3; Horan, "Opening Statement to the Banking Inquiry," 3.

383 Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 50–51; Con Horan, "Opening Statement to the Banking Inquiry," April 20, 2015, 3.

384 Brian Patterson, "Transcript of Brian Patterson (Financial Regulator) Hearing," June 11, 2015, 62.

385 Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank," 50–51.

386 Patrick Honohan, "Transcript of First Honohan Hearing," January 15, 2015, 123. Cowen initially claimed in his hearing that 'We didn't tell the Regulator what to do' but when pressed further said: 'To be honest and truthful about it, I wouldn't be in a position to recall at this remove what the circumstances were in relation to that matter. But I am assured by [William Beausang, a Department of Finance official he said he had spoken to] that what I'm saying to you is correct.' Cowen's letter was never supplied to the Inquiry even though Cowen said he had checked with the Department before his appearance and been told 'there's a letter on file from me' on this issue. "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," 42.

387 "Address by the Minister for Finance, Mr Brian Cowen TD to Financial Services Ireland on 2 March 2006," March 2, 2006, http://oldwww.finance.gov.ie/viewdoc.asp?DocID=3834.

The subject was therefore only addressed 'in a general way', i.e. without naming names, during the Context Phase of the Inquiry. *Irish Times* environment correspondent during the bubble, Frank McDonald, described how the rezoning process and the political corruption often involved:

> landowners...were frantic to have their land rezoned. Where local area plans were being done for villages in Laois, Monaghan or wherever, this was happening on a widespread basis. Decisions were being made that were totally irrational from a planning point of view, but which satisfied the urge of the landowners in question to make a huge killing on the sale of land for its speculative value as development land.
>
> …development plans were being made at the behest of developers, rather than on the basis of rational planning and what was good for the area or good for the country…the decisions that were being made were so irrational that it seems to me that there was no other explanation, in some cases anyway, except that there was corruption involved. [388]

By the 2000s, all these individual corrupt and merely 'business-friendly' decisions had become a structural factor underpinning the bubble. The prospect and reality of rezoning decisions encouraged land-banking by developers from the 1990s onwards and a huge amount of inappropriate development afterwards. Much of it was in the wrong place and would never have been financially viable without the smorgasbord of property-related tax breaks introduced and extended by successive governments. According to developer, Michael O'Flynn:

> we built a lot of houses in a lot of places where houses weren't needed. We zoned a lot of land, you know, in a lot of places land was...shouldn't have been zoned. We put a lot of infrastructure into land, into local authorities where...to build houses in places where they shouldn't have built houses in the first place…[389]

As well as incentivising useless developments that the state had to pay to service, the main function of these tax breaks was to shelter the income of rich people from tax while inflating property prices. As early as 1999, the Department of Finance advised that "the majority of the beneficiaries…are high-net worth individuals or corporate investors"' and warned of 'The possibility that tax incentives for property development have contributed to the emergence of asset price inflation'[390]. Reports commissioned by the Department of Finance came to the same conclusion. A November 2005 report by Goodbody Economic Consultants made the following finding in relation to the Urban Renewal Scheme, which was one of the biggest:

> The tax benefits of the Scheme have accrued to relatively few higher income individuals. There has also been significant inflation of property prices as a result of the tax incentives and this has benefited a small number of landowners and developers. Thus, the Scheme has had strong negative income distributional effects[391]

[388] "Transcript of Frank McDonald Hearing," March 12, 2015, 787.
[389] "Transcript of Michael O' Flynn Hearing," 138.
[390] quoted in Conor McCabe, *Sins of the Father: Tracing the Decisions That Shaped the Irish Economy*, 2nd ed. (Dublin, Ireland: The History Press, 2013), 54–55.
[391] Goodbody Economic Consultants, "Budget 2006: Review of Tax Schemes Volume II: Goodbody Review of Area-Based Tax Incentive Renewal Schemes," iii.

Likewise, a February 2006 Indecon report found that 'nearly all of the property tax incentives reviewed have been used primarily by high income earners…There is no doubt that the incentives have been a key mechanism for high income earners to reduce their tax liabilities'[392].

Indecon estimated that in total €6.8bn in tax was foregone through various property-related tax breaks from 2005-8[393]. As well as underfunding public services, this made the tax system far more regressive by placing more of the burden of taxation onto ordinary workers without the means to invest in apartment blocks, hotels or car parks.

The ESRI had publicly opposed many of these tax breaks[394] and even the government's property adviser, Peter Bacon, said he had advised Charlie McCreevy to abolish them while he was still Minister for Finance. [395] Yet despite all this, Bertie Ahern testified that he only twigged property-related tax breaks might have fuelled a property bubble in 'about 2009'[396]. Most of them were originally supposed to be abolished in 2002 but instead were repeatedly extended by McCreevy and Cowen, following lobbying from the property and construction industry. Cowen finally announced they would be gradually phased out in December 2005, meaning that as late as 2008, Fianna Fáil and the Greens were still handing out over €450ma year in Section 23-type reliefs on rental property to developers and landlords[397]. Simon Carswell explained in his opening statement why these tax breaks persisted for so long:

> These subsidies were left in place or were only starting to be phased out during the frothiest years of the property bubble as a result of the relations between the property sector and government/elected representatives and aggressive lobbying by commercial interests.[398]

In addition to incentivising property speculation with tax breaks, the government repeatedly cut taxes on property speculation and allowed lucrative loopholes to remain open in the relevant tax codes. Charlie McCreevy's second Budget in 1998 halved Capital Gains Tax on development land from 40% to 20%. This instantly made land speculation much more profitable and rather than reducing the cost of housing went straight into developers' pockets. Stamp duty rates were also repeatedly cut in the late 1990s and into the 2000s. There were also loopholes in the stamp duty code, which allowed developers to avoid paying the 9% rate via licensing/leasing arrangements that meant they never formally assumed ownership of a property. Cowen eventually closed that loophole in 2007, a long time after being told about it, but then didn't implement the law for a further three months after passing it. Another loophole, which was used in the notorious Dublin Docklands Development Authority(DDDA)/Glass Bottle deal, was to purchase property through shares so the investor was only liable for the 1% stamp duty on shares, instead of the 9% stamp duty on property.

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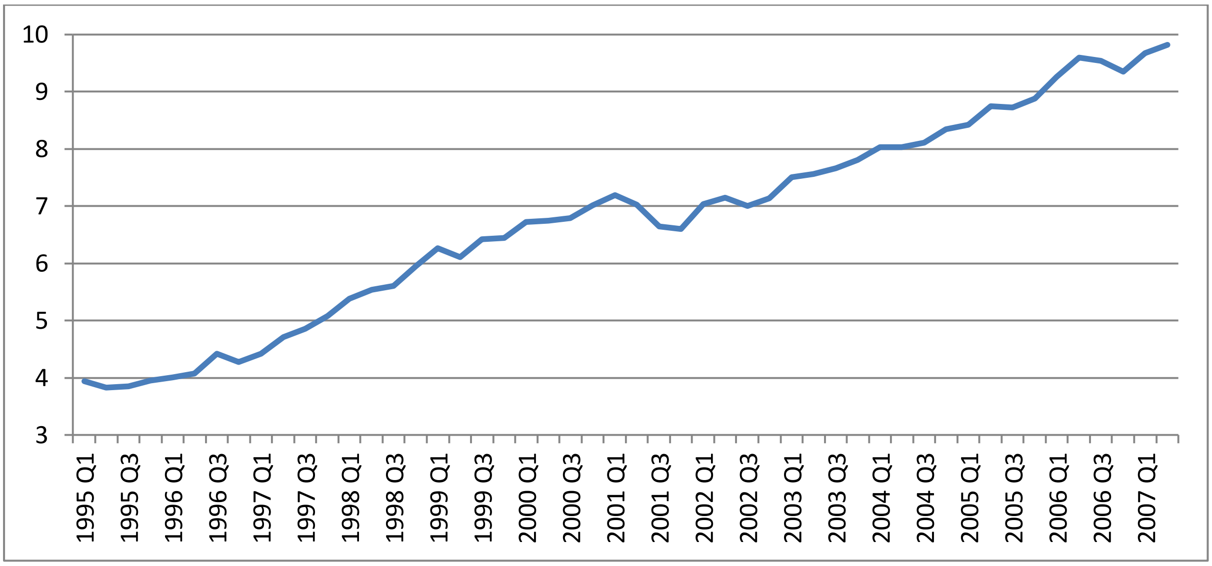
[392] Indecon, "Budget 2006: Review of Tax Schemes - Volume I: Indecon Review of Property-Based Tax Incentive Schemes" (Department of Finance, February 2006), vi, http://www.finance.gov.ie/sites/default/files/Taxreview2006Vol1.pdf.
[393] Indecon, "Budget 2006: Review of Tax Schemes - Volume I: Indecon Review of Property-Based Tax Incentive Schemes."
[394] "John FitzGerald Transcript.pdf," February 11, 2015, 5.
[395] "Transcript of Peter Bacon Hearing," 29.
[396] "Transcript of Bertie Ahern Hearing," 82.
[397] TASC, "Tax Injustice: Following the Tax Trail," 22, accessed June 30, 2014, http://www.tascnet.ie/upload/file/TASC%20Tax%20Injustice.pdf..
[398] Carswell, "Opening Statement to the Banking Inquiry," 4.

All of the above tax decisions prioritised the greed of property speculators over the needs of the majority. They reduced the tax base needed for public services and made the bubble even bigger and the fallout for ordinary people even worse. A more direct example of the same class bias was the decision in 2002, following much industry lobbying, to water down Part V in order to enable developers to avoid their social/affordable housing obligations[399]. The result was that a mere 3,757 social housing units were provided under Part V from 2002-11[400]. If the government had enforced the original legislation, it's estimated an extra 45,000 social housing units would have been built[401] - equivalent to roughly half the current housing list.

Negative Impacts of the Bubble on ordinary people

While the elites were partying and scratching each other's backs, even before it burst the bubble had many negative effects for ordinary people. They included rising house prices, huge mortgages, shoddy construction and fire safety standards, urban sprawl, long distance commuting and growing personal indebtedness, which by 2003 had already doubled to 90% of disposable income from a decade earlier[402]. The average price of a new house more than quadrupled from around €77,000 in 1995 to €332,000 at the peak in 2007 (Figure 3.4). Wages were completely unable to keep pace with this level of profiteering: average house prices leapt from four times average earnings in 1995 to nearly ten times at the peak of the bubble in 2006-7 (Figure 3.8). The 'solution' offered by financialised capitalism was more and more debt.

Figure 3.8 Average New House Prices to Average Annual Earnings 1995-2007[403]



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399 Byrne, "Opening Statement to the Banking Inquiry," 7.
400 DKM Economic Consultants and Brady Shipman Martin, "Review of Part V of the Planning and Development Act, 2000" (Department of the Environment, Community & Local Government, November 27, 2012), 26, http://www.environ.ie/en/Publications/DevelopmentandHousing/Housing/FileDownLoad,33908,en.pdf.
401 Aideen Hayden of housing NGO, Threshold, quoted in Kitty Holland, "Revised Social Housing Plans Described as 'missed Opportunity,'" *Irish Times*, October 2, 2014, http://www.irishtimes.com/news/social-affairs/revised-social-housing-plans-described-as-missed-opportunity-1.1949946.
402 Central Bank calculations, 2004 provided to the Inquiry by Frank Browne.
403 Department of the Environment, Community & Local Governmen, "Housing Statistics: House Prices, Loans and Profile of Borrowers."

100% mortgages were made generally available in 2005[404] and quickly grew from 5% of mortgages in 2004 to 15% in 2006[405] when they accounted for 36% of all first-time buyer mortgages issued and 69% of first time buyers borrowed more than 90% of the cost of their home[406]. Mortgages of more than 30 years also became commonplace, growing from 10% of all mortgages issued in 2004 to 39% in 2008 and reaching 48% in Dublin[407]. This was Ireland's version of subprime – an attempt to plug the gap between wages and house prices until the chasm between two finally became unbridgeable and the whole edifice collapsed. The financial exploitation of workers by banks and developers this involved was one of the factors in the crash both in Ireland and internationally but in Ireland the mechanism at work wasn't owner-occupiers defaulting on their mortgages. What happened was that wages were outpaced by consumer price inflation, due to developers and bankers profiteering on land and property prices and bosses generally taking an ever greater slice of their workers' pie in the form of profits. Developer, Michael O'Flynn, alluded to the role of price gouging in the property crash, saying:

> We were…in a way, we were pricing ourselves out of business because of the scale of price increases. That did worry us…when the average couple can't buy a house, you know, you know something is going wrong with your business model…there was probably a time in the 2000s when we should all have packed our bags, really, because of the price escalation of land[408].

He even went so far as to claim – obviously with the benefit of hindsight as developers or bankers were hardly complaining at the time – that:

> it was not in our interest to have house prices escalating to the extent they were, making super profits that we were putting back into the raw material, we were buying for new land. That is not a business model that can survive, okay? [409].

This admission is interesting as it demonstrates how what's profit for one capitalist is a cost for another and how profiteering can lead to crises by driving up living costs to unsustainable levels and then collapsing markets. The same mechanism applied in the commercial property market. Wages and consumer demand could not keep up with ever-expanding shopping centres and hotels, even with expanding amounts of consumer credit, especially when commercial rents and consumer prices were spiralling out of control. TV programmes like *Rip Off Republic* were popular at the time because they spoke to the incessant profiteering in all spheres of life by big business. The Global Financial Crisis intervened before this unsustainable situation caused the crash all by itself, but in this regard the credit crunch was only the catalyst that revealed the greater structural problem underneath.

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404 "Transcript of Cormac McCarthy (Ulster Bank) Hearing," May 6, 2015, 22–23.

405 Ranges of Loans to Value - National & Dublin Department of the Environment, Community & Local Governmen, "Housing Statistics: House Prices, Loans and Profile of Borrowers."

406 Department of the Environment, Heritage & Local Governmen, "Annual Housing Statistics Bulletin 2006," 2007, 19, http://www.environ.ie/en/DevelopmentHousing/PublicationsDocuments/FileDownLoad,14648,en.pdf.

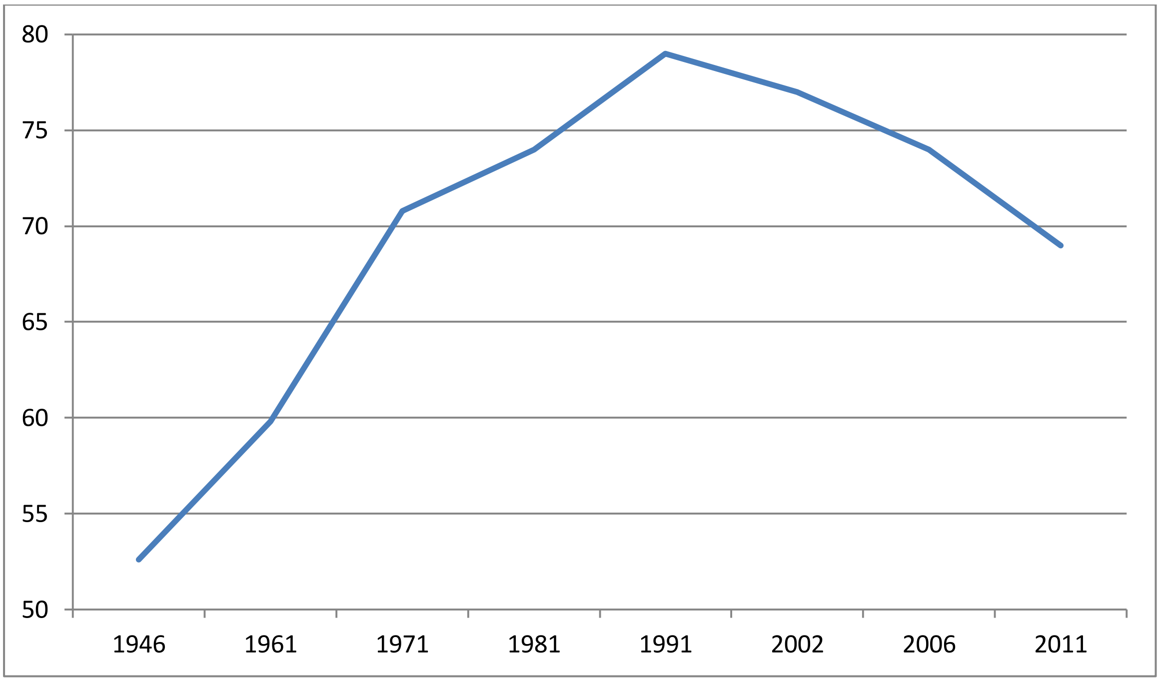
407 Department of the Environment, Community & Local Governmen, "Housing Statistics: House Prices, Loans and Profile of Borrowers."

408 "Transcript of Michael O' Flynn Hearing," 137.

409 Ibid., 138.

There was also a large section of Irish society that never benefited from the boom. The numbers forced to rent from private landlords significantly increased due to the privatisation of council housing: whether through the failed reliance on developers to supply it via Part V, or using private landlords to provide so-called 'social housing' in the private rented sector. For all the propaganda about a supposed Irish 'property-owning gene', home/mortgage ownership has been falling sharply since the 1990s, declining from 79% in 1991 to 69% in 2011 as workers were priced out by the bubble and impoverished by the crash (Figure 3.9). By 2006, home ownership was already below the EU average[410]. The last Census in 2011 found 19% of households (approximately 770,000 people) were renting from private landlords[411]. Around a third receive some form of rent subsidy from the state (such as Rent Supplement or HAP). Contrary to common perception, by 2011 Ireland had one of the highest percentages of people living in private rented accommodation in Europe[412]. That number has risen significantly since and is the section of society worst affected by the current housing crisis – whose origins lie in the 2008 property crash.

Figure 3.9 Percentage of Households Owning or Buying Their Home, 1946-2011



(based on Census data)

Many of the benefits that did accrue to working people during the boom were only temporary and were immediately reversed once the crash hit. In light of this, Bertie Ahern's efforts to paint himself as the hero of the boom who had solved all of Ireland's economic problems sounded like a bad joke. In his opening statement, Ahern said:

410 McCabe, *Sins of the Father*, 57.
411 DKM Economic Consultants, "Rent Stability in the Private Rented Sector: Final Report, Prepared for The Housing Agency on Behalf of the Private Residential Tenancies Board" (PRTB, September 2014), 4.
412 CSO, "Census 2011 Profile 4 The Roof over Our Heads - Housing in Ireland," html,text,pdf,xls, (August 2012), http://www.cso.ie/en/census/census2011reports/census2011profile4theroofoverourheads-housinginireland/; Eurostat, "Housing Statistics," March 2014, http://epp.eurostat.ec.europa.eu/statistics_explained/index.php/Housing_statistics.

> The main economic problems facing Ireland in the mid-1990s were high unemployment, net emigration, relatively low incomes and the need for increased productivity. A decade later these problems were substantially solved...when I first came into this House in 1977 and for right through the 1980s, our national debt was an unsustainable millstone around the neck of taxpayers. It was a barrier to national progress as huge sums of revenue had to service interest payments. In 1997, the year I became Taoiseach, 20 per cent of all taxes raised in the State were used to service the National Debt.

In 2014, €41bn was raised in taxes and €8.2bn spent on debt service so '20 per cent of all taxes raised in the State were [again] used to service the National Debt'! [413]. How this debt came to be placed on the shoulders of ordinary people is discussed next.

[413] Department of Finance, "Exchequer Statement End Dec 2014," January 5, 2015, http://www.finance.gov.ie/sites/default/files/Exchequer%20Statement%20end%20Dec%202014.pdf.

Chapter 4 - The 'Soft Landing' to the Crash

Three related myths have emerged about the period immediately before the crash. The first, examined in this chapter, is that 'nobody saw it coming' because everyone genuinely believed there would be a 'soft landing'. The second is that the government thought the banks only had 'liquidity' issues, in other words that they were only unable to fund themselves because of the global credit crunch and not because all the bad commercial property loans they had made to developers meant they were facing 'insolvency'. The third is that the Guarantee was a 'panic decision' on the night of September 29th 2008. As with all myths, none of them are true, and as with many, they serve a political purpose. Their function is to absolve Irish elites from responsibility by portraying the crash as a random 'one in a hundred year'[414] event, a natural disaster like a hurricane or earthquake that struck Ireland out of nowhere rather than a predictable crisis of Irish and global capitalism.

In reality, there were clear signs of an impending collapse from 2005 at the latest and plenty of evidence for the authorities to be concerned. Property speculators were aware on some level of an oncoming crash but blinded by the huge profits they were making, most didn't 'get out in time' and were left with their hands stuck in a rotting cookie jar. As the Central Bank's Chief Economist, Tom O'Connell, told the Inquiry, 'It is not credible that those who ought to have been aware of what was happening were in the dark. One can only surmise that…too many people were benefiting from the boom-time for prudent, avoidance measures to have been taken.'[415] Rather than the authorities taking any meaningful action, an elite consensus was instead constructed around the fairy-tale of a 'soft landing', including by a compliant media dependent on property advertising. This encouraged first-time buyers to keep taking out huge mortgages and helped keep the bubble going for bankers and developers until the last possible minute. As media expert, Harry Browne, told the Inquiry, editors would reject articles critical of the bubble 'because of the overwhelming consensus among Irish elites in 2006 and 2007 - probably in some sense a stronger consensus in that period when things looked like they might be a little bit shaky - that we need to hold the line and not talk down the economy.'[416]

The Tipping Point in 2005

There was a general consensus among the expert witnesses that 2005 was the tipping point of the bubble and the last year intervention could have made a significant difference to the severity of the crash[417]. In Chapter 2, the direct causes of the crisis were identified as the banks' massive expansion of lending (Figure 2.1), especially of high risk commercial property loans to property speculators (Figures 2.3), facilitated by undermining credit standards and cutting costs (Figure 2.15) – or as Bill Black put it, 'Grow Like Crazy!', 'Make Terrible Quality Loans' and 'Use Pathetic Underwriting'. This was driven by the banks' singular purpose of maintaining huge profits (Figure 2.13) and executive pay (Figure 2.10) in a context of increased competition that had reduced profit margins (Figure 2.12). Meanwhile, an underlying crisis of over-accumulation and consumer affordability caused by rising

414 Eugene Sheehy in "Transcript of Eugene Sheehy and Michael Buckley (AIB) Hearing," April 29, 2015, 8.
415 Tom O'Connell, "Opening Statement of Tom O'Connell," May 13, 2015, 8.
416 "Transcript of Harry Browne Hearing," March 25, 2015, 858.
417 Philip Lane, "Transcript of Philip Lane Hearing," January 21, 2015, 212; Alan Ahearne, "Transcript of 1st Alan Ahearne Hearing," March 4, 2015, 622; Gregory Connor, "Oral Testimony to the Banking Inquiry," February 25, 2015, 464; Rob Wright, "Transcript of Rob Wright Hearing," December 18, 2014, 70; Peter Nyberg, "Misjuding Risk - Causes of the Systemic Banking Crisis in Ireland: Report of the Commission of Investigation into the Banking Sector In Ireland," March 2011, 60–61.

inequality, in Ireland and globally, would have caused a crash anyway, even without the global 'credit crunch'[418]. Wages and house prices had already lost all correlation, as average new house prices increased from €77,000 in 1995 to €287,000 in 2005 and the ratio of wages to house prices more than doubled from 3.94 to 8.88 times average earnings (Figures 3.4 & 3.8). Finally, the Irish banks' dependence on foreign capital via the wholesale money markets to finance the bubble made Ireland particularly vulnerable to the Global Financial Crisis (Figures 1.6 & 1.5). All these dynamics were measurable and had converged by 2005, which was the peak year of lending growth for several banks, including AIB, and the second fastest for Anglo and BOI (Figure 2.2). Crucially, it was also the year commercial property lending got completely out of control (Table 2.1). Having more than doubled in two years to €75bn, it doubled again by 2008 (Figure 2.3).

With all this going on, at least some property market interests were wary of a downturn. John Moran of commercial property estate agents, Jones Lang La Salle, told Joe Higgins that 'we turned around to our client base at the end of 2005 and said, "We cannot see that these type of returns are sustainable in the longer term. If you want to take a profit perhaps you should think of exiting now".[419] Moran explained that 'Irish yields tightened significantly between 2003 and 2006, compressing from 6.00% to 3.70% for prime offices for example'[420]. In other words, the rate of profit for property speculators had fallen significantly. Under questioning from Joe Higgins, he elaborated that this 'caused…Irish capital to fly out of the country to seek better returns elsewhere'[421]. Already at the end of 2004[422], Irish investors had spent over €3bn on property abroad and the *Irish Independent* reported that 'the domestic commercial property investment spend now stands at a mere 20% of the overall total'. By September 2005, Irish investors 'owned' 18% of London offices[423] and in 2006 they invested a further €3.5bn in the UK and €2bn in Europe and the US[424]. The *Irish Independent* noted that 'The extraordinary Irish charge on the UK scene would never have been possible without the enthusiastic support of the Irish banks, who have become expert at facilitating complicated property deals involving syndicates of investors'.[425] Of the big developers, over €2bn of Mulryan's €2.4bn in bank debt was for UK property[426]; while as early as April 2006, nearly two-thirds of Quinlan Private's assets were overseas[427]. Michael O'Flynn[428] and Peter Cosgrave[429] also had 40-

[418] Patrick Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008," May 31, 2010, 6–7.
[419] "Transcript of John Moran, Jones Lang LaSalle, Hearing," April 2, 2015, 1029.
[420] John Moran, "Opening Statement to the Banking Inquiry: Issues Relating to the Nature and Functioning of the Commercial Real Estate Market in the Period prior to 2008 in the Context of the Banking Crisis in Ireland," April 2, 2015, 6.
[421] "Transcript of John Moran, Jones Lang LaSalle, Hearing," 1029.
[422] Con Power, "Feel-Good Factor Is Set to Build in 2005," *Irish Independent*, 2004, sec. Midweek Property.
[423] Irish Independent, "Irish Own 18% of London Offices," *Irish Independent*, September 28, 2005, sec. Commercial Property.
[424] Moran, "Opening Statement to the Banking Inquiry: Issues Relating to the Nature and Functioning of the Commercial Real Estate Market in the Period prior to 2008 in the Context of the Banking Crisis in Ireland," 6.
[425] Power, "Feel-Good Factor Is Set to Build in 2005."
[426] Sean Mulryan, "Opening Statement to the Inquiry," July 22, 2015, 12.
[427] Derek Quinlan, "Opening Statement to the Banking Inquiry," July 9, 2015, 3.
[428] Michael O'Flynn, "SECTION 1 APPENDICES TO THE STATEMENT OF MICHAEL O` FLYNN 30.6.15.pdf," June 30, 2015, 12.
[429] Peter Cosgrave, "Written Statement of Peter-Cosgrave," August 2015, 4.

50% of their property outside of Ireland by September 2008.[430]. This would suggest some awareness the Irish property market was going to fall, or maybe it just wasn't profitable enough anymore.

Anglo's head of Irish lending from 2005-7, Tom Browne, was also worried about the Irish commercial property market. He confirmed to the Inquiry that 'As far back as early 2005' he had told journalist, Matt Cooper, 'that it had become dangerously overheated' and that he had been 'trying to reduce the over-exposure to the Irish property market at that time in the bank''[431]. He explained that 'the first attempt'[432] to rein in lending at Anglo was a board decision 'In early 2006' to halt development lending to new customers. However, he admitted 'the policy itself was seriously flawed' because it allowed new lending to existing clients and also that it should have been 'more forcibly' implemented[433]. This is a huge understatement given Anglo's top 50 clients made up two-thirds of its Irish development lending so 'limiting' new lending to them was meaningless[434]. The result was that Anglo's Irish development lending actually *increased* by 50% from April 2006-April 2007[435], while its overall Irish lending grew 44%. These half-hearted efforts nonetheless indicate concerns at the highest levels in Anglo that the property market was turning from 2005-6. The only plausible explanation why lending was massively expanded anyway is the massive profits the bank, its developer clients and top management were making. As Professor Ed Kane, a renowned expert on banking crises, explained: 'The issue is: when will the party end? A person can recognise that the party has to end badly and still feel it is not ready to end and that they can make some money.'[436] The same happened at AIB and BOI, which increased their commercial property loans by €59bn from 2004-7 (Figure 2.4). Nyberg highlighted this, observing that they both 'continued to lend into the more speculative parts of the property market well into 2008, even though demand for residential property (a major end-user) had begun to decline by the end of 2006.'[437]

The authorities ignore the bubble

Unlike with the banks, direct involvement in profit-making was not a motive for ignoring the bubble on the part the Central Bank and Financial Regulator. Nyberg concluded that 'vigilant authorities should have been much more concerned by the end of 2005'[438], given the Financial Regulator 'had full access to any banking information it required, including regular prudential returns which

[430] The information provided by other big developers showed that the vast majority of their debts were in Ireland, although Bernard McNamara and John Ronan provided no meaningful information on most of their holdings. McNamara claimed not to have kept any documents that would allow him to provide this information. Bernard McNamara, "Written Statement of Bernard McNamara," October 2015, https://inquiries.oireachtas.local/banking/participant/BMN/EvidenceDocuments/BMN01B01/Bernard%20McNamara%20Witness%20Statement.pdf. Ronan gave no information about his largest property company, Treasury Holdings John Ronan, "Written Statement of John Ronan," September 2015.

[431] "Transcript of Tom Browne (Anglo) Hearing," September 9, 2015, 191. Browne was inconsistent on this point, claiming elsewhere in the same hearing that 'You would have been very comfortable…up to 2006 in terms of where you were at in terms of the overall exposure' but 'we could see from early 2006 that the market was getting seriously overheated'. Ibid., 165; 148.

[432] "Transcript of Tom Browne (Anglo) Hearing," 191.

[433] Ibid., 143.

[434] Anglo Irish Bank, "Lending Ireland Development Report as at 30 April 2007," April 30, 2007.

[435] cited in "Transcript of Tom Browne (Anglo) Hearing," 149.

[436] "Transcript of Ed Kane Hearing," January 28, 2015, 247.

[437] Nyberg, "Nyberg Report," 35–36.

[438] Ibid., 60.

included detailed financial information on individual institutions'[439]. Moreover, in June 2004, the Central Bank's head of Financial Stability, Frank Browne, warned the joint Central Bank-Financial Regulator Financial Stability Committee that 'The IMF, in its Global Assessment, notes that never has an increase in residential property prices occurred of a scale similar to that which has already occurred in Ireland over the last decade without a subsequent steep fall in prices'[440].

However, as previous explained, the Central Bank and Financial Regulator were discouraged from taking forceful action due to the economic power and political influence of the banks and the accommodating attitude towards them of government politicians. This was reflected in the general 'trust' of the banks to regulate themselves, which was designed to help attract foreign investment and help Irish banks 'compete' i.e. race to the bottom against foreign banks. This explains why the Financial Regulator identified almost all the main problems in the banks but either took no enforcement action or left it far too little, too late. As Nyberg: pointed out

> inspection reports on Anglo…correctly identified a number of more important problems in the bank at the time. However, there is no indication that these internal reports led to either a reconsideration of supervisory practices or serious consideration of regulatory action.[441]

Perhaps the most extreme example was the Regulator's interaction with INBS. It had been writing to INBS highlighting the riskiness of its exponential expansion of commercial property lending since at least 2004, when following a review by KPMG, it increased its minimum capital requirements by 1%, lowered its exposure limits for development land and prohibited it from entering into any more joint ventures with developers. However, INBS was so unperturbed that it actually accelerated its commercial lending – more than doubling it from €3.5bn in 2005 to €7.4bn in 2007 (Figure 2.4). The Regulator's only response was to write more letters and order another external review, by Deloitte, which again was an indication that it lacked the resources to tackle the situation itself. By 2008, it was still raising all the same issues it had in 2004 – as it pointed out itself in a letter to INBS.

The other main state agency tasked with ensuring financial stability[442] was the Central Bank. One of its main jobs was to publish an annual *Financial Stability Report* (FSR)[443], which was supposed to assess the overall financial stability of the economy and warn of possible risks. Honohan told the Inquiry that 'In terms of the analysis of systemic risks, the language of successive published financial stability reports was too reassuring, representing a triumph of hope over reality'[444] and in his report he said that 'the relatively sanguine conclusions tended to be reached on a selective reading of the evidence.'[445] The Central Bank's Chief Economist, Tom O'Connell also gave evidence that like Tony

[439] Ibid., 60–61.
[440] documents provided to the Inquiry by Frank Browne. The Financial Stability Committee was made up of senior staff including at the time Liam O'Reilly, Patrick Neary and Con Horan.
[441] Nyberg, "Nyberg Report," 63.
[442] CBFSAI and IFSRA, "MEMORANDUM OF UNDERSTANDING ON FINANCIAL STABILITY BETWEEN THE GOVERNOR AND BOARD OF THE CENTRAL BANK AND FINANCIAL SERVICES AUTHORITY OF IRELAND (CBFSAI) AND THE IRISH FINANCIAL SERVICES REGULATORY AUTHORITY (IFSRA)," 2003.
[443] Nyberg told the Inquiry that 'the Central Bank and the Financial Regulator 'were both formally responsible for the financial stability report…but in practice it was virtually only the Central Bank that contributed to that' "Transcript of Peter Nyberg Hearing," December 17, 2014, 15. This was confirmed by Tom O'Connell "Transcript of Tom O'Connell Hearing," June 10, 2015, 88..
[444] "Transcript of First Honohan Hearing," January 15, 2015, 101.
[445] Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008," 20.

Blair's 'dodgy dossier' in reverse, the *Financial Stability Reports* were deliberately 'de-sexed'. As he put it, 'The main body of the FSRs set out extensively how almost all indicators were pointing massively in the wrong direction. By contrast, the overall assessment and tone which reflected the views of the two Boards tended to be reassuring – talking of a soft landing'[446]. According to Frank Browne:

> The risks and vulnerabilities from emerging imbalances in the financial system were identified clearly by those conducting research and analysis and were presented to senior management at the Financial Stability Committee. However, they were toned down or even ignored completely by the senior management of the CBFSAI. [447]

Browne also alleged that 'senior management thought that it was more important to incorporate the views of the industry (who would invariably be offering only self-serving views…than it was to tap into the thinking of its own economist staff on the systemic risks to the domestic financial system.' [448]. This indicates once again the influence of the banks over the Central Bank and Financial Regulator and the deferential attitude towards them.

A particularly important failing of the *Financial Stability Report*s was that they failed to analyse the ramifications of the banks' growing specialisation in commercial property lending, which had increased by 265% from 2003-6 (Figure 2.3). Regling and Watson were critical that:

> Supervisors did not focus strongly on the extent of the possible, and really rather likely, swing in commercial property values, when the economy would slow down after a period of high consumption and overbuilding. It is hard to view the eventual impact of this on the capital of certain institutions as an exceptional or unforeseeable event[449].

This failing was admitted by O'Connell, who acknowledged that 'if you look at the banking crashes in most countries - Japan, Sweden, Finland and so on - it's commercial property that brings people down'. [450] The 2006 *Financial Stability Report* was the first to deal with commercial property at all, in the article mentioned in Chapter 3, which argued that 'the rates of increases in prices across different segments of the Irish property market have tended to trend upwards and downwards in a broadly similar fashion over the last thirty years, particularly during those periods of relatively slower economic growth' (Figure 3.6)[451]. However, in keeping with the Bank's characteristic burying of bad news, its findings were not incorporated into the Overall Assessment or Executive Summary.

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446 "Transcript of Tom O'Connell Hearing," 78.
447 Frank Browne, "Witness Statement of Frank Browne," November 2015, 20.
448 "25032015_Browne_vol1.pdf," March 25, 2015, 44–45.
449 Klaus Regling and Maxwell Watson, "A Preliminary Report on the Sources of Ireland's Banking Crisis," 2010, 40, http://www.betterregulation.com/external/A%20Preliminary%20Report%20on%20The%20Sources%20of%20Irelands%20Banking%20Crisis.pdf.
450 O'Connell, "Transcript of Tom O'Connell Hearing," 98.
451 Abstract - Alan Kearns and Maria Woods, "The Concentration in Property-Related Lending — a Financial Stability Perspective," in *Financial Stability Report 2006* (Central Bank, 2006), 133–44, http://www.centralbank.ie/publications/Documents/Part%201%20-%20Financial%20Stability%20Report%202006.pdf.

Also, the final draft contained what was described in board minutes as a "more circumspect conclusion" than the original[452]. Browne explained:

> This had the effect of qualifying extensively and weakening much of the previous conclusions which would have justified serious concerns that banks specialising in either residential or commercial property sectors would likely face falling prices across many of their respective sub-segments[453]

'Don't frighten the horses' → 'Pray to the Confidence Fairy'

The principal rationale offered by all Central Bank witnesses for not warning the public about the dangers of a crash was that the Bank was afraid of causing one by talking about it[454]. Even in his response to the Inquiry's report, Central Bank Governor, John Hurley, maintained:

> what's a Central Bank to do in that situation, particularly, where it has an interest in a gradual or soft landing, and it would like overvaluation to dissipate in an orderly way. What it doesn't do- and I think someone else has said before this Committee - it doesn't frighten the horses.

Even self-styled Cassandras like O'Connell agreed:

> even though...nearly all the indicators were pointing in a very bad direction…a central bank…could never conclude other than that "things are manageable." If they said, "The banks are going to fall over", you'd have a run on the banks massively...If the analysis proved to be negative, a central bank had to sort of put a positive gloss on things rather than frightening the horses.[455].

Likewise, according to David Begg, who was head of the Irish Congress of Trade Unions (ICTU) from 2001-2010 and had sat on the Central Bank board since 1995, 'what the bank was trying to do was to manage the situation down into what would be hopefully a soft landing, which, of course, might have happened had the international circumstances not arisen'[456].

In other words, the public were told there was going to be a 'soft landing' in order to protect the system (and everything would have been ok if it wasn't for Lehman brothers). As AIB economist, John Beggs explained:

> what all property has in common...whether you do residential or commercial or whatever, it has expectations of confidence as a...as a cornerstone of it all, so if that falters at a national level, all of these components or this diversification, just folds into one ...one bucket of... of risk. [457]

This points to the structural imperative created by the pro-cyclical, boom/bust nature of capitalism to downplay how bad things are during downturns because admitting the truth will cause a loss of

[452] quoted in "Witness Statement of Frank Browne," 38.
[453] Ibid.
[454] David Begg and John Dunne, "Transcript of David Begg & John Dunne Hearing," July 22, 2015, 29; 33.
[455] "Transcript of Tom O'Connell Hearing," 83.
[456] "Transcript of David Begg & John Dunne Hearing," 33.
[457] "Transcript of Bank Economists Hearing," May 7, 2015, 84.

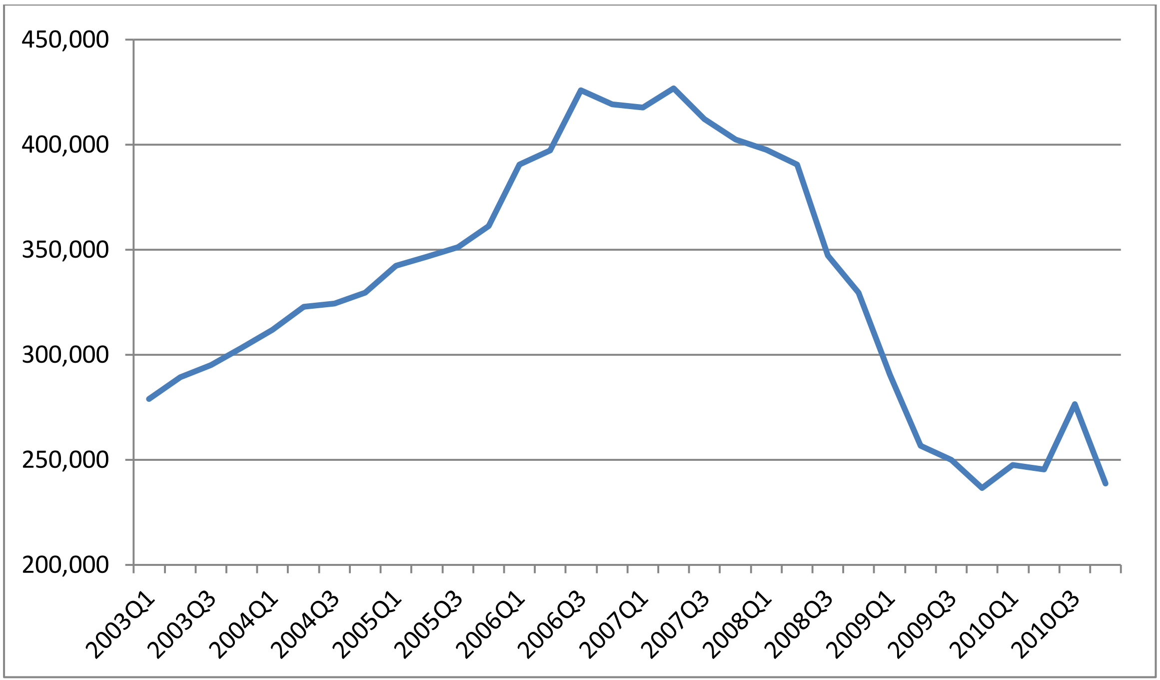
‘confidence’, spread ‘contagion’ and undermine profits. This profoundly undemocratic aspect of the capitalist economic cycle is treated as the natural order of things, no more avoidable than the weather. Like ancient peoples who prayed for the coming of the rains or the ending of the floods, or Catholics who prayed to the saints to intercede with God on their behalf, today we must pray that the ‘confidence fairy’ brings joy to the Gods of the markets.

At the same time as O’Connell argued, ‘people in the know were clear that things were problematic’ and that unlike the general public (or seemingly the media), they would have been able to ‘read between the lines’ of the comforting noises made by the Central Bank[458]. While O’Connell and Browne as employees of the Central Bank may have been afraid to speak out publicly, this should not have been an issue for Begg, who as head of ICTU should have been representing the interests of workers. However, despite telling Joe Higgins that ‘I always try to operate in the interest of working people’, he said ‘I did not see myself, nor was I, a representative of the trade union movement on the board.’[459] When asked if he ever considered resigning from the Board in protest, he answered, ‘it’s something I don’t generally do’, ‘It is much better to stay engaged and to try to influence in whatever degree you can’[460]. So Begg sat on the board throughout the crisis, the Guarantee, and the bailout.

Following the lead of the Central Bank, the bankers and the developers, the government also kept talking up the property market. In an address to a Real Estate Alliance Conference in April 2006 (which was ironically entitled “Everyone sees 20:20 with hindsight, we find foresight works better), Cowen told the assembled property industry interests: ‘There is currently a consensus amongst experts and analysts (domestic, IMF and OECD) that the most likely outcome for the housing market is a “soft landing”[461]’. Within six months, Dublin house prices had started to fall and would ultimately collapse by 44% (Figure 4.1). Yet as late as July 2007, Taoiseach Bertie Ahern derided property market sceptics as ‘merchants of doom’[462] and gave a famous speech in which he said ‘Sitting on the sidelines, cribbing and moaning is a lost opportunity. I don't know how people who engage in that don't commit suicide.’[463]

[458] O’Connell, “Transcript of Tom O’Connell Hearing,” 92–93.
[459] Begg in “Transcript of David Begg & John Dunne Hearing,” 25.
[460] Ibid., 28.
[461] Sunday Independent, “The Bombastic Speech That Must Haunt Cowen,” *Independent.ie*, April 22, 2012, http://www.independent.ie/opinion/analysis/the-bombastic-speech-that-must-haunt-cowen-26845566.html.
[462] Jody Corcoran, “Taoiseach Turns on ‘Prophets of Doom,’” *Sunday Independent*, July 1, 2007.
[463] quoted in Irish Independent, “Dr Ahern and Mr Hyde,” *Irish Independent*, July 5, 2007, sec. Editorial.

Figure 4.1 Average New House Prices Dublin 2003-2009[464]



The Media

Significantly, much of the media was right behind Ahern and the banks in rounding on anyone who dared to 'talk down the economy'. An example was the *Irish Independent's* editorial on Ahern's 'suicide' speech:

> The thrust of the Taoiseach's message was lost in the furore over his "suicide" gaffe. In a wide-ranging address the Taoiseach touched on many important matters, notably the reminder that Ireland has every reason to be confident about the economy. It was when he departed from his script to emphasise the danger and futility of "talking down" the economy that he made his slip.[465]

Much like the rest of the economy, the media had become financially dependent on the property industry during the bubble, with glossy property supplements in the newspapers and 'property porn' programming on RTE. The *Irish Times* told Joe Higgins that its revenue from property advertising had increased along with the bubble, from €10m in 2002 to €22m in 2006, when it reached 17% of its overall income[466]. The comparable figure at Independent News & Media was 9%, with property revenues increasing 89% from 2002-2007.[467] Both of the two main newspapers also bought property websites[468]; the *Irish Times* famously paid €40m for myhome.ie in 2006. This gave them an

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[464] Department of the Environment, Community & Local Government, "Housing Statistics: House Prices, Loans and Profile of Borrowers," July 7, 2014.
[465] Irish Independent, "Dr Ahern and Mr Hyde."
[466] "Transcript of Geraldine Kennedy and Maeve Donovan (Irish Times) Hearing," March 26, 2015, 956–957.
[467] "Transcript of Michael Doorly & Gerry O'Regan (INM) Hearing," March 26, 2015, 904, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/03/26032015_Doorly_vol1.pdf.
[468] Ibid., 910.

additional, direct investment in the performance of the property market[469]. Media expert, Harry Browne, linked this increasing media dependence media on advertising to wider processes of' neoliberalization' and 'an inscription of an unquestioning pro-business ideology, in practice, onto increasingly large advertising-heavy portions of the newspaper - indeed, sections that owed their existence precisely to advertising[470]. Likewise, Dr. Julien Mercille explained how:

> This affects news content because corporate advertisers tend not to subsidise television programmes or news stories that seriously question or attack their own business or the political economic system of which they are part, which would be directly contrary to their interests. [471]

This may help to explain why a mere 78 out over 40,000 *Irish Times* articles on the Irish economy from 2000-7 directly referred even to the possibility of a bubble[472] – which before the crash was almost always referred to positively as a 'boom'.

At the same time, the media often appeared to be doing all it could to inflate that invisible bubble. Although the former editor of the *Irish Independent*, Gerry O'Regan, claimed that 'there was no conscious attempt on my part, or on the part of the newspaper, to fuel what has been described as the property boom'[473], *Independent* newspapers in fact sponsored the *Irish Property Awards* every year until 2008. The 2004 ceremony was described in its pages as 'A glittering showcase of the cream of Ireland's property and development industries…attended by a record 1,000 property professionals with several hundred disappointed'. According to the *Irish Independent's* property editor:

> tributes were paid to the outstanding skills and performance of the individuals and firms involved. The winning projects and services provided by our outstanding agencies ably demonstrated the progress and innovation of this sector, which matches, if not surpasses, the high standards globally…The relaxed black tie event was a welcome respite for an industry that has worked to full capacity in recent years...

In 2007, 'Irish property deal of the year 'was awarded to the Irish Glass Bottle site, which ended up costing taxpayers hundreds of millions of euro, while five of the seven award-winning developers were among the top ten debtors to Anglo[474].

The *Property Awards* reflected the INM's generally obsequious coverage of developers, who were celebrated as Gods with the 'Midas' touch[475] and credited with restoring Ireland's national honour after its colonial past. Rather than signalling that the commercial property market here was 'overheated'[476], the fact Irish investors were spending twice as much in the UK as here was lauded as evidence of the growing prowess of Irish capitalists, who were finally taking their rightful place

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[469] "Transcript of Geraldine Kennedy and Maeve Donovan (Irish Times) Hearing," 960–961.
[470] Browne, "Transcript of Harry Browne Hearing," 842.
[471] Julien Mercille, "Opening Statement of Julien Mercille," March 26, 2015, 2.
[472] Ibid., 5.
[473] "Transcript of Michael Doorly & Gerry O'Regan (INM) Hearing," 902.
[474] Joe Higgins cited in: Ibid., 921–922.
[475] Derek Quinlan, "High Rollers Back Quinlan Private's Midas Touch for Daring €1bn Property Deals," April 8, 2004; Martin Fitzpatrick, "Newcomers to the Financial Bigwig List," *Sunday Independent*, November 6, 2005.
[476] Moran, "Transcript of John Moran, Jones Lang LaSalle, Hearing," 1038.

among the ruling classes of Europe. Headlines like 'How the Irish colonised a British property empire'[477] were commonplace as Irish developers buying UK property was portrayed as payback for centuries of national humiliation by the Brits. A few extracts give a flavour here:

> The citadels of the Empire are falling into the hands of the savages…Her Majesty's former subjects from across the Irish Sea are storming the bastions. The names of the new landlords going up over the doors are Quinlan and McManus and Quinn and O'Reilly and Mulryan. A reverse takeover of the old colonist is under way…The €2.5bn spent in Britain last year by Irish people was 2.7 times greater that the €900m spent in the Irish market[478]

> Irish property is now top of the world, with the feel-good factor set to fuel further expansion through 2005 and (hopefully) beyond. A new generation of aggressive local investors has made a dramatic impact on global commercial property - right up there among the international high rollers…The great overseas "buyaspora" has turned conventional patterns upside down - and a brave new world has dawned…[479]

> one wonders how long this dramatic advance of the Irish entrepreneurial classes in Britain will have to continue before it ceases, in our minds, to be counter- colonisation and is considered "business as normal". Once that happens, we can consider the Irish Question to be well and truly solved.[480]

This sort of coverage was consistent with Dr. Mercille's argument that 'news organisations largely convey the views of political and economic elites'[481].

In portraying property as a one-way bet, the media also played a significant yet intangible role in encouraging people to keep taking out huge mortgages just to put a roof over their heads and keep the bubble going. House prices had gotten more unaffordable every year since the mid-1990s so it was not unreasonable to worry the same would happen in the future (Figures 3.4 & 3.8) – unless you were someone with expertise in the property market as journalists and presenters of TV property programmes presumably were. Some of the worst advice was dispensed by RTE TV presenters, like John McGuire of *I'm an Adult, Get Me Out of Here,* who in May 2007 'advised first-time buyers to go for it before the election', predicting that 'it will be four or five weeks before momentum returns in the property market again' and that 'the best bargains will be happening now'[482] . McGuire was the managing director of a property finance company, whose mortgage brokers business subsequently

[477] Tom McEnaney, "How the Irish Colonised a British Property Empire," *Irish Independent*, April 23, 2005, sec. Review.
[478] Justine McCarthy, "The Irishmen and Their British Property Empire," *Irish Independent*, September 24, 2004.
[479] Power, "Feel-Good Factor Is Set to Build in 2005."
[480] Martin Fitzpatrick, "New-Comers to the Financial Bigwig List in the UK," *Sunday Independent*, November 25, 2005, sec. Business Opinion.
[481] Mercille, "Opening Statement of Julien Mercille," 1–3.
[482] Maeve Quigley, "BUY HOUSE BEFORE POLL," *Daily Mirror*, May 17, 2007.

went bust[483]. Likewise, *House Hunters* presenter, Liz O'Kane, owned a property and home finding business[484]. In a May 2007 webchat, she advised members of the public:

> buy now, buy if you can…Supply in property is currently outweighing demand and there could be deals to be done…
>
> My advice is to buy now…should the next government abolish stamp duty for first timers this will simply put the price of properties for first time buyers...UP!

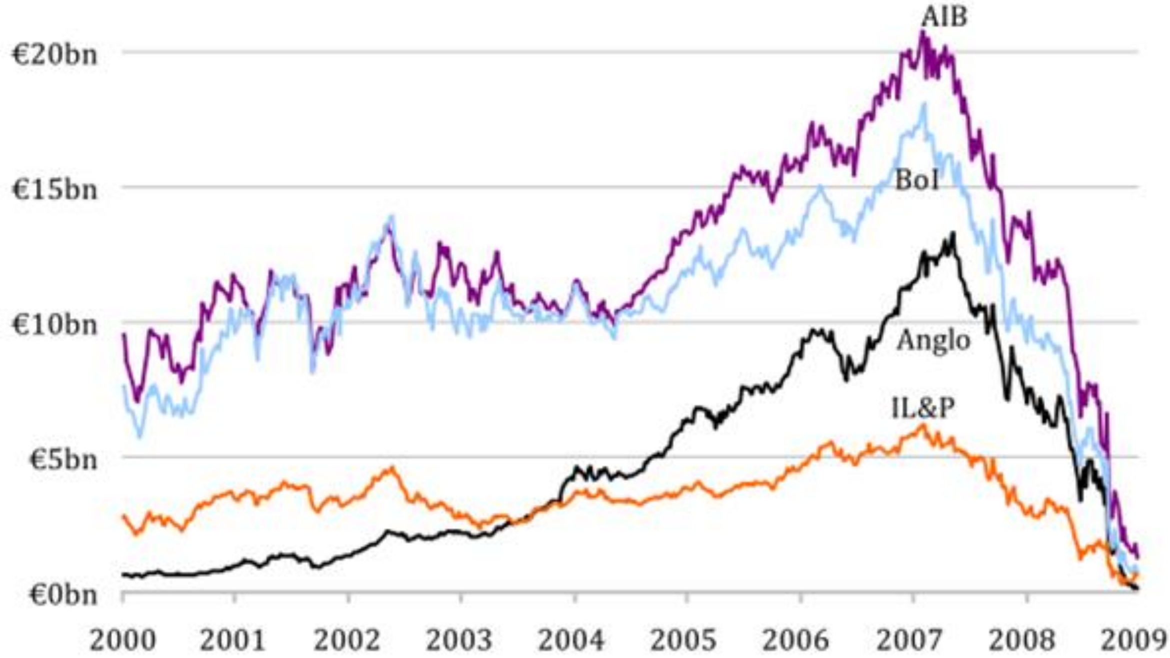
When asked directly, "Do you think that the property market could crash?", she answered, "No... I don't think any government can afford to let that happen. A levelling off is what we are seeing."[485]

Late Summer/Autumn 2007: The Crisis Begins

Meanwhile, concerns about the banks' property loans were emerging among financial market analysts and international investors. Irish bank shares peaked in February 2007[486] and fell fairly consistently thereafter (Figure 4.2). Given the faith of the government and all the establishment political parties in the wisdom of the markets, it's perhaps surprising they were not more alarmed by this collapse in the banks' share price. However, this was one area where the public was always told that the markets had it wrong and were over-reacting to the subprime crisis in the US. Once again, 'people in the know were clear that things were problematic'[487] but it wasn't in their interest to warn the wider public.

[483] John Maguire, "I Lost €15m and Fought Back," *Irish Independent*, January 8, 2012, sec. Weekend Magazine, http://www.independent.ie/lifestyle/i-lost-15m-and-fought-back-26809417.html.
[484] Drogheda Independent, "Entrepreneur Liz Takes the Stress out of Moving Home," *Drogheda Independent*, September 26, 2003, http://www.independent.ie/regionals/droghedaindependent/news/entrepreneur-liz-takes-the-stress-out-of-moving-home-27112414.html.
[485] RTE, "House Hunters - Webchat with Liz O'Kane," May 10, 2007, http://www.rte.ie/tv/househunters/webchat.html.
[486] Nyberg, "Nyberg Report," 14.
[487] O'Connell, "Transcript of Tom O'Connell Hearing," 93.

Figure 4.2 Share Prices of the Irish Banks 2000-2009[488]



Source: Irish Stock Exchange

Almost immediately after the May 2007 election (during which Fine Gael, Labour, Fianna Fáil and the Greens all promised to cut stamp duty and squeeze the last drops out of the bubble[489]), it became clear that a major crisis was developing internationally. The US subprime debacle had begun to develop into the Global Financial Crisis. From August onwards, there were shortages of 'liquidity' – the short-term cash that allows banks to fund their day-to-day operations – in the global money markets as the big banks and speculators became unsure where was safe to put their money. This led to collapse of Northern Rock in September 2007, further intensifying the credit crunch. It gradually became harder and harder for Irish banks to get the wholesale funding and big corporate deposits they needed to finance their bloated loan banks, as investors started to scrutinise banks with a lot of property lending.

Those investors included the National Treasury Management Agency (NTMA), which borrows money for the state and chooses where to invest its cash reserves and the National Pension Reserve Fund (RIP). In August 2007, it decided to stop placing deposits with the Irish banks in order to safeguard the state's money[490]. According to Brendan McDonagh, who was then the Finance Director of the NTMA[491] and the NTMA's former CEO John Corrigan, this should have signalled to other Irish authorities that the banks were unstable:

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488 Nyberg, "Nyberg Report," 14.
489 2007 Election Manifestoes
490 "Transcript of John Corrigan (NTMA) Hearing," July 15, 2015, 8; "Opening Statement of Brendan McDonagh (NTMA)," July 9, 2015, 2.
491 "Transcript of Brendan McDonagh (NTMA) Hearing," July 9, 2015, 80, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/07/09072015_BrendanMcDonagh_vol1.pdf.

> it obviously should have sent out a signal that those people, i.e. the National Treasury Management Agency, who had a strong market-facing role, had very fundamental concerns about the stability of the financial system. I mean, that was the obvious message that it should have sent… the signal was very clear and, and left…could not have left anybody in any doubt. [492]

As we shall see, rather than heeding this warning, the Central Bank and the Department of Finance instead pressured the NTMA to reverse course and 'support the banks' – a position that culminated in directing them to sink €20.7bn from the National Pension Reserve Fund into insolvent banks. For now, however, the stage was set for twelve months in which the government, the Central Bank and Financial Regulator, the banks and the developers looked on in horror while their system imploded – and devised elaborate schemes for bailing themselves out at our expense.

[492] "Opening Statement of Brendan McDonagh (NTMA)," 2; "Transcript of John Corrigan (NTMA) Hearing," 7.

Chapter 5 - The Slow Road to the Guarantee

Once the Global Financial Crisis got underway in autumn 2007, the authorities acquired evidence on top of evidence of serious problems in the banks' loans books that might make them insolvent. Bank shares were collapsing far more in Ireland than in other countries and the authorities were repeatedly told that this was because of market concerns about their over-dependence on property. The evidence gathered by the Inquiry also showed that far from being caught unawares on the night of the Guarantee, the Department of Finance, Central Bank and Financial Regulator had been preparing for a bank collapse since the summer of 2007 when they set up the 'Domestic Standing Group' (DSG). At the DSG and in the Central Bank, bank insolvency and guaranteeing insolvent banks were discussed right from the start. An email from the Department of Finance to the Central Bank and Financial Regulator, dated October 3rd 2007 states:

> Once an institution is insolvent the Central Bank cannot provide ELA [Emergency Liquidity Assistance] to the institution. In order for the institution to be assisted the CB would required [sic] some form of guarantee from the Government eg a letter of comfort. This would allow the CB to treat the institution as illiquid but solvent.[493]

This is what the government did on the night of the Guarantee but for the whole banking system rather than a single bank. It made an insolvent banking system 'solvent' by guaranteeing all its liabilities. This made it legal for the Central Bank and the ECB to keep shovelling money into bankrupt banks to replace all the liquidity they were losing because the markets knew they were insolvent and wouldn't lend to them anymore.

The state prepares for a crisis

The first evidence of crisis preparation by the state was the establishment of the Domestic Standing Group (DSG) in July 2007. All EU governments had been obliged to set one up as a crisis preparation measure but Ireland's found itself struggling with an actual crisis almost immediately. The DSG was a forum for the Central Bank, Financial Regulator and Department of Finance to exchange information on the crisis and drew up several drafts of a 'Crisis Resolution Options' paper. The NTMA was invited to attend some of its meetings, mainly to pressure them to place deposits with the Irish banks[494]. DSG documents, along with some other Central Bank and Department of Finance documents supplied to the Inquiry, give an insight in real time into how the state reacted to the crisis and the different options it was considering at different points in time.

Right from the start, all the options that were seriously considered by the authorities involved socialising the private debts of bankers, developers and bondholders. The alternative – of making the golden circle take their losses and protecting the useful aspects of the banking system by taking them into democratic public ownership – was never contemplated. In fact, rather than developing a solution over time that would lessen the impact of the crash on society, the weight of the burden to be foisted onto working people got progressively larger and larger. The rest of this chapter examines what we know about what authorities were saying and doing in private about the crisis and who was lobbying them, from August 2007 to September 29th 2008. The main focus is on the earlier part of

[493] Department of Finance, "Email and List of Issues for DSG Meeting 3 Oct 2007," October 3, 2007.
[494] Michael Somers, "Transcript of Michael Somers (NTMA) Hearing," July 9, 2015, 117, jhttps://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/07/09072015_Somers_vol1.pdf.

this period up to the St. Patrick's Day Massacre of bank shares in March 2008 in order to demonstrate how long the authorities had to prepare for the crisis and how much they knew, six months to a year before the famous 'night of the Guarantee'.

August 2007

August: The thrust of the Central Bank's first financial markets update provided to the DSG on August 31st 2007[495] – the same month the NTMA decided to stop depositing money with the Irish banks – was what it kept saying publicly for a year; 'This is not an Irish problem but a global one.' However, it warned that 'If liquidity difficulties persist into the medium term, a difficulty in accessing funds may lead to more expensive or harder to find credit in the Irish system, with potential knock on effect on interest rates and economic growth'. Less than a fortnight later, Northern Rock collapsed, causing chaos on the financial markets.

September: The Central Bank's next report to the DSG, dated September 21st, stated that there was 'No indication that Irish banks are vulnerable to Northern Rock-type scenario at this time' and that the 'Irish banks are not reliant on wholesale funding to the same extent.' Northern Rock's loan-to-deposit ratio was 322%[496] compared to 150-175% at most of the Irish banks and over 275% at ILP (Figure 1.6), but these were high enough levels to choke off liquidity for the banks throughout the next year. The Central Bank report flagged this could become more of a problem in future, explaining that 'the longer the current liquidity crunch continues the greater the prospect that it will give rise to pressures for the Irish financial system.' It also explained that ECB funding, which was available to Irish banks who put up certain types of eligible assets as collateral, was 'a very important safeguard for Irish banks'. Figure 4.3 shows the banks' growing dependency on ECB funding from 2007 onwards. This reflected a new phenomenon where 'some banks are researching potential borrowing counterparties directly prior to considering lending to them'. In other words, creditor banks were now paying attention to debtor banks' underlying business models before lending them money.

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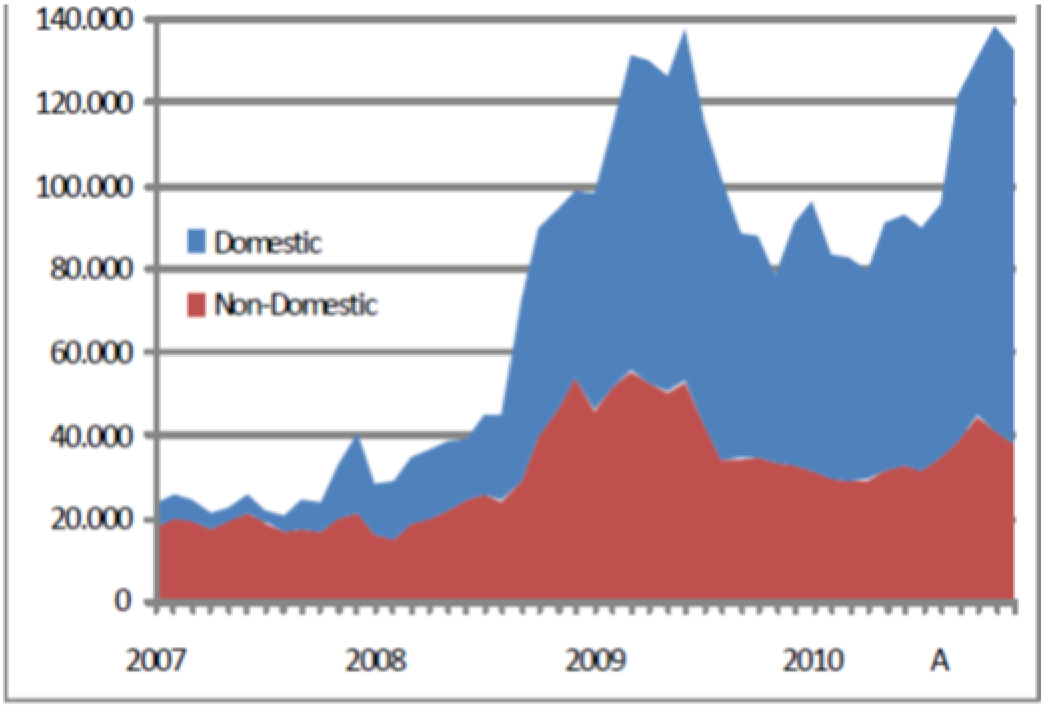
[495] CBSFAI, "Central Bank/Financial Regulator Views on Financial Market Development as Conveyed to DeDartment of Finance at Meeting of 31 August (summary Report)," August 31, 2007.

[496] Greg Pytel, "Memorandum from Greg Pytel: THE LARGEST HEIST IN HISTORY, Building the Great Pyramid: The Global Financial Crisis Explained - Written Evidence to House of Common," February 2009, http://www.publications.parliament.uk/pa/cm200809/cmselect/cmtreasy/144/144w254.htm.

Figure 5.1 ECB Funding for Irish Banks[497]



October:

In early October, the DSG began working on a 'Scoping Paper' on Financial Stability Issues[498]. A preparatory note drafted by Department of Finance officials recommended examining 'The legal position regarding a number of potential policy options for the State to provide support to financial institution in difficulty'. They included: 'the legal scope for a "letter of comfort" to be given to the Central Bank in an emergency situation confirming the Minister's intention to approach Dáil Eireann for legislative authority to enable the issuance of a financial guarantee to the Central Bank'. Reference was also made to 'the scope for NTMA to place a deposit with a bank' and amending the Deposit Guarantee Scheme[499].

The note then outlined three different scenarios of bank failure: where a bank was: 'Illiquid but solvent'; 'Nearing insolvency' or 'Insolvent'. Anyone who watched the news in 2008 will remember the mantra that the banks were 'only' facing liquidity issues and were not insolvent. So we were repeatedly told we were facing the first scenario, right up until the government started shovelling billions into the banks and it turned out they were all extravagantly insolvent. Crucially, it was only in the first scenario that the Central Bank was legally allowed to lend to a bank[500]. This was the case both for normal ECB lending where the banks put up eligible collateral such as mortgages as security and Emergency Lending Assistance (ELA), which Central Banks can only give to banks that have run out of eligible collateral but are still solvent.

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[497] Gary O'Callaghan, "Did the ECB Cause a Run on Irish Banks? Evidence from Disaggregated Data," *Irish Economy Note*, no. No. 13 (February 2011): 6, www.irisheconomy.ie/Notes/IrishEconomyNote13.pdf.
[498] Department of Finance, "Financial Stability Options –Scoping Paper," January 24, 2008.
[499] Department of Finance, "Email and List of Issues for DSG Meeting 3 Oct 2007."
[500] Frank Browne, "Witness Statement of Frank Browne," November 2015, 71; Department of Finance, "Financial Stability Options –Scoping Paper," 2.

In the other scenarios, 'Nearing insolvency' and' insolvency', nationalisation was suggested as an option. That this was only considered then, rather than when a bank was 'just' illiquid but had a healthy underlying loan book, indicates how right from the start the state's approach to nationalising banks was associated with imposing huge costs on the population. The type of nationalisation the authorities had in mind was the sacrificial style of temporary nationalisation that happened all over the world during the Global Financial Crisis, which socialises bank losses but then returns the banks to private hands as soon as they are profitable again, to re-start the boom/bust cycle. The Department of Finance note concluded by commenting that 'The failure of a small institution could have systemic consequences if its problems are likely to effect [sic] confidence in other larger institutions'. This was perhaps a reference to Anglo or INBS, which was already in such dire straits that it would decide to 'effectively cease lending and build liquidity' that December[501]. The last sentence reads: 'If there was a shock relating to property this could apply to all banks - this would have implications for any rescue operation.'[502]

An 'Update on Financial Issues' for Brian Cowen to brief a Government Meeting on October 9th was based on a relatively reassuring Central Bank update on financial market and makes no reference to the DSG's plans[503]. It said there were 'continuing signs of a return to more normal financial market conditions but wholesale lending rates remain high particularly in the Eurozone'. It also stated that 'Irish banks currently have a "good-name" in the market on account of their low sub-prime exposure and low dependence on short-term funding'. However, it also referred to 'significant losses incurred by high net worth individuals in relation to Contracts for Differences (CFD), which may have been the first Cowen or the Government heard of Sean Quinn's disastrous holdings in Anglo[504]. Despite all this, Anglo's former head of Irish lending, Tom Browne, told the Inquiry that when he left Anglo that month[505], with a €3.75m golden handshake, 'I'd no sense that the bank was under any stress as I was walking out the door…As I was leaving I had absolutely no sense of any issue coming down the track.'[506]

November

An Aide Memoire for Cowen to brief Cabinet, dated November 13th, notes that 'more generalised concerns about the Irish economy and the exposure of banks to the property sector has resulted in Irish banks having to pay a premium in accessing liquidity, and share prices have been depressed (making them increasingly attractive for takeover).' However, its overall tone is more reassuring because it is partly based on the de-sexed 2007 *Financial Stability Report,* published November 17th. This omitted the Bank's own analysis that house prices were overvalued by 39%, which had been deleted from an earlier draft and wasn't included in Cowen's written Aide Memoire either[507]. Based on the FSR, Cowen's briefing for Cabinet said:

[501] "Opening Statement to the Inquiry of Michael Walsh (INBS)," September 2, 2015, 4. INBS shrank its loan book from €12.3bn in 2007 to €10.5 in 2008 and reduced its commercial property lending by 19%.
[502] Department of Finance, "Email and List of Issues for DSG Meeting 3 Oct 2007."
[503] Department of Finance, "Update on Financial Issues - Government Meeting 9 October 2007," October 8, 2007.
[504] Ibid. According to *Anglo Republic,* Quinn had revealed his interest in Anglo to David Drumm and Sean Fitzpatrick the previous month Simon Carswell, *Anglo Republic*, 2011, chap. 7..
[505] Tom Browne, "Transcript of Tom Browne (Anglo) Hearing," September 9, 2015, 144.
[506] Ibid., 173.
[507] Browne, "Witness Statement of Frank Browne," 61.

> The underlying fundamentals of the residential market continue to appear strong. The central scenario is, therefore, for a soft, rather than a hard, landing…the rate of credit growth has eased and the rate of accumulation of private-sector indebtedness has moderated accordingly….notwithstanding the international financial market turbulence, the Irish banking system continues to be well placed to withstand adverse economic and sectoral developments in the short to medium term.[508]

Cowen's Aide Memoire also makes no reference to the commercial property market despite the FSR including its first ever article on the subject. That starts by saying that despite the focus on residential property, 'it could be argued that developments in the commercial property market have greater consequences for the stability of the Irish financial system.'[509] It concludes that:

> in times of financial stress, it is exposure to the commercial property market that causes the greatest credit losses for the banking sector. Possible explanations for this occurrence are relatively greater incidences of defaults on commercial property-related loans and the fact that commercial property prices tend to exhibit greater cyclical volatility[510].

This alarming observation was not included in the FSR's Executive Summary, which alluded to the disjunct between high commercial property prices and low rents but concluded that because this was happening everywhere (and was about to cause the worst global financial collapse since the Great Depression), things must somehow be ok:

> It may be of comfort that some international markets have also mirrored this trend of robust appreciation in capital values, indicating that global factors may explain some of these trends. Furthermore, other markets have not only experienced robust capital growth but have also experienced relatively static rental growth such that, in general, it appears that yields on European commercial property have also declined significantly. [511]

This reassuring tone was also reflected in media coverage at the time. Dr. Julien Mercille told the Inquiry that the *Irish Times* surveyed '"property experts"' that month 'to predict how the market would evolve in 2008. The six experts selected all held high-level positions with property firms. Not surprisingly, their forecast was enthusiastic.'[512]

Cowen's next update from the Central Bank via the DSG after its November 16th meeting gave some very clear warnings that Irish banks' liquidity problems were particularly bad because of market suspicions about their property lending. Cowen was told bank share prices have 'lost between 30% and 50% of their value since the start of 2007 because of negative investor sentiment regarding Irish

[508] Department of Finance, "Aide Memoire for the Government: Financial Markets Developments," November 13, 2007.
[509] Maria Woods, "A Financial Stability Analysis of the Commercial Property Market," in *Financial Stability Report 2007* (Central Bank, 2007), 75–90, http://www.centralbank.ie/publications/Documents/1.%20Financial%20Stability%20Report%202007%20-%20Part%201.pdf.
[510] Ibid., 89.
[511] Central Bank, "Financial Stability Report 2007," November 17, 2007, 16, http://www.centralbank.ie/publications/Documents/1.%20Financial%20Stability%20Report%202007%20-%20Part%201.pdf.
[512] "Opening Statement of Julien Mercille," March 26, 2015, 5.

banks and their exposure to the Irish property market'. It was also pointed out that: 'The decrease in value of Irish banks shares has been greater than in other countries' and reference is made to a '7 November report from Merrill Lynch setting out a negative perspective on the Irish banking sector because of property exposures.' Moreover, it cites 'anecdotal evidence that the change in the financing environment and restriction of lending is impacting on the property development sector' and that 'The quality of assets secured on speculative development land is a particular focus of attention for financial institutions…'

Cowen is also told that liquidity problems are only going to get worse because 'A number of Irish financial institutions have significant "roll-over" funding requirements arising from the beginning of next year. If the present market conditions persist, as expected, into 2008 there is an increased risk of liquidity issues arising for Irish banks.'[513] The update coincided with a spike of about €20bn in the Irish bank's reliance on ECB funding (Figure 4.3), which it explains:

> is provided at above market rates and is less attractive to banks which have to manage their liquidity while minimising the cost of funds. Where banks have good quality assets as lending collateral, they are using it to access market funding at more competitive rates. This suggests that any increased access to ECB liquidity is evidence of increased financial stress.

It concludes by saying that many commentators now believe 'the current market disruption will take an extended period (i.e. up to 2 years) to resolve'. Clearly, by the end of November 2007, Cowen, the Department of Finance and the Central Bank/Financial Regulator all knew that the banks' liquidity problems were not just due to the global credit crunch but were related to market concerns about their property lending. The then Attorney General, Paul Gallagher, also testified that from November 30th 2007 onwards, 'the Department was in constant contact with my office, looking at possibilities, identifying different options.'[514] This indicates that the increased seriousness of the situation was recognised. However, the really obvious thing to do would have been to start investigating if 'the markets' were right about the problems in the banks' loan books rather than continuing to effectively take the banks' word for it that everything was ok.

December

This was all the more obvious a course of action given that in December, Frank Browne proposed an additional 'more realistic' bank failure scenario for the Department of Finance's Scoping Paper where 'it is uncertain as to whether the bank is merely illiquid or is insolvent'. His rationale was that:

> With banks increasingly involved in financial markets, it may be very difficult, in a period of severe asset market turbulence, to know or even ascertain (without an in-depth and time-consuming examination) the true market value of a bank's assets or the asset market to which it may have a big contingent exposure. It may, therefore, be difficult to infer whether a bank is just illiquid or has become insolvent, especially in light of the incentives a bank may have to disguise its true state of health from a central bank or financial regulator[515].

[513] CBFSAI, "CBSFSAl Assessment of Financial Market Developments," November 16, 2007.
[514] Paul Gallagher, "Transcript of Paul Gallagher (Attorney General) Hearing," July 16, 2015, 5, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/07/16072015_Gallagher_vol1.pdf.
[515] "Witness Statement of Frank Browne," 71.

The Financial Regulator appears to have made some lame efforts to find this out. That same month, it carried out a brief ten day review of the five largest commercial property exposures of five Irish banks. This found that "institutions have been unable to obtain a Net Worth Statement from [a large debtor], as he is unwilling to disclose such details in writing. In addition, the statements provided by [two other large debtors] have not been certified by a third party"'. The inspectors also noted large variations in the estimated overall indebtedness of the same developers by different banks and one bank that made no attempt to find out how much one of its largest borrowers owed other banks. In addition, "the majority of facilities provided to the [big] borrowers…are currently on capital or complete moratoria" [516] , causing the Regulator to comment that "given the current repayment terms of most facilities….the fact that there are currently no arrears on any exposures reviewed would not necessarily be indicative of the financial soundness of the borrowers".[517] Identical findings were made by PWC, Merrill Lynch and NAMA[518], months and years later.

For Honohan, 'the obvious lesson' given 'this catalogue of banking deficiencies' was 'that loan appraisal had been wholly inadequate and personal guarantees could not to be relied upon' . The implication, he said, was 'that the solvency of all of the banks could be at risk given the declining value of collateral'[519] . Yet the Regulator reported that "all institutions confirmed to the inspectors that they have no concerns with the current or future repayment capacity of any of the borrowers"[520] and seems to have been satisfied with these reassurances despite all the evidence to the contrary. The head of the Banking Supervision Department, Mary Burke, confirmed that other than issuing post-inspection letters, there was no other follow-up with the banks[521]. She attributed this to a lack of resources and explained that despite the Global Financial Crisis, there was no increase in the tiny number of staff inspecting the banks until long after the Guarantee[522]. This was confirmed by Mary O'Dea[523], who was on the Board of the Regulator at the time. She recalled that the prudential/banking supervision side had requested a 'large increase in staff' 'around 2007-2008' but the Budget and Remuneration Committee 'had wanted to be convinced that there couldn't be efficiencies gained' from sharing IT and other services with the Central Bank first[524]. This lack of resources, which reflected the neoliberal philosophy of deferring to banks to regulate themselves meant the 'in-depth and time-consuming examination' of the banks' loan books needed to find out whether they were insolvent or just illiquid never happened.

Instead, Brendan McDonagh told the Inquiry that Cowen ended the year by ordering the NTMA to place deposits in the Irish banks. McDonagh said the NTMA's position at a meeting of the DSG on December 12th 'was that in the absence of a written direction from the Minister, we did not intend

516 This accounted for three-quarters of the 266 loans inspected. Out of 103 loans inspected at one bank, 61 were interest only and 33 were interest roll-up.
517 Financial Regulator, "Inspection of Commercial Property Lending," December 2007.
518 Frank Daly, "Opening Statement by Mr. Frank Daly, Chairman of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," April 22, 2015; Brendan McDonagh, "Opening Statement of Brendan McDonagh (NTMA)," July 9, 2015.
519 Patrick Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008," May 31, 2010, 70.
520 Financial Regulator quoted in ibid.
521 Mary Burke, "Transcript of Mary Burke Hearing," May 27, 2015, 77–78.
522 Mary Burke, "Opening Statement to the Banking Inquiry," April 29, 2015, 6.
523 Mary O'Dea, "Transcript of Mary O'Dea (Financial Regulator) Hearing," June 10, 2015, 12–13, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/06/10062015_ODea_vol1.pdf.
524 Ibid., 11.

reversing this policy…We made the point at the meeting that, if anything, the risks attaching to the banking system, internationally as well as domestically, had become even more pronounced'[525]. Cowen duly wrote to the head of the NTMA, Michael Somers on December 19th directing him to deposit €500m with AIB, BOI, ILP and EBS. Somers was so reluctant to do this that he sought legal advice as to whether he was obliged to comply[526].

January 2008

In the New Year, things got even worse. On January 10th, KPMG, PWC, Ernst & Young and Deloitte, who were auditing the banks' 2007 accounts, met with the Financial Regulator. KPMG said this was a 'general discussion' that included '[auditors'] opinions, going concern and valuation issues', 'risk management and the bank's ICAAP [Internal Capital Adequacy Assessment Process]'[527]. As part of auditing a bank's annual financial statements, auditors have to certify whether bank management are reasonable in believing that the bank will remain a 'going concern' for the coming year – in other words that it won't go bust in the next twelve months[528]. So the fact the 'big four' auditing firms were discussing 'going concern' and the adequacy of the banks' capital with the Financial Regulator in January 2008 suggests they were worried the banks might not survive the year. Whatever assurances the Regulator and the banks gave them meant they signed off on the banks' accounts as usual that March.

The next day, the DSG discussed another gloomy financial market update from the Central Bank and the latest draft of the Scoping Paper[529]. A summary of the Central Bank update in a memo to Cabinet a few days later[530] alluded obliquely to the meeting with the auditors, stating that 'the publication of audited accounts in due course' was one of 'The next two hurdles that the global financial system, including Ireland, face', alongside 'the rollover of significant long term funding arrangement early in the year'. The memo is the first documentary evidence of the Cabinet, and not only Cowen, being clearly told that the banks' liquidity problems were not just due to the global financial crisis. It states that 'negative sentiment about Ireland remains on account of concerns regarding the property market and the share prices of the banks have continued to fall'. Another problem mentioned in writing for the first time is the 'high level of competition for corporate deposits' which 'could cause difficulties for smaller banks'. However, these warnings were also couched against reassuring report from 'The Irish banks…that they feel that Ireland's "name" is getting a more positive response in the market; for example, Fitch's (rating agency) have recently improved Ireland's rating'. The conclusion also states it is 'important to emphasis [sic] that the Irish banking system is strong, liquid and well capitalised' and that 'Notwithstanding the current turbulence, the Irish banks are accessing their required liquidity, although their share prices have been significantly reduced.'

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525 "Transcript of Brendan McDonagh (NTMA) Hearing," July 9, 2015, 79, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/07/09072015_BrendanMcDonagh_vol1.pdf.
526 Ibid., 105.
527 'what was going in relation to liquidity in the system generally' was also discussed. "Transcript of Paul Dobey and Terence O'Rourke (KPMG) Hearing," May 14, 2015, 108–109, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/14052015_Dobey_vol1.pdf. 'what was going in relation to liquidity in the system generally' was also discussed.
528 Ibid., 72.
529 Browne, "Witness Statement of Frank Browne," 70.
530 Department of Finance, "Memorandum for the Information of Government - Financial Markets Developments," January 16, 2008.

The other main item on the DSG's agenda was the Scoping Paper, which now ran to 22 pages. Its stated purpose was:

> to identify significant issues relating to the options available to the Irish authorities in the case of a systemic threat to financial stability, , as well as consider any issues regarding the structures currently in place to oversee financial stability planning arrangements and also to manage a financial crisis.[531]

Having been passed back and forth between the Department of Finance, Central Bank and Financial Regulator, it aggregates their thinking at that point. However, William Beausang, who was the lead Department of Finance official dealing with these secret crisis management efforts[532] said that:

> key elements of the Department's assessment and conclusions set out in the Scoping Paper were not shared by the CBFSAI. Consequently, no agreement was reached at the DSG on the Scoping Paper and it was not submitted to the Minister nor the Secretary-General of the Department of Finance.'[533]

Notwithstanding this, the paper sheds a lot of light on what the authorities did on the night of the Guarantee as much of the logic in it (including the parts about guarantees which the Department and the Central Bank seem to have disagreed about) is consistent with what actually happened.

The paper begins by explaining the Central Bank/Financial Regulator's policy of 'constructive ambiguity' which 'involves not sharing full information about public authorities' likely actions in a financial crisis'. One reason given is the familiar spectre of the 'confidence fairy':

> Transparency regarding the preparations and preparedness of authorities for a financial crisis may help support public confidence in the event of a crisis but it may also constrain authorities' actions in any given crisis due to expectations of their actions. It may also condition or influence public perceptions of the likelihood of a financial stability event.

In other words, as with the myth of the soft landing, keeping us all in the dark was a conscious part of the state's crisis management strategy. Again, this was supposedly for our own good but it turned out somewhat better for the bankers and developers that it did for us.

The other reason for 'constructive ambiguity' is supposedly to minimise 'moral hazard'. The paper says this should encourage banks 'to monitor and manage risks that might otherwise be ignored if an institution was confident that the CBFSAI would definitely intervene'. A key aspect of this is which banks the state bails out with ELA or a guarantee and which it lets fail. However, as Frank Browne pointed out:

> Since it is known that some banks are too big to be allowed to fail (TBTF), and since ELA may well be required to prevent a TBTF bank from failing, there can, in fact, be little ambiguity about the central bank's approach to its policy of ELA with respect to such banks. The

[531] Department of Finance, "Financial Stability Options –Scoping Paper."
[532] More senior people like Kevin Cardiff and David Doyle played more of a role later on.
[533] William Beausang, "Clarification Statement of William-Beausang," September 15, 2015, 4.

> market knows that ELA will be triggered…an attitude of constructive ambiguity by the central bank could be, to a large extent, illusory.[534]

What Browne is getting at here is that AIB and BOI knew they were 'Too Big To Fail' (TBTF) from the authorities' perspective – or too 'systemically important' to use the politically correct terminology – and would have acted on that basis. In fact, this was so widely known, that Hurley and Neary reportedly even told the CEO of EBS, Denis Casey, that AIB and BOI 'enjoyed the benefit of the perception that they were too big to fail' but none of the other banks had 'the luxury of implicit government support'[535]. Professor Kane, who invented the concept of TBTF banks, told the Inquiry:

> This, of course, is something that the industry denies. I have been told by some bankers that they were fully aware and that they were exploiting taxpayers, but the Chairman will have a hard time finding this on the public record.'[536]

For smaller banks, like Anglo, ensuring they would be treated as 'TBTF' was more of a battle. During his hearing, Kane defined TBTF banks as 'banks that have political power to extract guarantees to support themselves'[537] and the interaction between Anglo and various representatives of the state over the next nine months could be seen as an effort to wield that power successfully. They were also helped along by the state's inertia until the crisis had advanced to such a pitch that the government was forced it to do the unthinkable and make a major intervention into the sanctity of the private market. By then, the situation had been allowed to deteriorate to such an extent that the nightmare scenario outlined in the scoping paper – where all banks are TBTF for systemic contagion reasons – was seen by the authorities bent on saving that system at all costs to have come to pass.

The scoping paper defines a 'A TBTF financial institution' as: 'one whose failure is believed to be likely- both directly through its impact on the real economy and indirectly through the risk that contagion effects will threaten the stability of other financial institutions - to provoke a systemic failure of the financial sector overall.' However, it outlines two situations where 'any institution may be TBTF'. The first is where 'public confidence in the system in general or general financial market conditions…is low' and 'the failure of any institution could cause systemic problems'. The second 'relates to the type of difficulties encountered by the institutions. If there is a perception that this type of difficulties (eg exposure to the property market) is likely to affect more than one institution this could also mean that its failure would have systemic consequences.' The conclusion is that 'The failure of even a small bank which is not systemically important in itself may not be acceptable in certain circumstances because of fear of contagion'. This was reiterated in a Department of Finance presentation in February, which states that 'If confidence fragile then small institution could trigger systemic difficulties which suggests all institutions are TBTF (in current market environment)'[538]. The acting Governor of the Central Bank, Tony Grimes, also confirmed that the idea of a 'domino' or

[534] Browne, "Witness Statement of Frank Browne," 10.
[535] Carswell, *Anglo Republic*, chap. 10.
[536] Ed Kane, "Transcript of Ed Kane Hearing," January 28, 2015, 246.
[537] Ibid., 240.
[538] Department of Finance, "Overview of Financial Stability Resolution Issues," February 8, 2008, 4.

‘contagion’ effect where one bank could bring down the others ‘was implicit…right the way through’[539].

The scoping paper then outlines what should be done in three scenarios of bank failure, where a bank is 1) illiquid but solvent; 2) insolvent or near insolvent; or 3) it is unclear if it is illiquid or insolvent. Its basic thrust is that the Central Bank should extend ELA in scenarios 1) and 3) and in scenario 2) as well if the bank is TBTF. However, if a bank is not TBTF, it states that ‘the preferred outcome for an insolvent institution may be its failure and subsequent orderly wind-down’ – indicating how high the stakes were for smaller banks lobbying politicians and civil in 2008.

A key ‘problem’ discussed throughout the paper is that unless it’s certain a bank is only illiquid but not solvent, the Central Bank will need a state guarantee because it’s illegal to give ELA to an insolvent bank:

> if an insolvent bank sought ELA, the CBFSAI would be legally prohibited from extending it. However, if the bank was systemically important and the Government agreed to extend a guarantee to its liabilities, then this would turn it from an insolvent bank into an illiquid but solvent one (with the State guarantee backing up its capital), so that the CBFSAI could inject liquidity to prevent contagion effects in the wider financial system…

The paper goes on to explain that according to the Central Bank, ‘letters of comfort’ from the Minister for Finance don't have a strong enough legal standing to cover its back on this and that existing powers under the 1954 State Guarantees Act would also be insufficient because they are ‘normally subject to a cash limit’ - which would presumably be a lot less than €440bn. Hence the conclusion that ‘a comprehensive guarantee would be necessary.’

Other possible actions mentioned in the paper include nationalisation and how to wind down failing banks under existing company law, through examinership, receivership and liquidation. Examinership is said ‘to offer the least difficulties and most advantages of all the procedures except possibly in the case of dire insolvency’. However, it can only be applied for by the CBFSAI, which would have to ‘demonstrate that the company is insolvent or likely to become so’ and also ‘satisfy the Court that there is a reasonable prospect of ensuring the survival of all or part of the undertaking’. A major snag the paper identifies with this is that ‘The CBFSAI do not consider that their supervisory data would be detailed enough/suitable to establish viability or to support the independent accountant's report to support its application’. In other words, the Financial Regulator’s ultra light touch approach to regulation meant it felt it didn’t have the information legally required to support an application for Examinership. Once again, this would seem like a giant flashing light for the authorities to start getting that information from the banks rather than continuing to ‘trust’ them.

An alternative option, ‘to consider a special insolvency regime for banks’ is also mentioned but according to several witnesses[540] and documentary evidence from the time[541] was not proceeded

[539] Tony Grimes, “Transcript of Tony Grimes (Central Bank) Hearing,” May 27, 2015, 26, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/27052015_Grimes_vol1.pdf.

[540] “Transcript of Hurley Hearing,” n.d., 116–117, accessed May 25, 2015; “Transcript of Tony Grimes (Central Bank) Hearing,” 34–35; “Transcript of Second Kevin Cardiff Hearing,” June 24, 2015, 69, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/06/24062015_Cardiff_vol2.pdf; “Transcript

with because it was seen as too legally complicated to develop quickly. This was due to the extreme level of protection of private property rights over almost everything else in the Irish Constitution, which clearly no one involved had any desire to test or reform. According to the acting Governor of the Central Bank, Tony Grimes, ‘There was also, I think, the view expressed that introducing it at that particular time [summer 2008] may reflect more the sort of crisis situation than might be helpful’[542]. In other words, yet again, ‘don’t frighten the horses!’

The significance of the Scoping Paper is that it demonstrates very clearly that the authorities had been preparing for the possibility of a systemic banking failure, caused by one or more banks becoming insolvent, and that they had also already connected this to banks’ dependence on property lending. The crisis management options discussed in it were debated again and again over the following months, including at the next DSG meeting in February.

February

A Department of Finance presentation at that meeting shows the three main options it was considering were ‘Orchestrated market-based solution (i.e. non-publicly organised private “take-over…), examinership and ‘as a last resort’ nationalisation[543] - all of which had gotten an ‘overall…favourable’ assessment from the Attorney General. It is also stated very clearly that:

> As a matter of public policy to protect the interests of taxpayers any requirement to provide open-ended/legally binding State guarantees which would expose the Exchequer to the risk of very significant costs are <u>not</u> regarded as part of the toolkit for successful crisis management and resolution[544].

This appears to reflect a significant disagreement at that point with the Central Bank given the acting Governor of the Central Bank, Tony Grimes, acknowledged during his hearing that in February 2008 the Central Bank was already considering ‘a system-wide guarantee to all liabilities’[545]. The presentation went on to differentiate between deposit guarantees, a ‘guarantee in respect of CBFSAI liquidity support to distressed financial institution’ and a ‘State guarantee to underwrite a Bank's solvency position’ which it said ‘could only be justified in circumstances that otherwise the entire financial system is at risk of collapse’[546]. The next slide again seems to indicate a disagreement on this with the Central Bank as it says the Department is:

> Seeking to clarify the legal basis for the requirement [from CBFSAI Explanatory Memorandum on ELA] that in order for the CBFSAI to inject liquidity into an insolvent

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of Brian Cowen Hearing – Regarding His Role as Former Taoiseach,” July 8, 2015, 91–92; “Transcript of William Beausang (Department of Finance) Hearing,” June 24, 2015, 96–97, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/06/24062015_Beausang_vol1.pdf; “Transcript of Paul Gallagher (Attorney General) Hearing,” 30–31.

[541] Department of Finance, “Department’s Powerpoint Presentation Re Contingency Planning,” April 17, 2008, 6.

[542] “Transcript of Tony Grimes (Central Bank) Hearing,” 34–35.

[543] Department of Finance, “Overview of Financial Stability Resolution Issues,” 10.

[544] Ibid., 11.

[545] Grimes, “Transcript of Tony Grimes (Central Bank) Hearing,” 26.

[546] Department of Finance, “Overview of Financial Stability Resolution Issues,” 16.

> institution *a Government guarantee of the institution's liabilities* would be required (my emphasis)[547]

The other point on the same slide states that 'the Minister may request the CBFSAI to consult with him both with regard to the provision of an ELA and the terms and conditions on which it may be provided. The CBSFAI is obliged to comply with such a request'. In other words, the Department is telling the Central Bank it has to do what the Minister says. A further suggestion of possible differences between the two comes in the reference to 'Review and any necessary reform of DGS [Deposit Guarantee Scheme] a priority given the requirement to ensure that examinership is a credit resolution option' when we know from the Scoping Paper that the CBSFAI didn't think their supervisory data was detailed enough for an examinership application, which only they could make. The report of the DSG meeting, which was attended by Beausang, the Prudential Director of the Financial Regulator, Con Horan, and the Central Bank Chief Economist Tom O'Connell, states that the CBSFAI agreed orchestrating 'market-based solutions' was the preferred option and felt it was 'Important to clarify whether examinership would allow certain normal banking activities to continue which might allow depositors to be paid on request'[548], as well as to investigate a special insolvency regime for banks, again suggesting examinership was not seen as a viable option. Of course, the public had no idea any of these intra-elite conflicts were going on; a few slides later, we see that the 'Primary objective' was 'to safeguard public I international confidence in stability of Irish financial system' and that apparently it was 'in the interests of the public that the situation is solved before it enters the public domain in order to prevent contagion'. That objective was certainly achieved – by saying nothing in public until after the government had guaranteed the entire banking system and cost us €65bn.

The CBSFAI's update on financial market conditions for the meeting, which was 'prepared for the Tánaiste [Brian Cowen] for use at government meetings' stated that 'recent negative assessment of the Irish banks by international investment banks has not helped sentiment in the market and their share prices remain low and volatile'. It also reported 'concerns about defaults in the commercial property sector that may arise in loans with moratorium or bullet repayments', an issue that had emerged from the Regulator's inspection of the five biggest bank exposures in December. However, rather than relaying any more of the 'catalogue of banking deficiencies' this had exposed, the only other detail given is what the bank had said about being 'generally happy with the "big players" in property developments' but having 'some concerns about the next tier of developers'[549].

March

March was another turning point for the worse. Cowen's briefing for a Government meeting on March 11th said market conditions were worsening and this was likely to persist, with capital markets effectively closed. International market sentiment about Ireland was said to be very negative due to the banks' exposure to the property market, growing credit risks, and because defaults were seen as likely due to deteriorating economic conditions. The banks were finding it hard to borrow for longer than three months and their Credit Default Swap spreads had increased. So had the spread between Irish and German government bonds – one of the first indications the banking crisis was becoming a

[547] Ibid., 17.
[548] Department of Finance, "Report of DSG Meeting 8 Feb 2008," February 8, 2008.
[549] Ibid.

sovereign crisis. The banks were now pressuring developers to start repaying their loans. No new developments were happening and the government was told that if 'builders begin to default and the banks are unable to refinance their exposures, this will have significant consequences for the banks in terms of profit and credit provision, as well as access to funding, and will have a further negative impact on sentiment regarding the Irish market'. More ominously still, there was an allusion to the banks potentially needing more capital and not being able to get it on the markets:

> As of yet the Irish banks haven't required capital to bolster balance sheets. There is a perception that if capital was required in the current market they might not be able to access such funds in international markets, or would have to pay such a high premium for such capital that it would affect their credibility in the market. A domestic or international institution would be unlikely to wish to increase or take on exposure to the Irish property market in the current market environment.

The update concluded that 'markets are not going to improve soon and may even deteriorate further' with Irish banks particularly vulnerable.

It was around this time that the Central Bank and Financial Regulator began asking the bigger banks to place deposits with the smaller banks to shore up their balance sheets in what became known as the 'Green Jersey Agenda'[550]. Hurley told the Inquiry:

> we met some of the major banks about the potential for their assisting smaller banks that came in to difficulty…you would expect in a banking system that if a small bank was in difficulty, that the first port of call would be the main banks because private sector solutions would be the main vehicle at that stage.[551]

Reference to this was made in Department of Finance briefings to Cowen the following month, which said the banks were discussing ways to assist each other access liquidity but weren't prepared to endanger their own operations. According to Cowen, 'the authorities…were probably trying to engage the banks to think beyond their own immediate concerns and recognise that it was in the interests of all of them that the Irish system be as well funded as possible in a difficult situation.'[552] Unsurprisingly, the bigger banks weren't keen on the rather quaint notion they would help out competitors they'd been engaged in a vicious race to the bottom with out of some kind of nationalistic sentiment. As Cowen put it, 'there comes a point...where commercial imperatives and duties to your own shareholder take precedence over any suggestion that you try and work collegially'[553]. Although for banks it's more like any point at all. In the event, AIB refused to lend to Anglo without a guarantee from the Central Bank. This defeated the purpose of the exercise. According to Neary, the idea behind it was' to avoid, I suppose, a commitment of public funds to any temporary liquidity situation.'[554]

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[550] "Transcript of Hurley Hearing," 101; Patrick Neary, "Transcript of Neary Hearing," May 28, 2015, 117, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/28052015_Neary_vol1.pdf; Grimes, "Transcript of Tony Grimes (Central Bank) Hearing," 25.
[551] "Transcript of Hurley Hearing," 101.
[552] "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," July 2, 2015, 117.
[553] Ibid.
[554] Neary, "Transcript of Neary Hearing," 118.

A while later, the so-called 'St. Patrick's Day Massacre' saw the share price of all the banks but especially Anglo collapse (Figure 4.2) leading to a massive outflow of corporate deposits. When asked when he thought Anglo had become insolvent, Brendan McDonagh identified this at the point when 'the markets had made the decision about banks like Anglo'[555]. Following a from phone call from David Drumm to the Central Bank Governor, John Hurley[556], asking him to put out a statement supporting the bank, both the Central Bank and Financial Regulator put out 'a strong statement of confidence' in the banks[557] . "The Financial Regulator is concerned that false and misleading rumours circulating in financial markets in recent days are connected to unusual trading patterns in Irish shares,' [558] According to *Anglo Republic,* Hurley had even checked the wording with Drumm first. The Regulator also launched an investigation into short-selling of the bank's shares, which Anglo was blaming for the share price collapse. In Simon Carswell's view, 'The interaction between Hurley and Drumm shows how cosy the relationship was between the bank and the state. Drumm had pleaded with the governor for a statement to protect the bank's share price; he'd got two.' [559]

A few days later, Anglo director and friend of Brian Cowen, Fintan Drury, arranged a phone call between the Minister for Finance and the Chairman of Anglo, Sean Fitzpatrick, about the share price collapse[560]. Fitzpatrick was attributing it to the markets having found about Quinn's secret CFD holding in the banks. Cowen told the Inquiry that he had taken the call but dutifully told Fitzpatrick this was a regulatory matter and he should contact the Central Bank/Financial Regulator[561]. Ahern said Cowen called to his home to update him on the Anglo situation a few days later but he revealed nothing material about conversation[562].

When asked why the authorities didn't make an emergency intervention in the banks after the Massacre despite their fear at the time of a systemic banking collapse, Grimes replied: 'It would've been a very big call at the time, I think. Each of the banks that we're talking about had substantial value still in terms of their share price'[563]. In other words, the state wouldn't intervene because it would have infringed on the private property rights of bank shareholders – even when faced with the strong possibility of a banking collapse. The most it could muster was an ineffectual increase in INBS' capital reserve ratio[564]. Incredibly, while all this mayhem was going on, the Regulator hired consultancy firm, Mazars, to carry out a nine-month in-depth review of the organisation. Among the things it was investigate was whether they needed additional staff![565] According to the head of the Banking Supervision Department, Mary Burke, that May she was refused an 'already "self-censored"' request for six more staff so as to established dedicated 2-person teams to inspect AIB, BOI, ILP & Anglo'[566]. She said she had already "self-censored" 'in the knowledge of previous experience in

[555] McDonagh, "Transcript of Brendan McDonagh (NTMA) Hearing," 103.
[556] Carswell, *Anglo Republic*, chap. 10.
[557] Simon Carswell, "Transcript of Simon Carswell Hearing," March 10, 2015, 462.
[558] Irish Independent, "The Political Contacts That Led to Controversy," *Irish Independent*, January 15, 2011.
[559] Carswell, *Anglo Republic*, chap. 10.
[560] Fintan Drury, "Transcript of Fintan Drury Hearing," July 30, 2015, 5.
[561] Cowen, "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," 88.
[562] Bertie Ahern, "Transcript of Bertie Ahern Hearing," July 16, 2015, 119.
[563] Grimes, "Transcript of Tony Grimes (Central Bank) Hearing," 26.
[564] Walsh, "Opening Statement to the Inquiry of Michael Walsh (INBS)," 4; 8 note M.
[565] "Transcript of Mary O'Dea (Financial Regulator) Hearing," 11–12; Mazars, "Towards a 'Best Practice Organisation': Final Report - For Presentation To The Authority," February 2009, 2.
[566] Burke, "Opening Statement to the Banking Inquiry," 4–5.

seeking additional resources' and 'the fact that the CEO had instructed that there would be no increase in staff complement'[567]; in the end she got an increase of 0.4 staff.

April-September: The Golden Circle goes into Overdrive

From April to September, global financial market conditions steadily worsened and interactions between the banks, Central Bank, Financial Regulator, Department of Finance, and the government went into overdrive. Kevin Cardiff, who was then a Second Secretary-General in the Department of Finance and described himself as 'de facto public sector co-ordinator for all the banking interventions reporting to the Secretary General and the Minister obviously, sometimes the Taoiseach'[568] gave the Inquiry a list of financial and political elites who had lobbied either John Hurley of the Central Bank or the Department of Finance for 'a broad legal guarantee' in the months prior to September 2008[569]. They included Charlie McCreevy in May, Davys Stockbrokers in July and in September, Gillian Bowler of ILP, and financier Dermot Desmond, then the fourth richest man in Ireland[570]. The first to ask was the Chairman of Anglo, Sean Fitzpatrick, who Cardiff said had asked John Hurley for a guarantee at the end of April, followed by someone with the initials 'DD' 'a few days later, maybe a week later' who 'suggested the idea of a broad guarantee'. Cardiff said there were two people with a 'substantial presence in the...in the financial sector' who this could have been but claimed he couldn't remember which it was from his notes. Apart from Dermot Desmond, the other obvious candidate would appear to be the CEO of Anglo, David Drumm.

Department of Finance briefings to Cowen dated April 21st, based on updates from the Central Bank, were even more alarming. Warnings were given about tightening of Irish bank lending due to the credit crunch, which 'if it continues long term and spills over into a significant deterioration in the economy and asset quality, it could damage the capital ratios or solvency of the banks'. Speaking notes prepared for Cowen for Cabinet included more reassuring language that the banks were solvent, well capitalised, and in robust health but notwithstanding this wider economic problems could be caused by a lack of credit due to their liquidity issues. However, they also said increased negative sentiment towards the Irish economy had impacted on banks' 'ability to access capital if it were required'.

A few days later on April 24th, a note was prepared for Cowen by Department of Finance officials for a 'meeting with some bankers'. It said the Irish banks were experiencing worse pressures than other banks internationally 'owing to wide-spread international concern regarding the exposure of Irish banks to the property market and in particular commercial lending'. The NTMA's placing of deposits, which had been done again in April at Cardiff's request, was also mentioned. An internal Department of Finance email that day discussed 'the potential for amending the State Guarantee Act 1954 to allow the Minister to provide a guarantee to a financial institution or the CBFSAI should it be required.' That evening Cowen went for dinner with the board of Anglo in their head office. Cowen testified that this was 'a sit down socialising and talking away informally'[571] and gave the following account of the extent to which Anglo's business was discussed:

[567] Ibid., 6.
[568] "Transcript of First Kevin Cardiff Hearing," June 24, 2015, 3.
[569] Ibid., 25.
[570] Sunday Independent, "The Rich List Top 100," *Sunday Independent*, March 30, 2008.
[571] Cowen, "Transcript of Brian Cowen Hearing – Regarding His Role as Former Minister for Finance," 97.

> my recollection is there may have been one of the executives at some stage, it was a very social occasion but at some stage, got up and made some comment about the banks...how their bank was doing and business and all the rest of it and size and all the rest of it but I wasn't ... it wasn't something that I was taking notes on…I didn't intend doing any business, I didn't do any business, and it was a very social occasion…[572]

On July 28th, Cowen who by then had become Taoiseach, spent a day in and around Druids Glen golfing, dining and apparently discussing the general economic situation of the country, but not Anglo, with three Anglo board members and economist, Alan Gray, who Cowen had appointed to the board of the Central Bank. When asked if it stretched credibility that Anglo was not discussed, Cowen answered:

> …If people want to be ... think up a lot of conspiracy theories, I can't stop them, you know, that's the way people are ... is that people want to do that, but I'm here under oath telling the truth. It was about economic issues - it was nothing to do with Anglo Irish Bank at all[573].

Cowen's friend Fintan Drury, who had arranged the outing[574], Sean Fitzpatrick and Gary McGann all backed up Cowen's account that Anglo was not discussed.

Over the summer, preparation of legislation to nationalise a bank continued and briefings to the new Minister for Finance, Brian Lenihan, and the DSG became steadily more alarming. On July 2nd, the Managing Director of AIB ROI, Donal Forde, gave the following account of AIB's lending practices to the Oireachtas Finance Committee:

> In regard to lending standards in AIB, we have behaved very responsibly in recent years and we have maintained a very prudent credit stance… I reassure the committee that we are determined to manage our business in the best interests of our customers and of the continuing development of the economy… AIB will be more resilient than some would like to think through the property cycle… We must have the national interest at heart to serve our own interests.[575]

Over the previous month, AIB's shares had fallen by 22%, with similar falls of 25% for BOI and 27% for Anglo and several Irish banks had been put on negative ratings watch by the ratings agencies indicating they could be downgraded[576]. The escalating crisis prompted attendance at a DSG meeting on July 8th by the acting Governor of the Central Bank, Tony Grimes, the Prudential Director of the Financial Regulator, Con Horan, and Kevin Cardiff. The report of the meeting, received by the Inquiry included the following strong warnings about the severity of the situation:

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572 Ibid., 90.
573 "Transcript of Brian Cowen Hearing – Regarding His Role as Former Taoiseach," 21.
574 Ibid., 20.
575 Oireachtas Committee on Finance, "Banking Sector: Discussion," July 2, 2008, http://oireachtasdebates.oireachtas.ie/Debates%20Authoring/DebatesWebPack.nsf/committeetakes/FIJ2008070200003?opendocument.
576 Department of Finance and William Beausang, "Revised Note for the Information of the Minister for Government Meeting - Financial Market Developments - Following DSG June 19th 2008," June 23, 2008.

> There were some indications that recent falls in share prices reflected share sales by long-term investors, indicating that if the current unfavourable market environment persisted there was an increased risk of a general loss of confidence in the Irish banks.
>
> International investors believed that the sharp slow-down in the Irish economy and property market would give rise to significant loan losses for the Irish banks, a collapse in profitability and the need to raise significant capital…[577]

However, despite all this the Financial Regulator reported that:

> This type of assessment does not correspond with that of the Irish banks. The FR reported a detailed line-by-line examination of its loan book by one of the major Irish banks which highlighted that even allowing for 'worst-case' loan losses, profitability would remain strong measured against objective market benchmarks[578]

When asked about this, Con Horan explained that this had been based on what the banks were telling them. 'I don' think we went in to check at that time', he said.[579]

September 2008

Throughout September, the situation continued to worsen. Two events that accelerated the banks' death spiral were the downgrading of INBS by Moody's on Friday September 5th and the collapse of Lehman Brothers on September 15th. The Moody's report attributed the downgrade to INBS' exposure to commercial property, which made up 80% of its loan book, in a context of plummeting land and property prices in Ireland and the UK[580]. A Reuters story later the same day said INBS was about to be liquidated. In the conventional narrative of the banking collapse, it is usually the 'false Reuters story' rather than the Moody's downgrading that is blamed for the rapid deterioration in the banks' situation after that point. That was certainly the spin put on it by the authorities and INBS, who succeeded in having the story withdrawn after contacting the Regulator to say it was 'totally erroneous'[581]

Crisis meetings were held that weekend with AIB, BOI, INBS, the Department of Finance, Central Bank and Financial Regulator all in attendance. AIB and BOI were there because the Central Bank and Financial Regulator were still hoping to persuade them of the merits of the 'Green Jersey Agenda' and lend €2bn to INBS[582]. In essence, the banks wouldn't touch it with a barge pole unless they were given a guarantee by the Central Bank. As Richie Boucher of BOI put it, 'to be honest, I felt

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577 Department of Finance and William Beausang, "Report of Domestic Standing Group Meeting- 8 July 2008," July 14, 2008.
578 Ibid.
579 Joint Committee of Inquiry into the Banking Crisis, "Transcript of Con Horan (Financial Regulator) Hearing," May 27, 2015, 18–19, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/27052015_Horan_vol1.pdf.
580 Document no. 21 Note to Minister re Mood's downgrade of INBS PAC, "Report on the Crisis in the Domestic Banking Sector: A Preliminary Analysis and a Framework for a Banking Inquiry," July 2012, 217, http://www.oireachtas.ie/parliament/media/committees/pac/PAC-Report---FINAL.pdf.
581 Michael Fingleton, "Transcript of Michael Fingleton Hearing," September 2, 2015, 166, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/09/02092015_Fingleton_vol1.pdf.
582 Cardiff, "Transcript of First Kevin Cardiff Hearing," 14; John Stanley Purcell, "Transcript of John Stanley Purcell (INBS) Hearing," September 2, 2015, 151.

we should get out of the building'[583]. The reason they gave, as recorded in a minute of the meeting by AIB, was that based on a previous review of INBS by BOI, the banks believed 'there was a potential loss on the total asset book of [INBS] of between 30%-50% in the event of sale/liquidation'. So they told the Central Bank/Financial Regulator that: 'it was not a realistic proposition for either institution to provide unsecured funding for an entity that had a hole in its balance sheet which would exceed its reserves'[584]. In other words, they said they wouldn't lend to INBS because it was insolvent. The Regulator reportedly disagreed, countering, presumably based on what INBS was saying, that they thought the write-down would be only 13%.

At this stage, the government and Department of Finance were worried at the lack of hard information on the banks from the Regulator. According to Cardiff,

> we believed...were led to believe that the regulator had a good picture of the banks under its remit, that reasonable loan loss stress testing had been done, that the banks were regarded as solvent, resilient, capable of withstanding significant shocks and we accepted that. And we stopped accepting it at the beginning of September when, when we had the Nationwide issue and it became clear that in fact, this general sense of how the banks were being run wasn't, wasn't being backed up by very specific data.[585]

The obvious dangers of trusting institutions motivated solely by aggressive profit-seeking to regulate themselves – in other words the 'light touch' regulatory approach the government had championed for so long to attract in foreign capital and help Irish banks to compete – had materialised. After years of under-resourcing the Regulator, the state via the NTMA and Department of Finance now scrambled to call in external investment banks to scrutinise the banks' books. Goldman Sachs was hired to look at INBS, and PWC at INBS, ILP and Anglo while the Department of Finance also hired Merrill Lynch and Morgan Stanley as advisers[586]. Like the Regulator, however, they were basically still just relying on whatever information the bank were giving them and by now there was little or no time to do an independent analysis of how much their assets were worth and what it would cost to save them. Patrick Neary told the Inquiry that their findings confirmed information the Regulator already had.

In the following weeks, the focus was on finalising legislation for nationalising banks and extending it to building societies[587], with INBS in mind, as well as legislation to allow the NTMA provide secured lending to the banks[588]. Several banks were also considering various merger arrangements with each other but this was only rearranging deckchairs on the Titanic.

By September 16th, the day after Lehmans collapsed, the board of the Financial Regulator was told that Anglo, ILP and AIB were all on course to breach legal requirements for the amount of liquidity

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[583] Richie Boucher, "Transcript of Richie Boucher (BOI) Hearing," May 6, 2015, 36, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/05/06052015_Boucher_vol1.pdf.
[584] AIB, "AIB Minutes of Meeting with BOI and CB/FR Re Irish Nationwide," September 7, 2008.
[585] Cardiff, "Transcript of First Kevin Cardiff Hearing," 203.
[586] Ibid., 36.
[587] Beausang, "Transcript of William Beausang (Department of Finance) Hearing," 6; McDonagh, "Transcript of Brendan McDonagh (NTMA) Hearing," 8.
[588] McDonagh, "Transcript of Brendan McDonagh (NTMA) Hearing," 8.

they had to hold within the next month. According to the former Director-General of IBEC, John Dunne, by this stage the idea of a blanket guarantee was on the table:

> there was a meeting of the regulator - I believe it was around about 16 September - when various options were discussed, if the deteriorating situation went over the cliff and became, you know, an Armageddon-type situation. And the issue of a guarantee, while not overly stated...overtly stated, was implicitly contained as a result of that meeting[589].

A Background note for Lenihan the next day on Financial Market Developments reminded him that – Irish Stock Exchange had lost almost 50% of its value since February 2007, compared to 18% for the Dow Jones in the US and 18% for the UK FTSE Index. AIB's shares had also fallen by 70% in the same period, BOI's by 75%, and Anglo's by 74% and in the last 2 days AIB was down 15% and Anglo 20%. The financial markets were also pricing in the likelihood of the banks going bust, as credit default swaps for Irish banks had risen 30-37% since September 12th[590]. Meanwhile over at AIB, the board was discussing the group's capital position and an Anglo board meeting was agreeing to contact the Central Bank and Brian Cowen 'to ensure that there is Government support for a workable solution'.

On September 18th, the CEO of INBS, Michael Fingleton, met with the Secretary-General of the Department of Finance, David Doyle, and asked for the limit of the Deposit Guarantee Scheme to be raised[591]. At a meeting later that day between the Department of Finance, NTMA and Financial Regulator, Lenihan agreed to raise the limit from €20,000 to €100,000. In the event of a bank run, this would benefit only corporations and a small minority of the richest in society. At the time, over 90% of AIB and BOI deposits were less than €22,000 and in 2013 the median value of household financial assets, for those that any, was €6,300[592]. That weekend, the Financial Regulator met with the banks about their dire liquidity situation. AIB requested a statement from the Central Bank that no Irish bank creditor would be allowed to lose out – in other words a guarantee of bank liabilities.

On September 21st, Goldman Sachs presented the results of their analysis of INBS to the Department of Finance. It included disclaimers stating that in the limited time available it wasn't possible to provide an official 'Audit of or opinion on [INBS'] financial position'; an 'Independent valuation or appraisal of the assets, collateral and/or liabilities of [INBS] or impairments to be taken; an opinion 'on the adequacy of provisions, capital, risk levels and/or risk management', or 'Provision of investment advice' but it was the best the government had to go on. Notwithstanding this, it went on to provide relatively detailed information on INBS that strongly suggested it was insolvent in the straightforward sense that its assets were now worth less than its liabilities:

- Combining the commercial real estate and residential loan book mark to market exercises results in a highly preliminary loan book valuation range of €4.7bn - €8.1bn

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589 David Begg and John Dunne, "Transcript of David Begg & John Dunne Hearing," July 22, 2015, 14.
590 Department of Finance, "Background Note for Minister for Finance on Financial Market Developments to 17 September 2008," September 17, 2008, ghttp://www.oireachtas.ie/documents/committees30thdail/pac/reports/documentsregruarantee/document16.pdf.
591 Fingleton, "Transcript of Michael Fingleton Hearing," 18.
592 CSO, "Press Release Household Finance and Consumption Survey 2013," html,text,pdf,xls, (January 29, 2015), http://cso.ie/en/newsandevents/pressreleases/2015pressreleases/pressreleasehouseholdfinanceandconsumptionsurvey2013/.

    - This corresponds to 40% - 69% of the loan book carrying value of €11.754[bn] as at 31 August 2008
- This assumes that the commercial real estate marks of 34% - 68% for the top 30 exposures apply to the entire €9.4bn commercial loan book[593]

In other words, if INBS had to sell its assets right then, it would lose €3.6bn- €7bn if the losses on all its loans turned out to be bad as the top 30 were looking at that point. Given INBS had around €1.8bn in regulatory capital that would leave it insolvent by €1.8bn-€5.25bn. The same figures were repeated in Merrill Lynch's initial presentation to the NTMA and Department of Finance on September 26th, which stated 'INBS has €11.7bn of loans...Writedowns of 30% - 60% results in an impairment of €3.6bn - €7bn'. In the event, INBS made losses of €6bn and received a bailout of €5.4bn from the state so Goldman Sachs and Merrill Lynch weren't far off. Their estimates were also very similar to BOI and AIB's at their meeting with the Financial Regulator when they refused to lend to INBS on the basis that they believed 'there was a potential loss on the total asset book of [INBS] of between 30%-50% in the event of sale/liquidation'.

When questioned about Goldman Sachs and Merrill Lynch estimates of INBS losses by Joe Higgins and also asked why he had redacted those figures from the Merrill Lynch presentation when it was originally given to the Public Accounts Committee in 2010, Cardiff replied:

> the mark-to-market value would be quite different from the going concern value for a bank that is in ongoing mode…there was no evidence to suggest that INBS was insolvent at that moment. But, certainly, if it had to sell all of its loans straight away or if market conditions deteriorated over time, they would start to burn through their…first of all, through the whatever profit they were earning [note: INBS made a loss of €280m in 2008], then through their capital and then could eventually fall into a negative capital position. So they were likely at some stage to need capital. Why was the document redacted? It was redacted probably on my judgment for legal reasons or for commercially-sensitive reasons ...sensitivity reasons[594].

That INBS 'were likely at some stage to need capital' from the state because they were insolvent is also reflected a few pages later on in the Goldman Sachs presentation. Under the heading 'Financing Package Parameters' and the subheading 'Regulatory Capital' , 'State support… structured as subordinated debt/preference share to bolster capital position' is mentioned, followed by a bullet point that 'Subsequent capital support may be politically sensitive (see NR [Northern Rock] capital requirement of up to €3bn by UK government in August)'[595]. All the above information suggests the state knew or had very very strong reason to suspect before they guaranteed INBS that a) it was insolvent in the sense that its assets were worth less than its liabilities at that point (on a mark-to-market basis) and b) that it would be insolvent in a regulatory sense in the relatively near future and so would need capital from the state to survive. Moreover, it had been given this information by AIB, BOI, Goldman Sachs and Merrill Lynch. That they might also have had similar suspicions about Anglo is suggested by a famous minute of a meeting of the Financial Regulator, Merrill Lynch, Central Bank, PwC, Arthur Cox, the Attorney General, the Taoiseach, Department of Taoiseach, Minister for

[593] Goldman Sachs, "Discussion Materials Regarding Strategic Options: Draft Working Paper," September 21, 2008, 26.
[594] Cardiff, "Transcript of Second Kevin Cardiff Hearing," 70–71.
[595] Goldman Sachs, "Discussion Materials Regarding Strategic Options: Draft Working Paper," 29.

Finance, Department of Finance, NTMA and Goldman Sachs on September 25th. After a note of Patrick Neary saying, 'there is no evidence to suggest Anglo is insolvent on a going concern basis - it is simply unable to continue on the current basis from a liquidity point of view. He felt INBS was in a similar situation' , it reads:

> D Doyle noted that Government would need a good idea of the potential loss exposures within Anglo and INBS - on some assumptions INBS could be 2bn after capital and Anglo could be 8½[596]

All concerned who were asked about it either said they didn't remember that being said or offered some other explanation of why it meant something other than what it says on the face of it. A further warning to the government about Anglo's potential insolvency was given on the night of the guarantee itself. AIB apparently advised against including a sentence in the public announcement of the Guarantee the next morning saying that all the banks were insolvent, on the grounds it was 'possibly dangerous in the sense that Anglo shares would be traded on foot of it, which could lead to complications for the Government.'[597]

Notwithstanding all this, the minutes of a Central Bank board meeting on September 21st show the board endorsing the general view that 'Unless the market situation were to improve and banks regained their ability to borrow on the money markets, the necessity of the Government giving an explicit guarantee for banking liabilities would have to be considered'[598]. The following week was filled with crisis meetings during which opinion in the upper echelons of the state progressively congealed towards the most drastic of solutions – a blanket guarantee for the €440bn[599] worth of liabilities across the Irish banking system. By September 25th, the Central Bank board had agreed that 'A key policy issue for the weekend was whether or not the Government should issue a formal guarantee for the liabilities of the six banks' and that 'the issue of an explicit Government Guarantee supported by a willingness to supply additional funding, if necessary, warranted detailed consideration'. One of the key supporters of this approach on the Central Bank appears to have been Alan Gray, who wrote to Kevin Cardiff after the board meeting advocating it[600]. Gray also received a surprise visit from Anglo's David Drumm and Sean FitzPatrick on the day of the Guarantee itself but insisted that "[N]o one from Anglo has ever asked me to take action on their behalf or to make representations on their behalf"[601]. Governor Hurley was also said to have 'advised the meeting that an explicit Guarantee for the State for the over €400 billion liabilities…was not something that he would have favoured up to now but, in the evolving situation, it required serious consideration'[602]. It was also noted that AIB and BOI 'to date had been negative on such a proposal but their views…might be changing in view of the increasing liquidity pressure on them as well'. This was a

[596] Department of Finance, "Transcript of Handwritten Note of Meeting with Financial Regulator, Merrill Lynch, Central Bank, PwC, Arthur Cox, Attorney General, Taoiseach, Department of Taoiseach, Minister for Finance, Department of Finance, NTMA, Goldman Sachs (for Part) Thursday 25/09/2008," September 25, 2008.
[597] Dermot Gleeson quoted in "Transcript of Neary Hearing," 80.
[598] quoted in "Further Material of Clarification David Doyle," October 23, 2015, 4, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/10/Further-Material-of-Clarification-David-Doyle.pdf.
[599] Patrick Honohan, "Transcript of First Honohan Hearing," January 15, 2015, 111.
[600] Alan Gray, "Letter from Mr Alan Gray to Kevin Cardiff Re Contingency Planning," September 25, 2008.
[601] "Transcript of Alan Gray Hearing," September 9, 2015, 97–98.
[602] quoted in "Further Material of Clarification David Doyle," 7.

reference to the fact that AIB and BOI wanted a guarantee for themselves but would have been quite happy for Anglo and INBS to be taken out.

It appears it was only on the night of the Guarantee itself that the final was decision was taken to guarantee all six banks and not to leave the more obviously insolvent banks, i.e. INBS and Anglo, out. However, given the main alternative being considered was sacrificial nationalisation that would have also put the state on the hook for their losses, it's unclear how much difference this would have made to the final cost. This was certainly how Cowen saw it, saying during his hearing: 'if it's insolvent, what do you do with it?...If you nationalise it you're taking on all the liabilities there and then anyway. So now you're taking on the losses'[603] Either way, the state was going to bail out the banks no matter what the cost.

That it was known this would have a very severe impact on the public finances is evident from an email sent from Brendan McDonagh of the NTMA to the Department of Finance on September 26th. McDonagh was asked for 'an analysis of the impact on the state's credit rating of a broad guarantee for all deposits/credits of all banks plus having to provide say €100bn in funding as estimated by ML just for institutions to be brought into "protection"'. McDonagh responded : 'we expect to be put immediately on negative watch and probably soon after be downgraded, how many notches from AAA we just don't know.' He also said it would increase the interest rate on Ireland's borrowing by at least 1%, at a time when a large fiscal deficit was emerging due to the collapse of the property/credit bubble. Merrill Lynch's advice was similar. A minute of an initial meeting on September 26th shows they said a blanket guarantee 'could be a mistake and hit national rating and allow poorer banks to continue'[604].

On the famous night of the Guarantee itself, the economic predominance and political pre-eminence of finance capital was played out behind closed doors as the interests of the banks became exactly, identically conflated with those of the state. In this moment of crisis, the needs of the banks became equated with those of the financial system and the wider capitalist economy. That's also why the two main banks – AIB and BOI – were largely responsible for the content of the guarantee in terms of the liabilities covered. Dermot Gleeson's note of the night, which he wrote a few days later, refers to an initial draft of the guarantee having been provided '(I think by Bank of Ireland)' and goes on to say:

> We furnished a more extensive formula (which we had brought with us) as to the sort of instruments and deposits that should be covered. (This formula was eventually adopted later in the night pretty well word for word).[605]

Various witnesses confirmed that the banks had suggested a wording for the guarantee but insisted the final decision had been the government's – as of course nominally it was. Both banks said they could not find a copy of their draft guarantee to give to the Inquiry.

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[603] "Transcript of Brian Cowen Hearing – Regarding His Role as Former Taoiseach," 59.
[604] Department of Finance, "Transcript of Handwritten Note of Meeting with Minister, Merrill Lynch, Central Bank, Financial Regulator and Department of Finance, 26 September 2008," September 26, 2008.
[605] quoted in "Transcript of Dermot Gleeson (AIB) Hearing," April 23, 2015, 115–166, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/04/23042015_Gleeson_vol1.pdf.

For AIB and BOI, the outcome was less fruitful in relation to the inclusion in the Guarantee of their erstwhile competitors, INBS and especially Anglo – which now rather than being held up as a model of aggressive capitalist growth had mutated into a walking corpse that everyone, apart from the Irish state, wanted to get as far away from as possible. Aside from 'saving' every last bank, no matter how big or how small, the only other consideration on the night appears to have been how this would be viewed by the global financial markets. Yet again, the goal was to restore 'confidence' and appease the gods of the markets – whatever the cost in human sacrifice and misery over the years to come.

Chapter 6 – After the Guarantee: the Cost of the Crisis

At the stroke of a pen, the Guarantee put the state on the hook for €440bn[606] worth of Irish bank liabilities. The consequences of that decision – and the determination of successive governments to honour it so as to protect Ireland's 'reputation' as a safe haven for capital – have shaped our economic and political destiny ever since. For the banks and the financial speculators, it meant the bondholders, who lend banks their capital on a longer-term basis, got a two-year Guarantee. According to Honohan, three-quarters of the bondholders in 2008 were non-residents[607] so the Guarantee meant foreign investors, on which Irish banks like the Irish economy, are completely dependent, would get their money back.

This was just one element of the neo-colonial financial relationship between the major EU states, the ECB and Ireland that had long existed beneath the surface of the bubble but burst out into the open once it bust. By September 2008, the Irish banks had also built up debts to the ECB of roughly €50bn in Eurosystem funding (Figure 5.1), which over the course of the crisis had gradually placed much of the private wholesale funding that had previously plugged the giant gap between the banks' deposits and their bloated loan books. The Guarantee was supposed to encourage the wholesale markets to resume lending these funds to the Irish banks. However, many such investors baulked at the huge liability the Guarantee had placed on the state and assumed that at some stage Ireland would have to default. As a result, the banks and through them the state gradually became more and more dependent on ECB and ELA funding, which peaked November 2010 at an incredible €140bn – 85% of Ireland's GDP[608]. At the point, Trichet threatened to pull the plug unless Ireland entered the Troika bailout and borrowed enough money from the ECB-IMF to pay back all the money the banks had borrowed from the ECB[609].

As explained in Chapter 2, in terms of the asset/loan side of the banks' balance sheets, by far the most problematic part of the Guarantee was the €158bn[610] in commercial property loans, which caused the vast majority of the banks' losses. That's why in guaranteeing the banks, the government was also socialising the private debts of Irish developers. In effect, all the resources and future tax revenues of the state were put up as collateral for their loans if they defaulted – which they did, over and over again. By September 2012, only 17% of the €74bn in commercial property loans transferred to NAMA were performing. This is almost the exact inverse of the peak rate of arrears on owner-occupier mortgages of 12.9% in September 2013[611], which unlike the debts of the rich are almost always repaid by the original borrower. Socialising these developers' loans by guaranteeing the banks destroyed the economy and we've been paying the price ever since[612]. This chapter attempts to count it.

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[606] Patrick Honohan, "Transcript of First Honohan Hearing," January 15, 2015, 111.
[607] Patrick Honohan, "The Irish Banking Crisis: Regulatory and Financial Stability Policy 2003-2008," May 31, 2010, 150.
[608] Jean-Claude Trichet, "Transcript of Jean-Claude Trichet Hearing," April 30, 2015, 33.
[609] Trichet, "Transcript of Jean-Claude Trichet Hearing."
[610] Brendan McDonagh, "NAMA Update," 2014, 5.
[611] Central Bank, "Residential Mortgage Arrears and Repossessions Statistics: Q2 2015," Other, *Financial Regulator*, (September 2, 2015), 2, http://www.centralbank.ie/press-area/press-releases/Pages/ResidentialMortgageArrearsandRepossessionsStatisticsQ42014.aspx.
[612] As of June 2015, AIB still had €13.8bn in commercial property loans, just under half of which is impaired. AIB, "Half Yearly Financial Report 2015," August 6, 2015, 65; 70,

NAMA

The establishment of NAMA in 2009-2010 copper-fastened the state's commitment to bailing out the banks, the developers and the ECB all at once. The €32bn NAMA paid for the €74bn in commercial property loans it took over from the banks were 'paid' for with NAMA bonds, essentially IOUs from the state to the banks that they could use as collateral to borrow from the ECB. As Michael Somers explained in his cringe-inducing introduction to Trichet's 'non-appearance' at the Inquiry[613], this arrangement had received the blessing of ECB President Jean-Claude Trichet in advance after Somers went out to Europe to ask his permission. 'Jean-Claude has always been a good friend to us', he simpered. The €32bn in NAMA bonds contributed significantly to the €140bn in debts run up by the Irish banks to the ECB by November 2010 and so played a role in bouncing Ireland into the bailout.

The immediate effect on the balance sheets of the banks was to crystallise losses of €42bn which were compensated for through a series of bank recapitalisations that in the end amounted to €64bn – so just the developers' loans in NAMA accounted for around two-thirds of the direct cost of the bank bailout. Given NAMA is now forecasting a 'profit' of €2bn over the €32bn it paid for the loans, this will leave an overall loss of €40bn for the state and everyone living in it. By the time it's wound up, developers will either have had their part of this €40bn written off, or else their loans will have been sold on at a discount to mainly US vulture funds who have bought 90% of NAMA's property portfolio[614]. Either way, the state loses out.

When NAMA was set up, the Minister for Finance, Brian Lenihan promised that there would be no debt forgiveness for developers, that they would be pursued for the full book value of their loans – not the price NAMA paid for them, and that they would not be allowed to buy their own loans back at a discount. NAMA also repeatedly insisted this would be the case[615] but then in January 2014 said it might sell loans back to developers eventually but 'any move in that direction would have to be carefully considered and public opinion gauged.'[616] Now that there's an acute housing crisis as a result of the collapse of the property market and land hoarding by NAMA until prices rise probably seems like an opportune time for this to be broken to the public – on the spurious grounds that all these developers who anywhere else in the world would be bankrupt are the only ones with the nous to kick-start the construction of housing.

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https://investorrelations.aib.ie/content/dam/aib/investorrelations/docs/resultscentre/resultspresentation/aib-half-yearly-financial-report-2015.pdf. Ibid., 71. BOI still has €15bn in commercial property loans (compared to €34bn in 2009), 45% of which is impaired BOI, "Interim Report For the Six Months Ended 30 June 2015," July 31, 2015, 56–57, https://www.bankofireland.com/fs/doc/publications/investor-relations/boi-interim-report-2015.pdf.
It wrote off over €4bn in commercial property losses from January 2014-end June 2015

[613] This was hosted by

[614] Minister for Finance, "NAMA Assets Sale: Written Answer No. 27," *Kildarestreet.com*, February 4, 2015, 27, https://www.kildarestreet.com/wrans/?id=2015-02-04a.56.

[615] Gavan Reilly, "NAMA Chairman Denies Builders Can Buy Back Their Properties Cheaply," *Business ETC*, June 14, 2011, http://businessetc.thejournal.ie/builders-trying-to-buy-their-nama-properties-at-knockdown-prices-155271-Jun2011/; Newstalk, "NAMA Says It Has Not Sold Back Any Loans to Defaulting Debtors," *Newstalk.com*, December 20, 2013, http://www.newstalk.com/reader/47.301/18459/0/.

[616] Catherine Shanahan, "Nama May Reverse Ban on Loan Buy-Backs," *Irish Examiner*, January 18, 2014, http://www.irishexaminer.com/ireland/nama-may-reverse-ban-on-loan-buy-backs-255686.html.

During his hearing, the CEO of NAMA, Brendan McDonagh, admitted that the vast majority of its debtors will never repay their debts and that 'less than five' of the original 772 debtors had repaid their debts up to that point. Despite this, 140 of the original 180 'large debtors'[617] have already exited NAMA, meaning many large debtors must already have had some of their debts written off from the taxpayer's perspective . The way NAMA is getting around recognising this as a write-down for developers is by selling the loans on to vulture funds at a knockdown price, so that in theory the developer still owes the full amount to the vulture fund and hasn't been given a write-down. In practice though, the state still loses the money and at least some developers have then bought their loans back off the vulture fund. An example is one of the biggest developers to have exited NAMA, Michael O'Flynn, who reportedly had his €1.8bn in loans sold on by NAMA to Blackstone, a vulture fund, for €1.1bn, leaving a €700m loss to the state[618]. O'Flynn has reportedly since made a deal with Blackstone to buy back some of the loans and get out of the rest of his debts[619].

Unfortunately, we have no way of knowing the extent to which this is taking place as NAMA operates under a veil of client confidentiality that runs directly counter to the public interest. As with IBRC, it's past time for a full public Inquiry into NAMA, untrammelled by confidentiality for its developer customers who have cost us billions, in order to establish who exactly is being bailed out at our expense and for how much. This would also allow a proper accounting of how much losses each bank has been responsible for. Both Anglo and INBS claimed to the Inquiry that they were responsible for less of the losses on the loans transferred to NAMA than the high 'haircuts' imposed on their loans would suggest. We have no way of verifying this because of the clandestine way in which NAMA has bundled together loans from different banks and then sold them off in large portfolios in which the price paid for individual assets is virtually impossible to determine. It also appears that developers who didn't go bankrupt as a result of being kept alive on the life support of NAMA can write off their losses during the crash against future profits and corporation tax liabilities – as can the banks – so we end up paying for their losses twice: once by bailing out the banks or writing off their loans and twice by writing off their future tax liabilities against losses that were actually suffered by the state, not the banks or developers. On top of all this, NAMA has been paying developers €11 million a year in wages[620].

The other side of the NAMA scandal is that since 2011 NAMA has been handing over billions of euro in cash to the banks and through them to the ECB throughout the worst depression in the history of the state. According to the Chair of NAMA, Frank Daly's opening statement, as of April 2015, NAMA had 'generated €25 billion cash', including 'nearly €20 billion' from 'asset and loan sales' and '€5 billion in non-disposal, mainly rental, income'[621] . It had given €17.6bn[622] of this to the banks in cash

[617] PAC, "Public Accounts Committee: National Asset Management Agency Financial Statements 2013," December 18, 2014, https://www.kildarestreet.com/committees/?id=2014-12-18a.56&s=NAMA#g688.
[618] John McManus, "Does Nama Pragmatism Mean Developer Bailouts?," *Irish Times*, May 19, 2014, sec. Finance.
[619] Jack Horgan-Jones, "O'Flynn Poised to Escape Blackstone Deal Will Sever Ties with Vulture Fund," *Sunday Business Post*, September 20, 2015, http://www.businesspost.ie/#!story/Home/News/O%E2%80%99Flynn+poised+to+escape+Blackstone+Deal+will+sever+ties+with+vulture+fund/id/c23873f5-fbba-408a-8ad8-603a0a513d64.
[620] Jack Horgan-Jones, "Nama Pays Developers €11 Million Every Year in Wages," *TheJournal.ie*, May 29, 2014, http://www.thejournal.ie/nama-pay-levels-developers-11-million-1491461-May2014/.
[621] Frank Daly, "Opening Statement by Mr. Frank Daly, Chairman of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," April 22, 2015, 8.

to redeem NAMA bonds. On top of this, it's also paid the banks interest on the NAMA bonds. At the time of his appearance, this left €14.3bn of the original bonds left to be paid plus interest - money that the state would have as income or land and property that the state could use to solve the housing crisis, if we weren't giving it to the banks to pay off bondholders and the ECB. In 2014, NAMA gave €6.5bn in cash to AIB and €1.6bn to BOI. This is effectively another form of debt service. According to David Duffy, the CEO of AIB, it was still using most of the €6.5bn NAMA cash it got last year to pay back the ECB[623].

Adding the NAMA bond cash given to AIB and BOI last year to the €8.2bn in official debt service doubles the total debt service for 2014 to €16.3bn – more than four times what the state plans to invest in social housing over the six years from 2015-2020. €3.7bn of the €31.8bn NAMA paid for the loans was for completed residential property in Ireland[624], amounting to around 15,000 residential units[625]. But by the end of 2015, NAMA will have offered only 6,000 units for social housing. Only 2,000 have been deemed acceptable by the councils[626].The rest are being rented out at the currently extortionate market rates. NAMA remains by far the largest land and property owner in the state. It owns/has an interest in around a third of development land in Dublin so changing its remit to solving the housing crisis – rather than contributing it by hoarding land to drive up property prices – could make a huge difference.

The Troika Bailout & Not Burning the Bondholders

The Troika bailout in November 2010 was the final stage in socialising €65bn in private banking debt, at the cost of vicious austerity and attacks on living standards. During Trichet's non-hearing, Joe Higgins tackled him on the undemocratic way in which the ECB threatened to cut off funding the banks unless Ireland entered an EU-IMF programme and imposed austerity:

> In your letter then to the Minister for Finance on the 19th November you said "It is the position of the Governing Council that it is only if we receive in writing a commitment from the Irish Government, vis-à-vis the Eurosystem on ... four ... points that we can authorise further provision of [emergency liquidity]." And then you say that a request must be sent to the Eurogroup. "The request shall include the commitment to undertake decisive actions in the areas of fiscal consolidation, structural reforms and financial sector restructuring." , what we call savage austerity in Ireland. Mr. Trichet, plain people, plain-speaking people in Ireland would call that blackmail. Would they be justified?

Trichet's patronising, imperial response emphasised the common purpose he had shared with Brian Lenihan in imposing misery on working people to bail out Irish and European banks:

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622 Ibid., 13.
623 David Duffy, "29042015_Duffy_vol1.pdf," April 29, 2015, 93, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/04/29042015_Duffy_vol1.pdf.
624 Comptroller and Auditor General, "National Asset Management Agency Management of Loans," February 2012, 34, http://edepositireland.ie/handle/2262/69735.
625 Ciarán Hancock, "Can Nama Help Solve the Housing Crisis?," *Irish Times*, December 9, 2014, http://www.irishtimes.com/opinion/can-nama-help-solve-the-housing-crisis-1.2030287.
626 Daly, "Opening Statement by Mr. Frank Daly, Chairman of NAMA to the Joint Committee of Inquiry into the Banking Crisis, Wednesday, 22 April 2015," 11.

> Sir, we had helped Ireland more than any other country. It seems to me that there is something which is missed here. We were the institution which was helping Ireland much more than any other central bank did for any country…
>
> Second, what is not clear enough in your observation is that the relationship with Brian [Lenihan] was extraordinarily confident. Brian knew that we were helping Ireland more than any other country, we had a lot of discussion on that. He was thanking me for the help he received. And he was in favour, of course, of a recovery programme, of a good plan that would permit to put Ireland back on its feet…We were together on the same side, trying to get out of a situation which was, unfortunately, the most dramatic you could imagine… We are in a situation were you get out of that, remarkably well…

Joe Higgins pressed Trichet on whether he had 'saving' the Irish people or saving the bondholders:

> The question Mr. Trichet is, were you there to save the Irish people or were you primarily interested in saving the big European bankers who were heavily exposed in Ireland? And up to 2008, capitalist European bankers and bondholders, as you know, gambled wildly and speculated on commercial and residential property. And created a huge bubble in pursuit of super profits. Now that is what capitalists do in the financial markets. But when their gambles crashed Mr. Trichet, how do you justify placing their massive burden of private debt, private debt, onto the shoulders of the Irish people who had no hand, act or part in their dealings? How do you justify the taking of €60 billion from the public services and the living standards of our people, putting them into the European financial markets? How do you justify that morally?

Trichet's response was essentially that there is no place for morality in a capitalist crisis:

> the question is asked to all governments the world over and particularly to all, I would say, advanced economies. Because we are speaking of a crisis of the advanced economies, which started in New York, as you know with the sub-prime and with Lehman Brothers. And that has happened everywhere and I fully agree with you. This speculation was totally unleashed, Ireland was very unfortunately a case in point…[627]

For all his apparent sympathy here for 'Ireland's' misfortune – which in reality is the same misfortune as that of working people across Europe and the US who were also shackled with debts bankers and developers – Trichet was a merciless opponent of any of the feeble efforts of two Irish governments to burn the bondholders. The Inquiry examined two main points in time at which this was attempted – firstly by the Fianna Fail-Green government at the time of the Troika bailout and secondly by the current Fine Gael-Labour coalition in March 2011. Both were given short shrift given the subordinate position of Irish elites in an international context. What happened to Michael Noonan when he tried to burn the bondholders shortly after coming to office was an object lesson in 'democracy', EU-style. During his hearing, Joe Higgins reminded Noonan how prior to assuming office, he had been 'highly critical of the bailout package, the troika package and, in particular, the lack of burden sharing with bondholders, more popularly referred to as burning bondholders' and then asked him to explain how his own efforts to do this had come so dramatically a cropper.

[627] Trichet, "Transcript of Jean-Claude Trichet Hearing," 36–38.

Noonan explained how he had intended burning €3.7bn of senior bonds left in Anglo and INBS. This was already a considerable lowering of sights given the NTMA had earlier proposed burning €9bn in senior bonds[628] but it still wasn't low enough for the ECB. Despite a prior Cabinet decision to attempt burden sharing, shortly before Noonan was due to announce it in the Dáil on March 31st 2011, he told Joe Higgins that he received a phone call from an angry Jean-Claude Trichet:

> What happened then was that the word got out at Frankfurt that we were thinking of doing this. The statement you read out there I had in my first or in one of the drafts of the speech ... in the draft that I was about to deliver to Dáil Éireann on 31 March. And you'll note it particularly said that I would introduce legislation to achieve the purpose of bond burning…
>
> So I am preparing to go to the Dáil and I get a call from Mr. Trichet and he asks me what are we doing and I told him that we were recapitalising the banks in accordance with the results of the stress testing that had been done…I told him that as part of the programme, we were burning bondholders and he didn't agree. He didn't agree and he asked me was I aware that this would be treated by the markets as a default, which was reasonably strong pressure…ELA, emergency liquidity assistance, was underpinning Anglo to the tune of €41 billion at that time. ELA can't be given to a bank that defaults

Noonan claimed that he initially attempted to resist Trichet's threats, recounting that 'I said well, I was still burning bondholders and it was Government... I had the authority of the Government to do so'. However, at the point Trichet played what from the government's point of view was a trump card by threatening the future of the precious little tax and regulatory haven that had already caused us so much trouble down in the IFSC. According to Noonan,

> he raised the question of the financial services industry in Ireland and particularly in Dublin and he suggested that even though he couldn't say categorically, it might not be possible for people in the financial services in Ireland, particularly in Dublin, to finance themselves on the market if they were situated in a country that was in default. So that was reasonable pressure as well. So I don't think he mentioned the bomb going off until the second telephone call. At that stage...I think at that stage, I said I have to consult with the Taoiseach so the call was discontinued and I informed the Taoiseach of the difficulty of carrying out what was the clear request of the Government but I was exploring the possibility, which was what was in mind. So after some time, I rang him back and I said we were still disposed to burn the bondholders and he said...he was...it's hard to know, like...English isn't his vernacular, you know. He sounded irate but----- He sounded irate but maybe he wasn't irate but that's the way he sounded and he said if you do that, a bomb will go off and it won't be here, it'll be in Dublin.

Noonan then pointed out that Trichet had denied saying this during his non-appearance before going to explain what had really got to him was Trichet's threat to the IFSC:

> I mean there were three issues that were recited to me. First of all, we'd be in default…Then he kind of ... he rattled me because I didn't expect it. He drew the Irish financial services sector into it and particularly the IFSC in Dublin and the possibility that they couldn't be

[628] John Corrigan, "Transcript of John Corrigan (NTMA) Hearing," July 15, 2015, 17.

> funded if they were in a country that had defaulted and then I think the third suggestion about the bomb going off was mainly in the second phone call but I mean it was a fairly strong argument.

Noonan said at that point he decided 'the risk was too high for the amount of gain that was involved and I changed my script and did not promise burden-sharing in the Dáil'. However, he was unwilling to acknowledge that what happened was a blatant subversion of democracy by the ECB given the Irish people had only recently voted Fine Gael and Labour into office on the back of election promises of 'not another cent' for the banks and the bondholders by Fine Gael[629] and 'Labour's Way or Frankfurt's Way'. In endeavouring to burn €3.7bn in senior bonds, at the same time as the government was putting another €16.5bn in recapitalisation into the banks and on the same day as the first €3bn payment was made on the Anglo promissory note, Noonan was therefore trying to save the government some face and avoid it being completely humiliated within its first month in office. Joe Higgins pressed him on the anti-democratic aspects of what occurred:

> So you, a representative of a Government that is supposed to be sovereign, on your way to report to a Parliament that is supposed to be sovereign about a Government decision to burn bondholders in a failed institution and that, on your way, the president, an unelected financial official of the European Central Bank threatened devastating economic consequences, including a default, and as you said, the most serious economic impactful events if you proceeded to carry out a decision that had been that had been made ... Mr. Noonan, is that not a really serious subversion of democratic rights----- by an official of the European Central Bank? And, Mr. Noonan, why did you not immediately report this to the national Parliament, to the Dáil, when you came in?

There then ensued a bizarre and frankly rather pathetic attempt by Noonan to pretend Trichet's series of threats, culminating in a reference to a 'bomb going off' were not actually threats because he hadn't actually used the word 'threat':

> Deputy Michael Noonan: Well, first of all, the word "threat" was never used either by myself or Mr. Trichet, and it was a conversation which was a reasonable conversation, and from his perspective, he seemed to think he was simply pointing out facts to me.
>
> Deputy Joe Higgins: He used the word "bomb".
>
> Deputy Michael Noonan: Yes, he was pointing out facts as far as he was concerned. So I don't want to exaggerate this, either the tone…
>
> ….
>
> Deputy Joe Higgins: Yes, I understand that…I understand the word wasn't used, but the word "bombs" was used-----
>
> Deputy Michael Noonan: Oh yes-----
>
> Deputy Joe Higgins: -----which does imply a threat, I would suggest.

[629] Irish Examiner, "Not a Cent More for the Banks, Vows FG," February 11, 2011, http://www.irishexaminer.com/ireland/not-a-cent-more-for-the-banks-vows-fg-144826.html.

> Deputy Michael Noonan: -----"bomb". The word "economic" wasn't used.
>
> Deputy Joe Higgins: Yes.
>
> Deputy Michael Noonan: And it was "bomb" singular not plural.[630]

The Cost of the Banking Crisis

Brendan McDonagh of NAMA has estimated the total loss of liquidity to the banking system in 2008 at €100bn[631]. Taken together, the €64bn cost of the bank bailout[632] and the €31.8bn in NAMA bonds given to the banks amounts to just under €96bn, suggesting that the state in effect took over responsibility for almost all of the funding lost by the bank during the Global Financial Crisis. There is a similar symmetry between the €64bn lost by the banks from 2008-2013 and the €64bn bank bailout. In his evidence to the Inquiry, Honohan estimated the eventual direct cost of the banking crisis at €40bn, taking into account bank levies, guarantee fees, and sales of bank shares to date but excluding the€2bn anticipated 'profit' from NAMA and any 'profit' from the liquidation of IBRC[633]. However, it also includes the current value of the government's shareholding in AIB and PTSB. This is yet to yield any benefit to the majority in society given both nationalised banks have continued to be run as though they were private enterprises, scalping their customers on interest rates and charges as before, hounding ordinary mortgage-holders in arrears and increasingly repossessing people's homes now that property prices are rising again.

According to Honohan, this:

> net figure is about the same as the aggregate haircut on the NAMA purchases of property-related loans: had there been no losses on those, the net fiscal cost of the assumption of banking liabilities would have been small. In other words, the main banks had enough pre-crisis capital (€28 bn between the top two) to absorb the actual and prospective losses on residential mortgages'.

In terms of the national debt, the bank bailout added €64bn to the national/ general government debt. Of this €43bn was added directly from bank recapitalisations and the promissory notes, while another €21bn was taken from the National Pension Reserve, meaning it was unavailable to reduce the amount of borrowing to plug the fiscal deficit that arose as a result of the bursting of the property and banking bubble. According to Brendan McDonagh, had that money been left where it was it would have increased by about 50% by now, adding approximately an additional €10bn to the cost of the banking collapse[634].

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630 Michael Noonan, "Transcript of Michael Noonan Hearing," September 10, 2015, 81–90, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/09/10092015_Noonan_vol1.pdf.
631 McDonagh, "NAMA Update," 7.
632 Public Accounts Committee, "Report on the Crisis in the Domestic Banking Sector: A Preliminary Analysis and a Framework for a Banking Inquiry," July 2012, http://www.oireachtas.ie/parliament/media/committees/pac/PAC-Report---FINAL.pdf.
633 Patrick Honohan, "STATEMENT BY PATRICK HONOHAN TO THE BANKING INQUIRY 'Nexus Phase,'" May 28, 2015, 8.
634 Brendan McDonagh, "Transcript of Brendan McDonagh (NTMA) Hearing," July 9, 2015, 97, https://inquiries.oireachtas.ie/banking/wp-content/uploads/2015/07/09072015_BrendanMcDonagh_vol1.pdf.

Another way of examining the cost of the crisis is to take into account the wider cost of the property and banking collapse in terms of the total extra borrowing since relative to 2007 levels. Total new borrowing by the government from 2008-2013 amounted to €136bn whereas if it had remained at the 2007 level of €1.6bn, only €9.6bn would have been borrowed over the period. This amounts to total new borrowing as a result of the property and banking collapse of €126bn; or it we add in the original NAMA 'contingent liability' of €32bn, an effective increase in total sovereign debt of around €158bn. On top of this, borrowing costs also significantly increased as a result of this massive increase in the debt stock. This additional debt stock (excluding NAMA) has incurred nearly €30 billion in *additional* debt service[635]. Even under the government's own 'optimistic' projections, the debt to GDP ratio will still be over 75% by 2021[636].

Austerity

This massive burden of debt has been supported by the imposition of vicious austerity for the last seven years, which is set to become permanent as the government has no intention of restoring the level of public investment needed to compensate for years of cuts and solve the multiple crises that have emerged across the public services. In his opening statement for his third appearance at the Inquiry, in calculating the 'Net cost of Government assumption of banking liabilities' p. 8, Honohan stated that 'Comparing tax and spending policies now with those in 2008, cumulative "austerity" savings of about €150 billion have been put in place. This sum continues to grow at close to €30 billion per annum'[637]. This gives a sense of the scale of the cost of the banking crisis for ordinary people but to really understand what it has meant requires explaining where all those cuts have come from.

According to CSO figures, from 2009-2014 nearly €34 billion[638] was cut from public capital expenditure on public infrastructure like roads, flood defences, council housing, hospitals and schools. By the end of 2015[639],'Voted public capital expenditure', doled out to government departments in the Budget each year, will have been cut by nearly €30 billion. On an annual basis, public investment was just under €10 billion in 2008, or 5.2% of GDP. In 2014, it was €3.75 billion[640] or 2%[641] – the third lowest in the EU.

Not surprisingly the public services that suffered the worst cuts are suffering the most now. Since 2008, €11.4 billion has been cut from public capital spending on housing[642], which together with the collapse in private investment as result of the bursting of the bubble is the reason why we now have a housing crisis. In 2008, there was €2.3bn in public investment in housing. According to the

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635 From 2008-2015 estimated.

636 NTMA, "Debt Projections," October 2015, http://www.ntma.ie/business-areas/funding-and-debt-management/debt-profile/debt-projections/.

637 Honohan, "STATEMENT BY PATRICK HONOHAN TO THE BANKING INQUIRY 'Nexus Phase,'" 8 n18.

638 Table 21 Receipts and Expenditure of Central and Local Government by Item and Year : Capital expenditure - Gross physical capital formation http://www.cso.ie/px/pxeirestat/Statire/SelectVarVal/saveselections.asp

639 Based on forecast in End-November 2015 Exchequer Returns, relative to 2008 levels of voted capital expenditure.

640 Table 21 Receipts and Expenditure of Central and Local Government by Item and Year : Capital expenditure - Gross physical capital formation http://www.cso.ie/px/pxeirestat/Statire/SelectVarVal/saveselections.asp

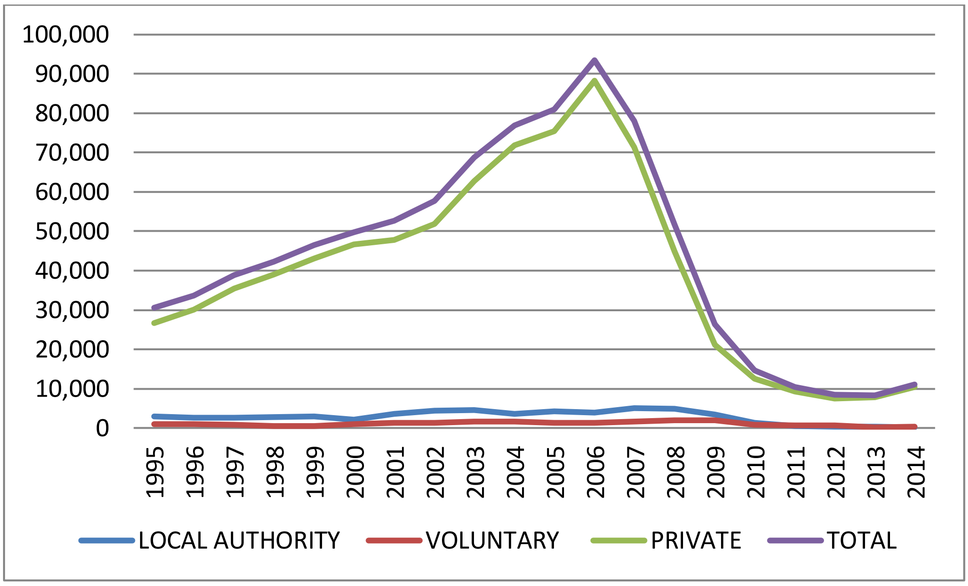
641 Eurostat statistics on General government gross fixed capital formation % of GDP http://ec.europa.eu/eurostat/web/products-datasets/-/tec00022

642 Department of Environment statistics for Public Capital Expenditure on Housing; Department of Finance, "Revised Estimates 2015," December 18, 2014.

Estimates for 2015, last year it was only €376 million and by 2021 the annual capital spend will still be only €400m(according the government's capital spending plan for the next 6 years).

We can see the effect on the ground in the collapse of house building. 93,419 houses were built in 2006, including 4,905 council houses and 1,896 voluntary homes built in 2008. In the first eleven months of last year only 11,314 were built[643]; including a pathetic 28 council homes and 218 voluntary homes in the first 9 months. If we had kept building at 2008 rates, 40,806 council/voluntary homes would have been built by the end of 2015, instead only 11,365[644] were built so austerity has cost us nearly 30,000 council/voluntary homes. In this context, it's worth pointing out that the €3.7bn in bonds Trichet ordered Noonan not burn is roughly equivalent to the government's entire capital investment in social housing over 6 years from 2015-2020 of €3.8bn under its Social Housing 2020 strategy.

Figure 6.1 New House Builds – Private, Council & Voluntary 1995-2014[645]

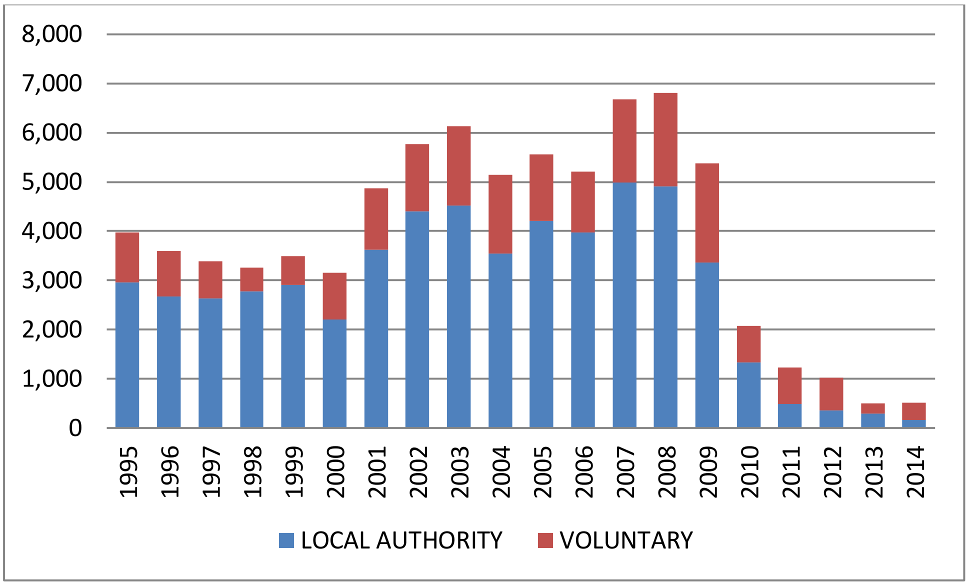


643 Department of the Environment, Community & Local Government, "Latest House Building and Private Rented Statistics," January 12, 2016, http://www.environ.ie/en/Publications/StatisticsandRegularPublications/HousingStatistics/FileDownLoad,15293,en.xls.

644 10,720 to end-2014 + 645 in first 9 months of 2015

645 Department of Environment statistics

Figure 6.2 New House Builds –Council & Voluntary 1995-2014[646]



Outside of housing, investment has been slashed across a range of other public services. Transport had nearly €3 billion in investment in 2008 but only €881m this year. Education was cut from €830 million to €565 million and health from €678 million to €382 million[647]. No wonder over 450,000 people are currently on waiting lists for hospital treatment[648].

Now the 'recovery' is underway, it might seem like a good time to start compensating for what even the *Irish Times* is now calling 'an era of underinvestment'[649]. Instead, the government plans to keep starving our economy and society of the resources it needs to develop. Under its capital spending

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646 Department of Environment statistics
647 Department of Finance, "Revised Estimates 2015," 133; 102; 174.
648 NTPF, "Inpatient/Day Case National as at 26/11/2015," November 26, 2015, http://www.ntpf.ie/home/pdf//2015/11/nationalnumbers/in-patient/National01.pdf; "Outpatient National by Group/Hospital as at 26/11/2015," November 26, 2015, http://www.ntpf.ie/home/pdf//2015/11/nationalnumbers/out-patient/National01.pdf.
649 Cliff Taylor, "Cliff Taylor: Government Is Vulnerable over Record on Public Services," *Irish Times*, December 19, 2015, http://www.irishtimes.com/opinion/cliff-taylor-government-is-vulnerable-over-record-on-public-services-1.2471545.

programme, €27 billion would be invested over the next six years[650]. That sounds like a lot but it's only €130 million more than during the depths of austerity from 2009-2014. This shows the government intends austerity to be permanent.

There are two main reasons the government has chosen this path. First, a shrunken state opens up more space for private investment and profit-making by the wealthy elites it represents. The housing shortage created by virtually abolishing council housing has gifted landlords and property investors a golden opportunity to profiteer, while massive cuts to health and public transport have encouraged the growth of private hospitals and transport operators. Second, continuing austerity will enable the bondholders to get paid. The government wants to start paying off the principal on the debt so although the interest component will gradually fall, the total amount of debt service will remain at over €8 billion a year[651] – twice next year's public investment budget[652] and more than double what the government plans to invest in social housing over the six years from 2015-2020.

These twin goals of shrinking the state and paying down the debt are reinforced by EU rules designed to continue austerity for similar reasons as the Irish government. They restrict the government's ability to make vital economic and social investments but their impact has also been exaggerated by a right-wing government that has consistently made deeper cuts than the rules require to protect the wealthier classes it represents and impress the 'markets'

Restructuring the tax system to take more from workers and less from capital

On the taxation side of austerity, in addition to the introduction of the Local Property Tax, a tax on people's homes, and water charges, across a whole range of taxes, the share of tax revenue levied on employers and capital has fallen, while the share on workers has risen[653]:

- The corporation tax share fell from 16% of the total tax take in 2003 to 11% in 2014
- Capital Gains Tax fell from 6.8% of the total tax take in 2006 to 1.3% in 2014
- Schedule D tax on business income fell from 5.6% of the tax take in 2004 to 3.8% in 2014
- PAYE has increased from 20.6% of the tax take in 2006 to 26%, with USC providing another 8.8% of the tax take in 2014..

The same thing has happened with social insurance[654]:

- Employers' PRSI fell from 74.6% of PRSI in 2007 to 73% in 2013
- Employees' PRSI increased from 19.9% of PRSI in 2007 to 21.6% in 201

[650] Department of Public Expenditure and Reform, "Building on Recovery: Infrastructure and Capital Investment 2016-2021," September 2015.

[651] The total cost of servicing the debt, including interest and principal repayments was just over €8 billion in 2013 and actually rose to €8.2 billion in 2014. Department of Finance, "Exchequer Statement End Dec 2014," January 5, 2015, 4, http://www.finance.gov.ie/sites/default/files/Exchequer%20Statement%20end%20Dec%202014.pdf.

[652] Department of Public Expenditure and Reform, "Building on Recovery: Infrastructure and Capital Investment 2016-2021," 21.

[653] Revenue Commissioners, "Revenue Net Receipts by Taxhead on an Annual Basis," 2015, http://www.revenue.ie/en/about/statistics/index.html#section1.

[654] Department of Social Protection, "Accounts of the Social Insurance Fund 2007," 2008, https://www.welfare.ie/en/downloads/sif2007.pdf; "Accounts of the Social Insurance Fund 2009," 2010, https://www.welfare.ie/en/downloads/sif2009.pdf; "Accounts of the Social Insurance Fund 2011," 2012, https://www.welfare.ie/en/downloads/sif2011.pdf; "Accounts of the Social Insurance Fund 2013," 2014, https://www.welfare.ie/en/downloads/sif2013.pdf.

The Impact of Austerity Cuts and Tax Increases

One of the main impacts of the economic collapse, made much worse by austerity has been the mass emigration of over 155,00 people (net) from April 2009-April 2015. As of December 2015, there were still 328,600 on the Live Register[655], with another 91,298 people on so-called "activation programmes" bringing the total unemployed or underemployed people to 419,898 or 19.4% of the labour force. Combined with public spending cuts and the restructuring of the tax system to place a far heavier burden on workers, there is abundant evidence of significantly increased inequality in Ireland since the crash. According to the ESRI's *Crisis, Austerity, Recovery: Income Distribution through the Great Recession in Ireland* report published last year, 'The poorest section of Irish society suffered the largest contraction in income as a result of the recession' [656], with the poorest 10% suffering a decrease in their income of 22% from 2008-2013, compared to an average decline of 13%. When housing costs are taken into account the gap is even greater, with the poorest 10% 'suffering an income contraction of 27 per cent compared to a 15 per cent national average.' This is a direct result of this government's decision to bring in five regressive budgets in a row. One result of this has been that 'The number of children living in consistent poverty has doubled during the recession'[657], with 135,000 children – or one in eight – 'experiencing material deprivation on a daily basis'. As Carl O'Brien in the *Irish Times* has argued:

> This is not just a sad and inevitable legacy of the economic crash. Instead, political and economic choices were made that caused this, such as paying billions of euro back to unsecured bondholders while cutting health, education, housing and welfare supports. [658]

Underlying these increases in poverty and equality is the increase in profits from 35bn in 2009 to €51bn in 2014, while the wage share of national income fell from 53.6% in 2008 to 48% in 2014[659].A single company, Apple, is sitting on $178 billion in cash, which is legally owned by its headquarters in Cork[660]. But the government is fighting the EU Commission so it *doesn't* have to pay us up to €17 billion in back taxes. Four other US companies, Microsoft, Google, Pfizer and Cisco, which also have significant operations here, have accumulated another $262 billion in cash reserves[661]. And it was

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[655] Taylor, "Numbers on Live Register down 9.7% in Year to December."

[656] "Those on Lowest Incomes 'Suffered Most' in the Recession," *Irish Times*, accessed April 26, 2015, http://www.irishtimes.com/business/economy/those-on-lowest-incomes-suffered-most-in-the-recession-1.2186880.

[657] Carl O'Brien, "CSO Report Exposes Frightening Scale of Child Poverty," *Irish Times*, January 22, 2015, http://www.irishtimes.com/news/social-affairs/cso-report-exposes-frightening-scale-of-child-poverty-1.2074429.

[658] Carl O'Brien, "CSO Report Exposes Frightening Scale of Child Poverty," *Irish Times*, January 22, 2015, http://www.irishtimes.com/news/social-affairs/cso-report-exposes-frightening-scale-of-child-poverty-1.2074429.

[659] Tom Healy, "A Wage Recovery," *NERI Blog*, February 27, 2015, http://www.nerinstitute.net/blog/2015/02/27/a-wage-recovery/.

[660] Simon Bowers, "Apple's Cash Mountain Grows to $178bn," *The Guardian*, February 2, 2015, sec. Business, http://www.theguardian.com/business/2015/feb/02/apple-cash-mountain-grows.

[661] Adrian Weckler, "Apple Is Now so Rich It Could Buy Half of Ireland," *Sunday Independent*, May 3, 2015, http://www.independent.ie/business/technology/news/apple-is-now-so-rich-it-could-buy-half-of-ireland-31190877.html.

estimated last year that corporations across Europe were sitting on nearly $1 trillion in cash out of a global cash pile of $2.8 trillion[662].

Hoarding by rich individuals is equally massive. The richest 300 people in Ireland have increased their wealth from €50 billion in 2010 to €84bn in 2014[663] and the richest 13 are all billionaires, with €38 billion between them[664]. Beyond the super-rich, 'More than half of the country's net household wealth rests in the hands of just 10% of the population, while people in less well-off sectors of society owe more than they own… The top 5% of households can lay claim to almost 38% of net wealth while 15% of the wealth lies in the pockets of the richest 1%.' [665] It's past time for a radical alternative to this failed system that puts people's needs before profit and takes control of the resources in society for the benefit for all.

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662 Deloitte, "Cash to Growth - An EMEA Research Report," September 2014, 2, http://www2.deloitte.com/content/dam/Deloitte/global/Documents/About-Deloitte/emea-cash-to-growth.pdf.

663 Nick Webb, "Ireland's Richest Restore Fortunes to over €84bn," *Sunday Independent*, March 8, 2015, http://www.independent.ie/business/irish/rich-list/irelands-richest-restore-fortunes-to-over-84bn-31044996.html.

664 Irish Times, "Rich List: Wealthiest 250 in Ireland Worth €75bn All Told," *Irish Times*, April 26, 2015, http://www.irishtimes.com/business/personal-finance/rich-list-wealthiest-250-in-ireland-worth-75bn-all-told-1.2189580.

665 Peter O'Dwyer, "Top 10% Own over Half of Irish Wealth," *Irish Examiner*, May 12, 2015, http://www.irishexaminer.com/ireland/top-10-own-over-half-of-irish-wealth-330046.html.