

# HOUSES OF THE OIREACHTAS

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## AN COMHCHOISTE FIOSRÚCHÁIN I DTAOBH NA GÉARCHÉIME BAINCÉI- REACHTA

### JOINT COMMITTEE OF INQUIRY INTO THE BANKING CRISIS

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*Déardaoin, 26 Feabhra 2015*

*Thursday, 26 February 2015*

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The Committee met at 9.00 a.m.

#### MEMBERS PRESENT:

Deputy Pearse Doherty,	Senator Sean D. Barrett,
Deputy Joe Higgins,	Senator Michael D'Arcy,
Deputy Michael McGrath,	Senator Marc MacSharry,
Deputy Eoghan Murphy,	Senator Susan O'Keeffe.
Deputy Kieran O'Donnell,	
Deputy John Paul Phelan,	

DEPUTY CIARÁN LYNCH IN THE CHAIR.

## Context Phase

### Mr. David McWilliams

**Chairman:** In commencing this morning's proceedings I welcome everyone to the 11th public hearing of the Joint Committee of Inquiry into the Banking Crisis. At our first session this morning we will hear from Mr. David McWilliams on issues related to early warnings, divergent and contrarian views in the context of the banking crisis in Ireland. David McWilliams is an economist, writer, broadcaster and journalist. He worked initially as an economist with the Central Bank of Ireland, the Union Bank of Switzerland and Banque Nationale de Paribas. Since 1999 he has been a broadcaster, writer, economic commentator and documentary maker. He has written four books, writes two weekly economic columns and he has made various documentaries. He has brought a one man economic stand-up show to the stage at the Abbey Theatre. David McWilliams is credited with being one of the first economists to predict a boom in Ireland's economy and for his predictions of an Irish property bubble building from 2000 to 2007 which would ultimately burst. He was the first to coin the phrase "ghost estates". In January 2007, David McWilliams was selected as one of 250 young global leaders by the World Economic Forum and he is a regular speaker on the international circuit. I welcome Mr. McWilliams.

I wish to advise the witness that by virtue of section 17(2)(l) of the Defamation Act 2009, witnesses are protected by absolute privilege in respect of their evidence to this committee. If the witness is directed by the Chairman to cease giving evidence in relation to a particular matter, and continues to do so, the witness is entitled thereafter only to a qualified privilege in respect of the evidence. The witness is directed that only evidence connected with the subject matter of these proceedings is to be given. The witness has been informed previously that the committee is asking witnesses to refrain from discussing named individuals in this phase of the inquiry. Members are reminded of the long-standing ruling of the Chair to the effect that Members should not comment on, criticise or make charges against a person outside of the House or an official by name, or in such a way as to make him or her identifiable. Can I invite Mr. McWilliams to make his opening remarks to the inquiry please.

**Mr. David McWilliams:** Thank you very much, Chairman. It is a pleasure to be here. I just want to make some opening remarks about the period in question, starting with 2000 and going up to 2008 and beyond. It is my opinion that the Irish banking system, and by extension the rest of the Irish economy, was set up to fail. I saw this earlier than anybody else and I made this opinion and these ideas available as widely as possible. In fact, I probably spent the best part of a decade trying to warn as many people as possible on as many platforms as possible that our property market was going to crash and that when it did, our banking system would be in a situation where money would fly out of the system and lead to a banking crisis. I did this in hundreds of thousands of words; not thousands, but hundreds of thousands of words, in dozens of articles, two a week in the *Irish Independent*, the biggest selling newspaper in the country, and in *The Sunday Business Post*.

I made documentaries about this. I had my own TV show on TV3, which was watched by tens of thousands of people. I warned people at every juncture that our housing market was a credit bubble and credit bubbles bust and it is not a matter of if they bust but when they bust. The documentaries of *The Pope's Children* book, which I wrote, were watched by 36% of the Irish watching audience; that is a lot of people. *The Pope's Children*, and I do not say this for any other reason than to make the point, was disseminated extremely widely and was the best-selling non-fiction book, not of the year, but of the decade, and it was published in 2005. So these ideas were out there, disseminated widely, in the most accessible way. When I hear the view that nobody saw this coming or that this was in some way a shock or we were taken by surprise, I do not believe that is the case. I think the Irish property crash and the banking crash were both incredibly predictable and absolutely preventable.

This testimony will be a little bit different in the sense that it will not be about what should have or could have happened, and if we had seen that, if we did not see that, and my God I cannot believe we missed that. This testimony will be taken from contemporaneous articles, pieces of work that show thinking at the time. This was not isolated thinking. In fact, I believe, and my experience through the period from 2000 onwards was, that many thousands of ordinary Irish people could see what was happening. The difference is that I was an economic commentator and an economist and I had the platform of the media to deploy these ideas. I cannot tell you the number of times I went into bars and pubs and chatted to people and they said, "Hold on a second, this doesn't seem right; what is going on here?" So it is not as if a significant part of the population was not already worried. I want to make that point that this was preventable and predictable, and that these views were widely disseminated. There were not a huge coterie of individuals doing this but it was certainly out there.

One could probably ask oneself why did this guy, who is a former Central Bank economist, an investment bank economist, why did he not just come home to Ireland, keep his mouth shut, play the game and get on with business. The reason is I felt that if one has a specialty, if one understands something, one has something like a patriotic duty or a moral imperative to say that the policy or numbers of policies that we have together will lead our country into catastrophe. I think it was a patriotic thing to do. It certainly was not a worthwhile thing to do and it certainly was not fashionable and it certainly did not make me popular. The interesting thing is that all through this period I was accused of being unpatriotic when I believe in actual fact it was something that was essential to do if one had the education and the experience to do so. I remember people saying that I was unpatriotic for talking down the economy. The committee might remember that expression, "Talking down the economy". I think that was maybe a reaction on the part of certain parts of the establishment to somebody saying, "Hold on a second, this thing will not last."

It seems to me from a political perspective that on every big economic issue, Ireland tends to split between insiders and outsiders. The insiders are people with "pull", the old fashioned word, with access to power, and the outsiders are people who are actually on the outside. In the case of the property market and the associated banking and credit explosion, the insiders were the bankers themselves, estate agents, people who were doing well out of the property market, parts of the professional classes who were doing very well, and senior Government officials who were looking the other way or were not necessarily taking on board what was clear. These are the people on the inside who were actually doing well. Then, of course, political parties, because if there is a property boom there will be a tax boom. If there is a tax boom then there will be lots of goodies to give out, lots of sweeties to give out. So I think they are the insiders and in the situation of a housing boom where house prices are rising well above what the aver-

age person can afford, the outsiders are simply the people on the outside who are forced to play a game in which the dice is loaded against them from the start. I think that is important; there is a political context in this.

I suppose I devoted such enormous energies to trying to warn about this for two main reasons. The first reason was because I believed that hundreds of thousands of ordinary Irish people would end up in negative equity and would end up in debt and would end up in a situation where their lives would be destroyed by the debt associated with the housing market and they would end up being the people who paid. That is a social reason. The second reason, and this is very important for the context of this, is that I had worked both inside the Central Bank in Ireland in a crisis but, more crucially, I had also worked outside in investment banking. What I see and what I saw were panics in investment banks, panics in financial markets, and I could see that every single day we avoided taking responsibility for this mess. Every single day we said, "It will be grand," or, "There will be a soft landing," or, "Don't worry about it, it is the markets." We were therefore condemning ourselves to run out of options when the crisis happened. The more we ignored, the more desperate we became and therefore the more we ignored the more likely we were to end up, which we did when the crash came, in a situation where our choices were not between good and bad but between bad and worse.

The crash was inevitable. Now why was it inevitable? This is the key. It was inevitable because of the way in which the banks were financing themselves. Again I wrote all of this at the time. I was writing this in 2000 and 2001. This is not me thinking back and looking with hindsight. This was obvious to anybody who was trained. It was obvious. This is not the sort of thing that anybody who is trained could not see. This panic did not have to happen. The panic of September 2008 did not have to happen. It was not anything that was pre-ordained. It could have been fixed very early. The problem is if there is no housing boom there will be no banking boom. If there is no banking boom there will be no banking crisis. If there is no banking crisis there will be no interventions, such as the guarantee, and there will be no bailout. All of these things are the consequence of bad economic policy, not the cause. They are the consequence. What happens in banks when they get out of control is that they all end in bank runs. A bank run is when people take their money out. A bank run is called a run because it happens quickly; it is not a bank amble or a bank stroll or a bank stroll around the park with a dog. It is a run because people panic. That panic will be more extreme if there is what is called hot money, if there is international money financing the banks. When I saw this in 2004 that was when I realised we had a serious problem.

The Irish banking crisis began in 2000, not in 2008 as is sometimes suggested. It began in 2000. The great English economist John Stuart Mill, speaking about the railway crash that happened in Ireland during the Famine, said that crashes do not destroy the wealth of a nation, they merely evidence the extent to which wealth has already been destroyed by stupid decisions taken in the boom. So the destruction of the Irish balance sheet did not happen after 2008; it actually happened before. That is the nub of the issue, because prevention is always better than cure; we know that. There is a direct link therefore between not heeding the warnings and vilifying those who warn. There is a direct link between this and the subsequent panic which need not have happened and the decisions that were taken.

The best way to look at this credit banking panic is through the prism of a forest fire. Let us imagine a forest fire in a small place; the pyromaniacs start the fire which, in this case, are the banks and the forest is the general economy. The people who are supposed to be the firemen, the regulators and the monetary authorities, look the other way and say "Don't worry about the

fire”. Some people would have said we have had them before and they have been quite nasty but this one will be different. The firemen say “Don’t worry, we’ll be grand, it will blow itself out.” Then the fire engulfs, not only the forest, but is about to engulf the entire village beside it. The village leaders, the politicians, are faced with the choice - does one let the thing blow and see what happens because one never knows maybe a house will remain, or does one put it out? At that stage one has to put out the fire with every single method possible. Why? Because it is already engulfing the entire place. If one looks at the situation in that way one can see the way in which I, who wrote this a long time ago, think about these situations.

Who started the fire? I wrote many years ago that property markets can only increase with credit. Property markets do not increase as a result of supply and demand. That was a big canard. It does not happen that way. It is credit. Who gave the credit? The banks. Worse, what happened? When the banks ran out of our deposits - normally the bank would say to itself I have a deposit here that will allow me to lend - they borrowed other people’s money to give to us to buy houses that we were buying and selling to each other at expensive prices and calling it a miracle. Whose money did they borrow? They borrowed from the Germans, French, British, etc. There was hot money coming in. For example, one of the largest banks took 100 years to build up a balance sheet of €60 billion but it doubled that in three years. Let us think about that. Why? Because it had all this money coming in.

What was the regulation called? It was called light touch regulation. Light touch regulation means one guarantees, almost makes certain, that the banking system is going to implode because hot money always leaves. When hot money leaves then the rest of the money leaves too. We actually set the entire thing up and this is crucial to a fail.

The interesting thing is a lot of people said: “Don’t worry. The free market will discipline the banks.” That does not happen. Let me explain what happens in the free markets. On the way up the free markets do not discipline the banks but do the opposite and allow the banks to do what they want. As a consequence we have an extraordinary situation where one joins the EMU, which was an unusual decision we might talk about later but it had a material impact on the economy, most of which in my opinion is negative. We have light touch regulation, we get this flood of money into the banks which facilitates over-lending and then the over-lending facilitates over-borrowing. All of this sounds familiar now but back in 2003 nobody was discussing it or those who did were vilified. I shall play the committee a little 40-second clip of me on “Prime Time” in October 2003 which was watched by 400,000 people. This is important and I said:

The Irish housing market is a scam. It is an enormous financial swindle that could potentially confine an entire generation of young Irish workers to years of bad debt. Far from being a reflection of economic vitality and fundamental demand the housing bubble is, in the main, a vacuous financial confidence trick that has been foisted upon us by an alliance of banks and the landowners.

Today, in Ireland, the price of the average house is close to ten times the average wage. This represents an economic failure on a monumental scale. Behind this nonsense is excessive and irresponsible lending from our financial institutions. The situation would be laughable if it were not so serious.

That clip dates from October 2003. I said: “The Irish housing market is a scam.” That is what it was and that is what I want to come back to. It was financed by over-lending not demand.

## CONTEXT PHASE

A lot of people have asked me what made me think like that while other economists did not. I will wrap up but I want to make the following point about what happens when house prices rise. Economics tells us that when the price rises the demand falls, that is what we teach kids in school. In Ireland the opposite happens with house prices. When the price rises the demand rises because people get panicked. One hears that all the time. People say: "Jesus, prices are going up by 10%. I'd better get on the ladder now because if I don't I'll have to pay another 10% next year." A very active rise in prices, once it is allowed, creates a dynamic in people's heads to buy more, not less. This is why economists could do with common sense, which is what I have always felt. I urge them to talk to people. I suggest they forget the models, talk to people, ask them what they think and then think about supply. Economists will say "Oh, when the price rises the supply goes up".

The main houses we have in Ireland are a stock of housing. The houses are already built. Someone like my Mum would trade down from a family house, she would move on and some other family would have the home. Let us think about what happens when house prices rise. My mother would say, and it is natural, "I won't sell that now if they are going up by 20%. Wouldn't I be mad to sell so I shall sell next year". That would be a totally rational decision for my mother. Not only does the price not work, it amplifies the problem. It ends up that supply eventually adjusts but it adjusts far too late. We end up building houses in the wrong place for the wrong people at the wrong price. That is why I coined the expression "ghost estates".

In 2006, I was travelling back from Westport having visited Allergan, a factory which produces Botox, not for my own use. I visited for a piece of research I was doing about who made Botox. While I drove back from Mayo to Dublin I saw that every little town had a huge big estate and was reminded of a conversation I had had the night before. I was thinking, because I had talked to a local guy the night before about the famine in Mayo, about how extraordinary it was and how unbelievably catastrophic it was. He talked about the famine villages around Delphi and that neck of the woods. He said they were like ghost villages and were kind of creepy. When I saw the estates on my drive back home I thought they were exactly the same and that they were ghost estates. It is funny because when one comes up with a term one does not realise that it will drop into the lexicon so quickly. Obviously the "breakfast roll man" was building the "ghost estates". All these things happened but the ghost estates are indicative of how supply does not respond.

One wonders why people behave like this. I want the committee to understand, at the very beginning, why the economy behaves like this. People behave like this because we are all impacted by each other. Economists think we are all rational. We are not. We are highly irrational. Has anyone every met a more irrational animal than us? We fall in love, we follow stupid football teams - all the things that make no sense. The reason is that everything we do is impacted by other people.

A couple of months I was in the Aviva stadium with my son. In Dublin, there are two types of people. There are those people who buy their own tickets to the Aviva and there those people who get paid to go to the Aviva. I fall into the former camp. I remember Ireland scored three tries against Australia in the first 18 minutes. Even though I had really good seats with my 12-year old I saw none of the tries. Why? Every time the Irish team did well everyone seated in front of us stood up. Then I had to stand up and my kid had to stand up and get on my shoulders. Then the people behind me had to stand up and that continued for all the people behind them. That is exactly how the economy works too. The fellas who stood up first had no idea they were sending a signal to me to stand up because I was behind them. I had no idea that I was impairing

the view of the people behind me. We had all paid to sit in the Aviva but we ended up standing. That is how the economy behaves. When people see house prices rising in Ireland they buy houses, if they can, not because they want them but because other people are buying them. That type of herd behaviour is essential to understand why a property boom in a country like ours, if it is not controlled, gets totally and utterly out of hand unless of course one is lending to this property boom in which case one is making money so does not care. The question is, why did the banks not see this? Why did they not see that their own balance sheets were being impaired? I believe it is because banks' balance sheets play tricks on them. Every time a chunk of money goes in to the economy, house prices rise. That means the banks' collateral rises so they feel safe. Every time the collateral rises they feel safer and safer and ultimately they lend more and more and more. Then, if your bonus is related to your share price you have a greater interest in lending more because lending more makes you rich and gives you profits.

**Chairman:** Move towards a wrap up now Mr. McWilliams because we also have to ask you some questions.

**Mr. David McWilliams:** I am trying to get to the point of why this economy works as it does and why we need to have a set of views of the economy which reflect what actually happens in reality and not in some dream world of academia. I am saying the banks' balance sheets play tricks on them and they ultimately go bust. Why is that? Because they are allowed to borrow yet more. They keep borrowing and the balance sheets look fine. Then they realise the more they borrow, the worse the balance sheet is, but they don't see it.

Why did the interest rate not rise? Because we are in the EU. We have this crazy situation in that we have decided we are Germans. What is that all about? Ireland does most of its trade with Britain and the US, yet we have a currency attached to Germany. Somebody else may elucidate as to why that is. When German interest rates fall, our interest rates fall too. When our interest rates fall there is no warning sign from outside. That is hugely important because it is material to the next ten years, not just the last ten years.

We also have an issue with groupthink. Why did nobody, or very few, speak out? I believe groupthink is something that happens in many aspects. I believe that if you have ideas in Ireland which are beyond the mainstream, those ideas go through three phases. The first phase is open ridicule, the second phase is violent opposition and both of these happened to me. The third phase is where we are now which is that everybody pretends they were on your side all the time. This is what happens. Groupthink shifts because it is a conventional wisdom. We can talk about this during the questions.

**Chairman:** I will ask that you wrap up please Mr. McWilliams. Much of what you gave the Committee in your opening statement will be also be addressed in the questions this morning.

**Mr. David McWilliams:** This is all about 2006. During 2007 and 2008 I became very worried. My articles became extremely agitated. I could see the smart money leaving the country. One could see this in repo rates and credit default swaps. In *The Pope's Children* and in the accompanying TV series, I said that certain well known Dublin banks were then little more than out of control hedge funds, leveraging themselves and their clients' money into property. I said that these outfits usually went belly-up. I worried, but not because I had any contact with the banks. I was so toxic at that stage that I had never been in any of the banks. I may have bumped into one or two of them at economic conferences but that was the height of my contact. I had no insider knowledge or data. This was simply an economist working in the banking system, on his own and at his own desk, who could see what was going on.

## CONTEXT PHASE

**Chairman:** Mr. McWilliams I have afforded you more time than any other witnesses that have come before the committee. You are now on 25 minutes. Usually the limit is 15 minutes so I will have to ask you to wrap up.

**Mr. David McWilliams:** We can wrap it there.

**Chairman:** I am moving to questions. The lead questioners today will be Deputy John Paul Phelan and Deputy Pearse Doherty with 20 minutes each. Other questioners will have eight minutes after that. I will set the scene. Mr. McWilliams, you mentioned the housing price bubble in your opening address this morning. Given that you were warning for such an extensive period of time, was there any point prior to 2007 when you thought that your warnings may have been mistaken?

**Mr. David McWilliams:** No. I became increasingly certain because the evidence was all over the place, from the hard economic numbers to the anecdotal evidence and conversations. When you see house prices going completely out of kilter, you realise there is a serious problem. One of my best leading indicators was a piece in the Irish Times called Take Five, a part of its property section which offers city by city house price comparisons. The article showed readers the difference between a two-up two-down house in Dublin city for €500,000 and a 17 bedroom chateau outside Paris with a direct RER rail link to Place de l'Opéra, for the same price. As the property-credit-borrowing binge became worse, it struck me that there was no way we could avoid a banking crisis. It became a matter of when, not if.

**Chairman:** You mentioned in your book *The Pope's Children* that a property crash was on the way. You based this on the Minsky Kindleberger credit cycle analysis. Can you please outline to the Committee what that theory means?

Can you also inform the inquiry if any person in authority contacted you in regard to the concerns you were raising at that time?

**Mr. David McWilliams:** It is an interesting question. The book *The Pope's Children* was so widely read that these ideas were in the ether. This was not an academic book that nobody read, it was the biggest selling non-fiction book of the decade. This has all happened before, all over the world. We can go back to the Romans or even the Bible. Deuteronomy and Leviticus, two books in the Old Testament, deal with debt forgiveness after booms. We are not talking about something new, we are talking about something that is deep in our culture.

Most mainstream economists in Ireland believe in classical economic theory and I do not. I never have. I will give an example of what happens in peoples' heads when prices rise. There are two stand out American economists I learned about after I left postgraduate studies and university in Ireland; Charles Kindleberger and Hyman Minsky. They understood that once credit was put into the mix, it profoundly changes the way people behave. Members will know this from talking to their constituencies. Kindleberger outlined the various stages of the cycle. There are seven stages.

One is when something material happens or actually changes. In our case we joined the European Monetary Union and our interest rates in the long term went from a real interest rate of about 6% down to almost zero. Our interest rates fell which changed the landscape profoundly. House prices begin to rise in this first stage of Kindleberg's model. The second stage is euphoria. People begin to think it is because of themselves that their house price is rising. They think they are clever. House prices continue to rise. The third phase is gearing, which is



when the banks get involved with the idea that one can remortgage a house to buy two gaffs in the Algarve. Gearing means that the whole thing starts to get a little bit crazy. The fourth phase is the mania phase when people become manic. People actually flew to Bulgaria to buy houses, financed by their houses in Ireland. Banks are now pushing the money. The fifth phase is the bubble phase. We all lived through it and know what it is. The sixth phase in the Kindleberger cycle is the phase of distress. This is when people start to dislike the smell of the situation. Early people get out and start selling. The seventh phase of the Kindleberger Minsky cycle is called *torschlusspanik*, a German phrase from when it happened in Germany and Austria in the 19th century. It translates as shut door panic, when everybody jumps and runs for the door and tries to sell. The whole thing collapses. This happens in assets all the time and I could see this.

There are three phases which happen next. The first is the Minsky moment. This is crucial because our banks had a Minsky moment in September 2008. A Minsky moment is when a bank realises it does not have any money and must sell good assets to pay for the losses on bad assets, because those assets are entirely bought on margin. Once one buys something on margin, one is in the lap of the gods. So we had Kindleberger's seven stages, then we had a crash and then came the Minsky moment where we had bank collapses. Again, this is all in the book. At that stage only massive state intervention can help. It is described as requiring a hegemon, that is, a big country or large institution, a central bank or the ECB, say, to come in and right the situation. That is because they, like me, do not believe in classical economics. The economy will not right itself after this type of boom and there must be an intervention.

**Chairman:** That leads me to my last question. I ask Mr. McWilliams to be as succinct as possible in all his responses as we have another witness attending later. He referred to that big moment and the big intervention that is required-----

**Mr. David McWilliams:** I apologise for interrupting the Chairman. I did not answer his last question, which was whether anybody in authority contacted me, at any stage, to discuss my concerns. The answer is "No". Categorically, not one adviser, not one Minister, not one civil servant, not one member of the regulator contacted me. Nobody did. In actual fact, I would have been toxic to all of them and they probably would have avoided me like the plague. All of this was going on and never once was I asked my opinion on anything by anybody, informally or formally.

**Chairman:** To come back to the Minsky moment, Mr. McWilliams spoke about how the big intervention might manifest itself. In the Irish situation, it was in the form of the banking guarantee. Did the design and implementation of the guarantee have any relationship to Ireland's entering a bailout programme two years and two months later?

**Mr. David McWilliams:** Yes, I believe it definitely had. As I said at the start, the guarantee, the bailout, all of these issues are the consequence of the pathetic policy from 2000 to 2008. The outcome was foreseen and certain. It was simply a matter of how bad it was going to be. That was really the question that was revealed over the course of the subsequent few years.

**Deputy John Paul Phelan:** I welcome Mr. McWilliams. As a pope's child myself, my first question relates to his book, *The Pope's Children*, published in 2005. It was this book, in many respects, which brought Mr. McWilliams to national prominence. One reference in that book particularly struck me when I reread it recently, namely, the statement that the decline of Germany had changed Irish psychology and was central to Ireland's success. Will Mr. McWilliams outline briefly what he meant by that?

**Mr. David McWilliams:** There is a chapter in the book called *Vorsprung Durch Credit*, which was a play on an Audi advertisement slogan. One has to come up with these things, and it seemed to work at the time.

**Deputy Kieran O'Donnell:** Its called marketing.

**Mr. David McWilliams:** Yes, it seemed a good chapter heading. What I was trying to explain, which had not really been explained before and certainly had not been explained to the Irish people by the policy makers, was that once one joins a monetary union, what one is effectively doing, if there is no regulation of one's banks, is getting the PIN number to the ATM card of the richest person in the room. Of course, the richest person in the EU's room was Germany. It was rich and it was in decline. After reunification in the early 1990s, the united country swallowed up the former East Germany and it cost it a fortune to do so. Germany's economy then began to stagger under the weight of those repayments and as a result of the cultural and demographic shift. The country started to go into decline in the period from 1995 to 2005. For Ireland, this meant our interest rates, which were really set for the Germans, went to levels that were totally inappropriate for the boom we were having. It meant that the normal way in which one warns people that things are out of kilter, which is by setting higher interest rates, not only did not happen but we actually got lower interest rates.

I was trying to explain in the book where the money was coming from. I remember going to pubs and people asking, "Where is all this bloody money coming from?". I recall a builder friend of mine who worked with me years ago in Boston saying to me that the difference in Ireland at that time, compared with the past, was there was now no problem getting money. For the 2005 book, I invented a German character whom I named Udo Lindenberg after a German crooner. This guy was sort of the German version of France's Johnny Hallyday - not a great gig to attend, I suspect. I invented the character and named him for this singer I had heard of. Udo represented the old, parsimonious German saver. Banks hate savings because they do not make any money on them. In fact, they pay out for savings. In that situation, they asked themselves who they could give them to in order to make money on Udo's savings, and over here was Ireland.

**Deputy John Paul Phelan:** I will bring Mr. McWilliams forward now to the very early part of September 2008. In a radio interview on RTE's "Saturday View", he stated that a crisis was imminent in the Irish banking system and that at least one Irish bank would be closed before Christmas. He said in his 2009 book, *Follow the Money*, that he received a number of telephone calls from bankers in the wake of that interview who accused him of causing panic. Will he indicate how many calls he received and what was said during those conversations?

**Mr. David McWilliams:** I received two telephone calls, neither of them from persons who would have been household names. This goes back to a very important point. In Ireland, we have an inability to accept reality. It is a national issue we have. In a crisis, the most important thing is to define one's reality not as one would like the world to be but as it actually is. Once one has defined that reality and got the facts, then one can do something about it. Once something has been done about it, one can then face into the crisis. It struck me that in Ireland, all the way through 2007 and 2008, the official policy was to delay and pray. It was a case of we will say everything is grand and pray the cavalry will come over the hill and save us.

**Deputy John Paul Phelan:** To clarify, what was the nature of Mr. McWilliams's telephone conversations with those bankers?

**Mr. David McWilliams:** They said they had heard me on the radio and both referred to “dangerous talk” and warned about frightening the horses. The problem with that is that I knew, not from talking to bankers but from looking at what are called repo spreads and credit default swaps, that all the hot money, this significant investor money, was leaving. Whose money gets called after that? Your mum’s money and my mum’s money gets called. It falls to depositors, in other words. What struck me as really strange was the more they spoke about “dangerous talk”, the more they imperilled the deposits of the little guy, because the big guy always gets out first. The context is this idea of delay and pray and not being honest with ourselves. The more they denied it, the more terrified I became because it either meant they did not understand the significance of what was happening, they did not have any facts at their disposal or they actually did not care.

**Deputy John Paul Phelan:** I have another question about Mr. McWilliams’s radio interview in September 2008.

**Mr. David McWilliams:** I have the transcript here.

**Deputy John Paul Phelan:** Was the former Minister for Finance, the late Brian Lenihan, on the same panel or did Mr. McWilliams meet him that day in another part of the building?

**Mr. David McWilliams:** I had never met the late Brian Lenihan before that day. I was on a panel with him; Brendan Keenan, my colleague and economics editor at the *Irish Independent*; and then member of the Opposition, Deputy Richard Bruton. I had written an article the night before for *The Sunday Business Post* in which I said exactly what I have just outlined, namely, that the banks were not being truthful. Either they did not know what was happening, which is unforgivable, or they would not admit what was happening, which is another issue. My recollection was, now that I have the transcript, that the first about half an hour was spent talking about the public sector. I think Brian Lenihan was involved in a partnership negotiation. We talked about the public sector, and there were budget cuts coming. I interjected and said, “We can talk about this all we like - I can read the echo verbatim, but we will put it into the record - but the problem is the banks and that the Irish banks risk going bust in the next couple of months”. I cited the Swedish example and I said what was happening in Ireland was exactly what happened in Sweden and in Japan.

**Deputy John Paul Phelan:** Did he, at that time, invite Mr. McWilliams to make further contact?

**Mr. David McWilliams:** I have the quote here from the Minister, and again I can absolutely understand why a Minister for Finance in a country does not want to precipitate, or has no interest in precipitating, any further panic than is already there. The Minister replied to me and said, “That is dangerous talk”. I think when we get to a situation where telling the truth is regarded as dangerous, the Deputy knows that we are in the last resort saloon. We came out of the RTE interview and there was chitchat and pleasantries and Brian Lenihan said to me, “You seem to know what’s going on”. He said to me, “You got all this right in the last couple of years” and he laughed. He said, “Why don’t you come in and advise me because everybody else is in advising me?” That was the actual quote. He said, “Here is my number” and he scribbled it down. I scribbled it down, I think, on the back of one of the books I had taken in with me. That was the first time I met Brian Lenihan, so I took his number.

**Deputy John Paul Phelan:** About 11 days later on Wednesday, 17 September, Mr. McWilliams made a phone call to the Minister.

## CONTEXT PHASE

**Mr. David McWilliams:** I thought to myself that pray and delay could be a tactic but that there has to be a strategy. I was really fully expecting a strategy to come out, that this is what we were going to do, that we have a bank resolution mechanism and we know how to deal with this. At every juncture during those two weeks, nothing was coming. It was still the same thing, that the banks are well capitalised and that the Irish banks have been stress tested. One will remember all that sort of stuff. The crucial point to appreciate is that the rich guys get their money out; it was a poor average person who gets burned in a bank run. That is what happens.

**Chairman:** The diary that you are working-----

**Mr. David McWilliams:** At this stage, it was already on Joe Duffy, which I think as a leading indicator would suggest that if it is on Joe Duffy, it is real. You can quote me on that.

**Deputy John Paul Phelan:** What was the nature of that phone call on Wednesday, 17 September, and what did Mr. McWilliams say?

**Mr. David McWilliams:** I went on “Prime Time”. Now just think of what happened. Lehman’s had gone bust and the Americans had tried to let a bank go bust and ring-fence it - this idea that one can amputate the leg - but what had actually happened was the opposite. Not only did it not stop the crisis-----

**Chairman:** The Deputy is asking you about a sequence of meetings you had with Brian Lenihan. We can fill in the historical parts ourselves.

**Mr. David McWilliams:** After “Prime Time”, I realised-----

**Deputy John Paul Phelan:** In the phone call on 17 September that Mr. McWilliams made-----

**Mr. David McWilliams:** Yes. That is why I called him. I realised-----

**Deputy John Paul Phelan:** What was said?

**Mr. David McWilliams:** He said, “I’m busy now, I will call you back”. That was fine. I was sitting at home and the phone rang. My expectation was that he would say, “Listen why don’t you come in and talk to ourselves in the Department”. He asked where I lived and I said Killiney. He said he would be out to me in an hour. That was the meeting.

**Deputy John Paul Phelan:** The famous meeting took place, I think from reading the book again, between 10.15 p.m. and 2 a.m., so it was a four hour meeting.

**Mr. David McWilliams:** No. I think the book said two. It was well after midnight. It could have been 2 a.m. or 1.30 a.m. It was around that.

**Deputy John Paul Phelan:** Before he arrived, was Mr. McWilliams preparing any thoughts or views as to what he might say to him?

**Mr. David McWilliams:** No. It is a funny thing. It might not feel strange for members as they are politicians, so they meet each other all the time, but I have never had a politician in our house. I certainly never had a Minister in our house. We had a little panic and my wife said that I had better go and buy some biscuits, so I found myself in Centra in Ballybrack buying digestive biscuits and milk. I am just giving a sense of-----

**Chairman:** I need to move to the substantive part of this engagement, please.

**Mr. David McWilliams:** Had I got anything prepared-----

**Chairman:** I am looking forward to the coffee break later this morning but we need to deal with the issue.

**Mr. David McWilliams:** The good thing was that I had an article that I was sketching out that night in my head. It was published subsequently in *The Sunday Business Post* and was called “The State must act as a safeguard”. What this sketch was doing was that it was looking at the options available to the country and seeing what could work.

**Deputy John Paul Phelan:** So Mr. McWilliams was preparing himself for his-----

**Mr. David McWilliams:** In preparation for this, I realised that I have written over 1.2 million words of economics which have been published in this country, so it is a lot. These articles are sketches but it is a good contemporaneous note on the thinking.

**Deputy John Paul Phelan:** On that very point, did Mr. McWilliams take a note of the meeting or after-----

**Mr. David McWilliams:** I published-----

**Deputy John Paul Phelan:** I understand but after he left that night, did-----

**Mr. David McWilliams:** No. I did not take notes but I was very well aware of what the conversation had been about. I suspect that this article is as close to a contemporaneous note, and that was published. It was published on the Sunday but was written on the Friday.

**Deputy John Paul Phelan:** Further on in the book, I think on page 16, Mr. McWilliams says he got the impression that the Minister was quite isolated from his officials and sceptical of the advice he was getting. Briefly, why did he come away with that impression?

**Mr. David McWilliams:** The most important thing in all these crises is to establish the facts. I said to him, “Do you know the facts?” and “Do you absolutely know what is going on?”. He said “No, I am getting different numbers all the time”. I said to him, “Okay, so you don’t know the facts, so what you have to do is do something temporary to buy yourself time until you find out the facts”.

**Deputy John Paul Phelan:** That leads me to my next question. Again, on page 16, it says the Minister asked Mr. McWilliams what he would do. I want the witness to briefly outline what his response was.

**Mr. David McWilliams:** We went through - I can go through it here in this article - why a variety of other ideas would not work. Does the Deputy want me to go through that?

**Deputy John Paul Phelan:** Yes, please.

**Mr. David McWilliams:** The first idea after Lehman’s was that a country could let a bank go and that would insulate the system. If the United States could not let Lehman’s go, with the deepest financial market, with the best central bank in terms of ability, with its own currency and with its own monetary policy, we could not do that because it did not work in the States. The second day after Lehman’s failed, the Americans did what would be called the nationalisation route. They nationalised AIG, the massive insurance company. Nationalising would not have stopped the bank run in Ireland because the bank run was systemic in the sense that people

were taking money out of all the banks, so you nationalise one but it just means that people will say, “Who is next?”. That is exactly what happened in America.

The next day Merrill Lynch went bust. I did mention to the Minister that I found it ironic that his lead advisers were Merrill Lynch, people who could not even keep their own bank solvent, let alone advise others. At the time, he was aware.

The third option was that one of the big Irish banks would buy one of the small Irish banks, the idea being if you have a big balance sheet, you can actually take over a smaller balance sheet but I said to him at the time that all the Irish balance sheets were bust because we all knew they were doing the same thing. So even without the figures, you knew that they were all bust. I remember saying to him that I thought “two bad balance sheets does not make a good one”.

Then he said, “What about the idea of giving a €100,000 guarantee to depositors?”. I said, “That could work but you cannot really be half pregnant, Minister” and I remember he kind of smiled at this. I said that if until yesterday you said the banks are well capitalised and then tomorrow morning you say, “Do you know what, not only are they not well capitalised, they are going to bust but we will protect some people”. When the hot money is owned by people in trading floors, that does not cut it. In fact, that proved to be the case. A limited €100,000 guarantee was introduced on the Friday after that and it did not work as money continued to flow out. Just as I had been thinking, once you admit that you have a problem, having denied it all the way up, it opens the floodgates, which it did.

Finally, I said, “There is one other option,” and he said, “Well, we are working on that other option.” The Merrill Lynch options show that the Department was working on what was called the blanket guarantee. Blanket guarantees have been used in 14 out of 42 bank crises. They are not unusual, but the Irish one was followed in Denmark and Germany a week later. It is only as a last resort and I remember saying to the Minister, “I don’t know; I don’t have the facts, but I think we are at the last resort. What you have got to do [this is very important for the record and it is written down in black and white in all of my documents] is you have got to introduce a holding guarantee which buys you the time to allow your auditors and your civil servants to go in and find out the facts. You cannot do something permanent when you are not in possession of the facts and if you are not in possession of the facts and that is the case right now, you need to do something temporary with a time limit. That time limit you have got to figure out.”

**Deputy John Paul Phelan:** What time limit did Mr. McWilliams have in mind?

**Mr. David McWilliams:** In the article I said up to two years and it is written in black and white: “The Government could do this for a limited period. This is absolutely crucial. This is a holding guarantee. Let us say two years.”

**Deputy John Paul Phelan:** On page 22 of *Follow the Money*, Mr. McWilliams said that because the Irish banks’ funding had become unstable, if their funding as well as their deposits were not guaranteed, they would come crashing down and that they would have to come up with the money immediately for people’s deposits. When he spoke to the Minister about this, did he include subordinated debt in the guarantee, as well as-----

**Mr. David McWilliams:** No, subordinated debt is strange. There are 14 other instances around the world of last resort guarantees, given when time is running out and confidence is shattered and the state has to step in or the alternative is a bank run and a total collapse of the banking system. We know from the Great Depression that this is not what you want. This

causes recessions to turn into depressions. However, in all cases, there is a distinction between debt and equity for corporate finance receiverships. Equity like instruments are never included and subordinated or junior debt is subordinate to or underneath and at no stage did I ever imagine that such debt would be included and the reason is that it is known that in all corporate finance receiverships subordinated debt is an equity like instrument. It comes at the very, very last and has many more of the characteristics of a share than a bond. You get paid more to hold the subordinated debt, so you are being paid for the risk. If you are being paid for the risk over and above everybody else, when the risk materialises, you cannot expect to be paid in full.

**Deputy Pearse Doherty:** Cuirim fáilte roimh Mr. McWilliams to the committee. I will follow on from Deputy Phelan's questioning.

Mr. McWilliams has put on record his engagement with the Minister for Finance on that Wednesday night and we can read about it in his book, *Follow the Money*. The committee is gathering evidence and he will be the only person who can give us evidence on the other interactions he had with the late Minister. Will he clarify the number of telephone calls between him and the then Minister from 17 September onwards? It appears from his book that there may have been 12 telephone calls and two face to face meetings.

**Mr. David McWilliams:** That is right. When I say 12, it could have been 13 or 14. I was in China during all of this period.

**Deputy Pearse Doherty:** We will come to the detail in that respect.

**Mr. David McWilliams:** Then I had two face to face meetings with Brian Lenihan. The final one was on 4 October 2008 and I never saw him or met him again. It shows a very intense period of discussion and after that, I never met Brian Lenihan again. I met him once at a meeting of about 60 to 70-----

**Deputy Pearse Doherty:** If Mr. McWilliams will allow me, I will get into that because the Chair will keep me tight to my time.

**Mr. David McWilliams:** Okay, go for it.

**Deputy Pearse Doherty:** Mr. McWilliams referred in his book to the call on Friday, 19 September saying that when the then Minister rang to say they were contemplating a partial guarantee, he indicated that his view was that such a guarantee would just alert the world. Did the Minister explain what they were thinking about in respect of a partial guarantee?

**Mr. David McWilliams:** I would like to say of the then Minister that he was very discreet when he met me. He was very professional. He never gave me indications that anything was being decided. He more or less wanted to use me as a sounding board rather than anything else. He did not have to explain a partial guarantee. What it means is that if it is €50,000 or €100,000, the state will be behind it. I said to him that that was all very well if the bank run was Irish people going to ATMs, but the bank run would be the billions of euro of hot money being traded on international financial markets. What they would look at in the context of a partial guarantee was if all of the denials up until then had been wrong and that would spook them even more. I have worked on financial markets and seen how they work.

**Deputy Pearse Doherty:** I appreciate that. I just wanted to know what the then Minister was saying.

## CONTEXT PHASE

**Mr. David McWilliams:** He said they were going for that. I said, “Go for this and see does it work.”

**Deputy Pearse Doherty:** Mr. McWilliams said there were telephone calls on a daily basis. One of his comments regarding the calls was that the then Minister said his officials in the Department were dead set against a full guarantee. What did he say to Mr. McWilliams about the officials’ opinion on such a guarantee?

**Mr. David McWilliams:** I said to him, “You can be dead set against a full guarantee but a temporary one, if you know the facts ... up until now the officials had consistently understated the extent of the problem, so a full guarantee should only be introduced temporarily to attain the facts if the banking system was imploding.” What I thought he was saying about the officials was they still felt the banking system was not going to implode.

**Deputy Pearse Doherty:** Can I clarify this because we are taking evidence? Did the then Minister for Finance say to Mr. McWilliams that his officials were dead set against a full guarantee?

**Mr. David McWilliams:** Because they did not realise the extent. They believed a partial guarantee could work. Hours after the partial guarantee had been introduced on the Monday, it was very clear it had not worked. This is the whole point. It had not worked and, therefore, they had to realise that. Their hope was things were not as bad as they seemed and this is consistent with an entire orchestra of underestimating the problem. The partial guarantee was introduced. Had it worked, it would have been fantastic, but it did not. Then you are into a totally different reality.

**Deputy Pearse Doherty:** Did Mr. McWilliams have any other conversation with other members of the Cabinet during this period?

**Mr. David McWilliams:** I had one telephone call from John Gormley towards the end of the week I was in China and he asked me what was going on. I said, “You should tell me because I am actually in Beijing. I have no idea what is going on.” He had read the article in *The Sunday Business Post*. Again, it was more of a sounding board discussion. Apart from those two, I had no conversations with anyone.

**Deputy Pearse Doherty:** Did Mr. McWilliams have any conversation with John Gormley about a full guarantee?

**Mr. David McWilliams:** No. I told him to read what I had written and buzz me back, but he did not. They were pretty busy at that stage.

**Deputy Pearse Doherty:** With regard to nationalisation and conversations with the late Brian Lenihan, did Mr. McWilliams discuss the option of nationalisation? Can he inform us what Mr. Lenihan was saying about that issue if it was discussed?

**Mr. David McWilliams:** He asked whether nationalisation of one of the smaller banks could work. I said that it could but that it would not stop a bank run. We must be very clear about what we were trying to do. We were trying to prevent a national run on the banking system. What signal does it send by nationalising a small bank? It sends a signal that the bank is problematic. In a panic, does it say that people should not worry and that the rest of them are fine, or does it make a depositor wonder what will happen if one bank has been nationalised and is about to go under? I informed Brian Lenihan that exactly this tactic was taken by the IMF



in 1998 in Asia. There was a crisis in Thailand with the baht, followed by crises in Malaysia and then Indonesia. The IMF came in and said the countries should nationalise the bad banks, which they did. People thought that this was the organisation that did not see anything coming and was now telling us that it was limited to a certain bank. It created an accelerated bank run.

The second thing is that by nationalising a bank in the middle of a crisis, we take on all of the liabilities so we do not give ourselves the temporary idea to find the facts. This involves crystallising losses today.

**Deputy Pearse Doherty:** I appreciate that.

**Mr. David McWilliams:** This means not achieving what we were trying to achieve, to stop a bank run, and ending up with a large bill straightaway because people did not know the facts.

**Deputy Pearse Doherty:** I am not getting the merits of nationalisation as opposed to not nationalising. It is more the thinking of the then Minister for Finance. Mr. McWilliams seems to have had a large amount of contact with the second most powerful politician in the State at a time of major financial crisis. During that contact, did the Minister indicate any time that he was in support of nationalisation, particularly coming to the final point?

**Mr. David McWilliams:** No, as I said, Brian Lenihan was always incredibly discreet and professional and never indicated at any stage that he had any preference. This is as I would have expected. He listened and I suspect he had his own opinions. At no stage did he give an indication of where he was going. He was talking to a lot of people around this period. I felt very sorry for him because it struck me that it would be a bit like me being elevated to the Attorney General in the middle of the biggest constitutional crisis the country has ever faced and having to make a decision. Against that background, I probably would have called around to prominent lawyers and asked them what they think of this.

**Deputy Pearse Doherty:** The Governor of the Central Bank, Professor Honohan, gave evidence to the inquiry that Brian Lenihan “agreed with the idea of an overall guarantee but he also thought that INBS and Anglo should be nationalised there and then”. Was that expressed to Mr. McWilliams?

**Mr. David McWilliams:** That was never communicated to me, certainly not from Brian Lenihan. I said to him that if he did not know the facts, how do we know that the next problem will not be in one of the bigger banks. This is what subsequently ended up being the case. He never communicated to me any overall preference. He was always in listening mode.

**Deputy Pearse Doherty:** There was daily contact and Mr. McWilliams gave advice on the first day. What was the reason for coming back for advice on a daily basis and phoning Mr. McWilliams when he was abroad?

**Mr. David McWilliams:** He wanted to know what was going on in the international community. I was going to a World Economic Forum event like the one in Davos but in China. He was asking all the time what foreigners were saying. He was asking what people outside Ireland, looking in, were saying and I was keeping him up to date on the conversations I was hearing. There were loads of sessions on the banking system. The purpose for him calling me when I was in China was to see what people on the outside were saying. I told him at one stage that one of the deflating things about being an Irish person is that others do not think that much about us at all. We think that they think hugely about us but they do not. To the extent that I was listening to them, they were saying that all the European banks have problems, that the

European Union must come in and that Ireland was in the eye of the storm. They were all sure that there would be some pan-European solution.

**Deputy Pearse Doherty:** Mr. McWilliams says that he was very discreet in his contact but also that Mr. Lenihan doubted the regulator and the Governor of the Central Bank.

**Mr. David McWilliams:** I do not think one needs to be the Minister for Finance to doubt the regulator at that stage. Let us think about what has happened. The bank regulator has not seen the biggest bank catastrophe in a western democracy in a long time. Did Deputy Pearse Doherty doubt him? Brian Lenihan was saying that he was not too sure. A lot of people could not see how someone could miss this. It was more that he was incredulous.

**Deputy Pearse Doherty:** In the opening statement sent to us, although not in his oral presentation of it, Mr. Williams mentioned that in March 2009 he wrote articles that “the guarantee should be rescinded”. This is something that has been repeated time and time again. Can Mr. McWilliams inform the committee when he formed the view that the guarantee should be rescinded?

**Mr. David McWilliams:** The first part was that when I wrote these articles, my idea for the guarantee was a holding guarantee to figure out the problem and move on. The question is whether that should be in one year or two years. The time horizon is important. I remember saying to the Minister that if people are worried their money will not be in the bank when they go to get it out, and a two-month or three-month guarantee is given, that is not long enough to assuage the average punter that their money is safe. People must be given time sufficiently far out that they think they will be grand. Two or three months would have taken us to Christmas and was not that far. On the other hand, I said to him that auditors need to find out the facts about the maturity obligations of all the loans of the banks so that we did not cover too much.

**Deputy Pearse Doherty:** I appreciate that. Mr. McWilliams has provided that in evidence over numerous articles but the question is when Mr. McWilliams formed the opinion that it should be rescinded. The Chairman will cut me off and I also want to come to Mr. McWilliams’s contrarian views.

**Mr. David McWilliams:** During October, I wrote extensively that I was beginning to get worried about the nature of this. The first was about the inclusion of subordinate junior bonds and the second was the way of tying the weaker banks into other banks. I became worried that what I thought was an emergency measure to protect depositors was going to end up being used as a cloak to protect bank creditors.

**Deputy Pearse Doherty:** The banks signed the deed of guarantee on 24 October. Is it Mr. McWilliams’s position that the guarantee should have been rescinded after the banks signed up, or before?

**Mr. David McWilliams:** Absolutely. After meeting Brian Lenihan on 4 October, I found myself back on the outside, where I had been since 2000. Contact became sporadic and then there was nothing at all. I thought this was simply the way he was moving away from my thinking. My thinking was to be as flexible as possible and to try, as much as possible, to buy oneself time. His thinking, and the Department’s thinking, became harder and harder and then the migration towards we are going to pay everything became almost obvious to those of us who were worried about it. I began to write constantly warning people that this was being used as a way for full payment, in the case of a bankruptcy, which was never the objective.

I argued that we should move to what is called the savings and loans model in the United States. That model came about as a result of a big collapse there in the 1980s and 1990s where eventually they realised the cost of bank bailouts was going to be too much. They decided that what they were going to do was force the bondholders - the debtholders - to take equity which made them shareholders in the banks which, in a way, allied the banks and shareholders in the same place. That was increasingly my thinking and then the following became so obvious to me after NAMA. What NAMA did with the guarantee was it ensured that this country would end up selling our assets at a discount and buying our liabilities at a premium. That is morally wrong but is also a financial disaster. At that point we had created the ELA or emergency liquidity assistance. That meant the banks' liquidity was solid so one could have rescinded the guarantee, kept NAMA in place and nothing would have happened because the ECB was back in there and the Central Bank was back in. That was the idea by-----

**Deputy Pearse Doherty:** I am sure some of my colleagues will also pick up on that point.

**Mr. David McWilliams:** Yes.

**Deputy Pearse Doherty:** In an article published in *The Sunday Business Post* on 20 January 2008 Mr. McWilliams wrote:

A few years ago, one of Ireland's best known bankers indicated to me just how important it was that the Irish banks remained Irish-run in a downturn. His nightmare scenario was an Irish property market slump, coincident with a change of management in Ireland's major banks. In a crisis, he envisaged a response that was almost a type of financial war-cabinet, where bankers would have a direct line to the governor of the central bank and the Minister for Finance.

Without mentioning names, is this the same conversation Mr. McWilliams referred to in chapter 10 of his book *Follow the Money*, on page 129?

**Mr. David McWilliams:** It is the same conversation.

**Deputy Pearse Doherty:** Is it reasonable or not to say that the elements of the scenario that were outlined by the banker in 2005 to Mr. McWilliams appeared in the response in 2008?

**Mr. David McWilliams:** No, I do not think so. I think this was a conference that I was chairing. Because it was 2005 and because nobody at that stage was talking about property busts and our banking problems, and I was the chairman, so I said "Hold on a second. It is all very well to say that the economy is flying along. What happens not if, but when, this implodes?" I said what was likely to happen was that Irish banks would be bought by some other banks, Wilbur Ross-type characters or whatever it happened to be in the case. I then got the response that it would be better if Irish executive remained at the helm.

**Deputy Pearse Doherty:** The banker suggested, at that time, that there would be "a type of financial war-cabinet, where bankers would have a direct line to the Minister for Finance."

**Mr. David McWilliams:** That is what happened at the end. I remember writing, I think around December, that we had experienced, and I recall this, a financial coup d'état-----

**Deputy Pearse Doherty:** Yes.

**Mr. David McWilliams:** -----where the banks are running the show and the citizens are miles behind. That is what really happened in the period.

**Deputy Pearse Doherty:** I shall ask a final question but I will get a chance to comment later. Mr. McWilliams has provided the committee with extensive evidence in the form of documentaries and written material that he had written from the period 2008 which foretold the financial crisis. If it was as obvious as he has said, why was it ignored by what he called the insiders?

**Mr. David McWilliams:** That is a huge question. In a small country one gets significant vested interests. When a small country experiences a banking and property boom many people will make a lot of what looks like very easy money. That cohort of people have a clear incentive to vilify the maverick.

With respect to my own profession of economics, it amazed me at the time that so few, in any positions of power, did anything or said anything. I have found it amazing that people were swanning around with titles like bank expert and international bank expert. I said “Well, hold on a second. You were living in the country that had the most catastrophic bank crisis and you didn’t open your beak.” People watching this are entitled to ask that question.

There is a thing in Ireland which I refer to as conventional wisdom. When conventional wisdom sets in it is repeated by serious people. People say “He is not a serious person but I am a serious person because the guy beside me is a serious person.” Then he repeats the mantra and then mantras replace hard thinking. Once mantras replace hard thinking then every serious person buys into them. J.K. Galbraith said something very interesting about changing one’s mind. It is very hard to change one’s mind if one is a serious person. He said that when faced with the choice of changing one’s mind or finding the proof that indicates one does not have to, the vast majority gets busy finding the proof. Let us consider that thought in the context of this country. People like me were regarded with the view that it could not possibly be right, what this guy is saying, because the vista is too apocalyptic. One of the views was “Ah but he spent too much time abroad.”

I feel, and this is worrying for subsequent future years, that when this society coalesces around what I would call a simple truth, such as there will be a soft landing or the banks are well capitalised, it is an extraordinarily dangerous place to be. It means that, like lemmings, we all go over the cliff together.

As I have always thought, if one thinks of a quadrant of maverick, consensus, right and wrong, which applies to politics as well, if one is in that consensus and one is wrong then people adopt the view that we are all wrong together and sure that is grand. People think “We are all a bit stupid but we are all stupid together”. If one is in the consensus and one is right people think “Sure, we are all geniuses, that is great. Jesus, you are smarter than me. Oh my God, you are outrageously smart.” If one is a maverick and one is wrong then one is a maverick that is wrong. In that case one is incredibly isolated, laughed at, sneered at and regarded as being somebody who is not serious.

**Chairman:** Please conclude.

**Mr. David McWilliams:** Let me make this very important point. If one is a maverick and one ends up being right then one is a very uncomfortable person to be around.

**Chairman:** I want to round off this session by asking a simple question. I hope Mr. McWilliams gives me a short answer and then I shall call Deputy Higgins.

At the time of the guarantee, and in Mr. McWilliams’s engagements with Mr. Lenihan dur-

ing that period, was it his view that the banks were in need of liquidity or were they insolvent?

**Mr. David McWilliams:** That is a very good question.

**Chairman:** Can Mr. McWilliams answer my question?

**Mr. David McWilliams:** I can try. Illiquidity leads to insolvency. This is the distinction I hear all the time “Oh, they were just illiquid and they were not insolvent.” This is a very important thing to look at bank crises.

**Chairman:** Is it Mr. McWilliam’s view? Mr. McWilliams wrote extensively about this matter at the time.

**Mr. David McWilliams:** If the bank is illiquid it will go insolvent. That is the key. If one thinks it is illiquid then one has to prevent it from being illiquid because if it is illiquid it will go insolvent in a panic. It does not matter if one thinks the banks might necessarily be solvent. They will become insolvent when liquidity dries up so one has no choice.

**Chairman:** In 2008, Mr. McWilliams, in his book *Follow the Money*, wrote the following:

The question for the state is whether we are looking at a situation of illiquidity or insolvency. Pessimists say the banks are insolvent; optimists argue they are simply liquid. If it is insolvency, which is unlikely, then there are the normal longer-term measures to deal with bad debts.

In September 2008, in an article published in *The Sunday Business Post*, he wrote, “In contrast, a full guarantee would have meant full protection with creditors.” I am still trying to establish his assessment. Is it his view that the banks were in need of liquidity or were they insolvent which in layman’s terms means they were bust?

**Mr. David McWilliams:** If one did not inject liquidity they would go bust, definitely.

**Chairman:** I thank Mr. McWilliams and call Deputy Joe Higgins.

**Deputy Joe Higgins:** On 10 June 2001, Mr. McWilliams wrote on his website:

A property boom transfers huge wealth from wage earners to landowners with the banks sitting in the middle facilitating the trade. Wage earners become relatively poor ... Periods of speculative excess also lead, in every country, to extraordinary disparities of wealth. The “new rich” typically have their counterpart in a “new poor”. In Ireland, the property bubble has created an entire demographic section of highly indebted commuter-workers in tandem with a booming private client business for the banks and brokers.

Does Mr. McWilliams still hold to that analysis?

**Mr. David McWilliams:** Absolutely.

**Deputy Joe Higgins:** In an article dated 11 February 2001, Mr. McWilliams summarised how cheap credit flowing into a country can destroy it with illusions of wealth. He colourfully referred to the Spanish conquest of Latin America and the ransom which the Incas paid for their unfortunate emperor. In one week, he wrote, “the Spaniards plundered more gold [from there] than the entire continent of Europe produced in a year”. He continued, “A monumental mass of gold and silver crossed the Atlantic between 1540 and 1580 - Gold robbed from Latin America paid for everything”. He concluded:

## CONTEXT PHASE

There was hardly any lasting positive effect on the Spanish economy. How did Spain manage to waste one of the biggest financial windfalls in human history? And are there any lessons for modern Europe and Ireland in the history of the Spanish gold rush?

In Ireland, were there any equivalents of the indigenous peoples of Latin America who were robbed? If so, who were they? Were there individuals or institutions that were the equivalent of the Conquistadors? Were there individuals or institutions that were the equivalent of the Spanish aristocracy who Mr. McWilliams said in his article benefited hugely? How did Ireland manage to waste the biggest windfall in the history of the State?

**Mr. David McWilliams:** I have always liked using history to explain matters. The interesting thing about human nature is that it never changes. All these things happen again and again. At the time, what really struck me as fascinating from an economic historian's perspective was how Spain went from being the richest and most aggressive colonialist country in Europe in the 16th century to the poorest in the 17th century. How did that happen? There are many theories but one in particular struck me. What actually happened was that when they plundered all the gold from Latin America, it became easier not to work. Huge swathes of the Spanish manufacturing and agricultural sectors stopped because the Spaniards did not bother working. The people who actually got the most benefit from the Spanish plunder of the Inca gold were not the Spanish but the Dutch and the British who actually made the nails, the hammers, the guns and other products they sold to the Spaniards. That always struck me as interesting.

What the Spaniards had was a massive monetary stimulus, like in the context of Ireland. They woke up one morning and had all the money in the world. We woke up one morning and through the banks had all the money in the world. As had happened in Spain, when one has all the money in the world, prices and inflation rise and one abandons manufacturing. Why should we make stuff when we can actually sell a site down the road?

**Deputy Joe Higgins:** That is the question.

**Chairman:** As we have three minutes left, we need to move into the 21st century.

**Deputy Joe Higgins:** Why would the financial markets plough money into land and speculation rather than, in Mr. McWilliams's words, into science, technology and innovation, especially when the European Union had between 20 million to 25 million unemployed?

**Mr. David McWilliams:** It is less risky at the time. If the Deputy thinks about it, if one puts money into land in Ireland, how many tax breaks does one get? Loads. How much cheap capital does one get? Loads. Why does one get cheap capital? It is because the banks say they know what land smells and feels like. However, take someone like Apple's founders. They tell the banks they are going to build the most amazing computers out of a garage and will need X millions of euro to do so but have no guarantees or collateral, just that it is all in their head. The banks will not give someone like that money.

What I was trying to explain in the historical context was that one part of our economy would become bloated with capital while another part would become totally starved. That is where we have to go to in Ireland. We have a massively efficient multinational sector but very little domestic industry. I believe this is because of the way in which Irish capital was given out in the boom, namely, that it always favoured land. At the very top of the boom, 88% of every single loan given out by an Irish bank in this country was to a property or property-related investment. When one allows the banks be the sole arbiter of the distribution of capital, one

will get endemic short-termism. Why? It is because it drives up their share prices and bankers' bonuses are paid by share prices.

**Chairman:** The Deputy has one minute left.

**Deputy Joe Higgins:** I had better fast forward.

**Mr. David McWilliams:** That is the problem with starting with Pizarro.

**Deputy Joe Higgins:** In his written statement, Mr. McWilliams stated when one speaks against mainstream views, there are three phases, first, the open ridicule phase, second, the violent opposition phase and, third, everyone pretends they were on your side all the time phase. It reminds one that, apparently, 15 years after the Easter Rising, it would have taken Croke Park to accommodate everyone who claimed they were in the General Post Office that Easter.

**Mr. David McWilliams:** It is a bit like all those who were at the first U2 gig in the Dandelion Market.

**Deputy Joe Higgins:** In his written statement Mr. McWilliams stated, "Had the warnings been listened to and acted on, rather than dismissed and ridiculed, it would have been possible to avoid a banking crisis". Mr. McWilliams was a media commentator and had a media platform. What role does he believe sections of the mainstream media played in the generation of the property bubble? Was the media an impartial observer, vested interest or neither?

**Mr. David McWilliams:** I can only answer in the context of myself. Never once was anything I ever said muzzled by any editor. I have written for *The Sunday Business Post* all the way through. It is the newspaper of the economic, financial and political class. I went through three editors at that newspaper. Nobody ever telephoned me or censored my articles. I have also worked for the *Irish Independent* for many years. It is the largest newspaper in the country and, again, never once has anything I ever said been spiked or questioned by an editor. I am bit of a gypsy because I have worked for TV3, RTE and Newstalk, the main television and radio stations. Never once has anything I have written or suggested been interfered with.

It is not that there was a corporate line for people like me. Maybe I was like an exotic creature in the zoo in that they always have to have one of us. What is quite funny is the number of people who wrote about the boom saying it would all be grand and it was fantastic but are now saying they all saw it coming. I have never been muzzled or interfered with by anyone.

**Deputy Joe Higgins:** What about the media in general?

**Mr. David McWilliams:** As for the general attitude, I must admit I think it really is down to the specific journalists, writers, opinion writers and commentators. I really think that and do not think there was a general feeling. That said, if one picks up a newspaper and one has 1,000 words by David McWilliams stuck in the middle saying watch this, and one has 20 pages of glossy advertising in the supplement then clearly, there is a bias in there.

**Chairman:** I call on Senator MacSharry.

**Senator Marc MacSharry:** I thank Mr. McWilliams for his attendance. I have three and a half questions and so will move quickly. I will start in this century and will take all the books as read. Bearing that in mind, Mr. McWilliams mentioned the forest fire and so on. Going back to the era, for politicians specifically as opposed to economists, what to Mr. McWilliams indicated most strongly that not all was right with the regulator or the Central Bank in respect

of advice they were giving?

**Mr. David McWilliams:** I do not know. Where does Senator MacSharry want to start?  
Politicians-----

**Senator Marc MacSharry:** Let us say that I am Brian Lenihan. What would have stated clearly to me that the Central Bank and the regulator may not be what they needed to be in respect of what I was getting from them?

**Mr. David McWilliams:** On the most important thing, has the Senator ever played school-boy soccer?

**Senator Marc MacSharry:** No.

**Mr. David McWilliams:** Schoolboy Gaelic?

**Senator Marc MacSharry:** No.

**Mr. David McWilliams:** No sport. What sort of a man is the Senator at all? Does everyone know the expression “the banger” in football? Sometimes, were one to play schoolboy soccer, one would turn out for the under-12s and a lad with a beard who looked about 22 would turn up for the other bunch.

**Senator Marc MacSharry:** We would call him a ringer.

**Mr. David McWilliams:** Okay, so it is a banger in Dublin. If a banger turns up on a team and scores five goals against one, one knows there is something wrong. The young fellows are tiny and he is a big lad. Banks can be bangers too, by which I mean that if a bank emerges out of nowhere and begins to record profits that are extraordinary and way out of sync with what traditionally had been the case, either the people are geniuses or there is something going on. If one thinks about banking, it is a very simple business. One lends 2% or 3%.

**Senator Marc MacSharry:** Okay I get it.

**Mr. David McWilliams:** This is important. If I were a politician, I always would be hyper-sceptical of hyper-success because I would wish to know what actually was going on in there.

**Senator Marc MacSharry:** Mr. McWilliams believes the absence of the regulator and the Central Bank stating that this is a bank that took 100 years to get to €60 billion, as he stated earlier-----

**Mr. David McWilliams:** And doubled it in three.

**Senator Marc MacSharry:** Yes. The fact that the regulator and the Central Bank might not have been saying that was a big issue and should have been ringing alarms-----

**Mr. David McWilliams:** It is an enormous issue. I mean-----

**Senator Marc MacSharry:** I am not trying to lead but-----

**Mr. David McWilliams:** It is an enormous issue. However, what is much more important is to say it at the time and not to say it now, when everyone knows. I mean having the balls to say it when it was not popular and was not what everyone was saying. I mean saying “Hold on a second, I do not mean to rain on your parade but I feel this is wrong”. The regulator should



scare the daylight out of bankers. The regulator is the Elliot Ness of the gig and should swagger in. The regulator should be able to say “Come in lads and lock the door; I am worried about this”. Once one gets a situation where they perhaps are all a bit too cosy, the institutions - I am not talking about individuals - become part of the problem.

**Senator Marc MacSharry:** So they all went native. Is that it?

**Chairman:** That is a matter for the committee to decide. Senator, that is a leading question.

**Mr. David McWilliams:** Okay, but in terms of politicians-----

**Senator Marc MacSharry:** How wrong would the statement “they all went native” be? Is it right, is it wrong or is it a fair assessment?

**Mr. David McWilliams:** The Chairman-----

**Chairman:** If Mr. McWilliams will permit me for a moment, I will ask the-----

**Senator Marc MacSharry:** I was giving a number of options.

**Chairman:** The Senator’s option still is wrong. I ask him to reframe his question and not to use a leading question.

**Senator Marc MacSharry:** To ask the question again and a good few minutes have elapsed, in Mr. McWilliams’s mind, what act should have indicated most to the political leaders of the day that the regulator and the Central Bank were not interpreting the facts?

**Mr. David McWilliams:** The amazing thing is the Senator is looking for one act. There is an entire cornucopia of evidence.

**Senator Marc MacSharry:** The first act.

**Mr. David McWilliams:** For example, I recall writing extensively. I appeared on John Bowman’s “Questions and Answers” television programme in or around 2004 and alluded to the fact that all the commentary about Ireland was about a budgetary expansion at the time of approximately €3 billion. There was the whole budget thing and the Minister for Finance of the day was on the panel. I said the most important thing was not that €3 billion has been injected into the economy by the Government but that €23 billion has been borrowed in the same period by the private sector. The private sector was borrowing and injecting into the country eight times more than the budget surplus. In my mind, that would have been a moment.

**Senator Marc MacSharry:** As that was only one question and I have eight minutes, we must work better at this.

**Chairman:** Apologies, the Senator has a bit more time. He has two more minutes.

**Senator Marc MacSharry:** Four minutes.

**Mr. David McWilliams:** Does this go on every day? Is it like this all the time?

**Senator Marc MacSharry:** Yes it is.

**Chairman:** Be quick.

**Mr. David McWilliams:** Is there something I should know about?

CONTEXT PHASE

**Senator Marc MacSharry:** Mr. McWilliams said he was “slapped down by [his] own profession and the establishment”. Did he mean journalists or economists?

**Mr. David McWilliams:** Economists.

**Senator Marc MacSharry:** Would Mr. McWilliams say economists therefore were largely complicit in pushing the “Let’s party” agenda?

**Mr. David McWilliams:** While I do not think one could say that, I can say what amazes me. It seems to me that the single most explicit profession that almost made certain that one missed this was to be called an economist.

**Senator Marc MacSharry:** To move on from that and similar to what Deputy Higgins may have been asking Mr. McWilliams, does he think that other than himself, were the media largely complicit in pushing?

**Chairman:** I would withdraw the word “complicit”. I ask the Senator perhaps to ask Mr. McWilliams’s view on the behaviour of the media during the time.

**Senator Marc MacSharry:** Would Mr. McWilliams say-----

**Mr. David McWilliams:** Senator, I answered the question.

**Senator Marc MacSharry:** He gets the message anyway.

**Mr. David McWilliams:** I get the message and answered the question. In my case, and one is talking about making big documentaries for RTE, I was never ever-----

**Senator Marc MacSharry:** The joint committee knows that Mr. McWilliams was not. However, I am interested in his view of others and of the industry. Was there a herd mentality in the industry that drove the partying?

**Mr. David McWilliams:** Yes, there undoubtedly was a herd mentality.

**Senator Marc MacSharry:** That is good.

**Chairman:** A final question.

**Senator Marc MacSharry:** With regard to Economic and Monetary Union, EMU, I do not have the time to get into it now but perhaps other questioners will follow on.

**Mr. David McWilliams:** That is a shame.

**Senator Marc MacSharry:** It was where I would have liked to have focused more. In any event, should Ireland have joined the euro?

**Mr. David McWilliams:** Not at all. There is no shred of economic, financial or monetary persuasive evidence to suggest that. We are a country that trades overwhelmingly with the English-speaking world, with America, Britain and Canada, where our kids go. Where do Irish kids go when they look for work? I do not see them rocking up to Bordeaux. They go to the English-speaking world. There is no scintilla of economic evidence that suggests anything other than a prejudice. EMU is a continental system; we are an Atlantic race and an Atlantic economy. It makes no sense and it has been disastrous for this country.

**Senator Sean D. Barrett:** I welcome Mr. McWilliams, with whom I have had many previ-

ous meetings on these topics. During what years was Mr. McWilliams at the Central Bank?

**Mr. David McWilliams:** It was from 1990 to December 1993.

**Senator Sean D. Barrett:** In what section was Mr. McWilliams?

**Mr. David McWilliams:** The international economic affairs section, which at the time was dealing with the post-Maastricht build-up to EMU. That was my first job.

**Senator Sean D. Barrett:** Were issues of the prudential regulation of banks discussed when Mr. McWilliams's group got together in the Central Bank?

**Mr. David McWilliams:** The first time I worried about the way Ireland's economy might deal with a crisis was during the currency crisis in the Central Bank in 1992. I was working as an economist in the department that was dealing with the European Union and the putative European Central Bank, as it became. I was always amazed at the extent to which the people on the inside denied reality. The beauty about Ireland is that if a currency is overvalued, one can see it not in outflows of money but in the length of the queues of Toyota Corollas at Sainsbury's in Newry to buy cheap Harp for Christmas. Deputy Doherty will know this as someone from Letterkenny. If the Irish currency is overvalued relative to sterling, the currency of our major trading partner, Irish people go across the Border to buy stuff. We have a living economic experiment in Dundalk, Letterkenny and Lifford. During the currency crisis I pointed out to one of our bosses who was claiming there would be no crisis or devaluation that the *Irish Independent* was reporting on these queues of punters, although they were probably driving Ford Escorts rather than Toyota Corollas at the time. I got the impression that sometimes when one was inside, one was being dictated to by the tyranny of one's own peer group. If one's peer group consists of the fellows one meets in Brussels, conversations might not reflect the country one is supposed to be discussing. I refer to that psychology in a book called *The Good Room*.

**Senator Sean D. Barrett:** We were asking about the prudential regulation of banks. Did Mr. McWilliams ever come across the people who were in charge of that?

**Mr. David McWilliams:** No, it was a very stratified organisation. To tell the truth, I cannot recall who would have occupied that role.

**Senator Sean D. Barrett:** There was criticism in the Honohan report of the fact that approximately 15 out of 1,200 staff were working on prudential regulation of banks.

**Mr. David McWilliams:** Is the Senator asking what the other 1,185 were doing?

**Senator Sean D. Barrett:** That did not seem to indicate that it was much of a priority. I take it Mr. McWilliams did not meet the people who had the job of ensuring banks were solvent.

**Mr. David McWilliams:** I was 24 years old at the time. I had just completed a master's degree and it was my first job. What stuck with me, however, was the level of group think in the place.

**Senator Sean D. Barrett:** It argued very strongly against the McDowell report. It wanted to regulate the banks. Could Mr. McWilliams see it carrying out that task?

**Mr. David McWilliams:** The evidence when I was writing about this suggested that not only was it not carrying out its regulatory function but that it was also facilitating a type of ir-regulation which would lead to this crisis.

**Senator Sean D. Barrett:** When we joined the euro, against the advice of Mr. McWilliams and others, could we have regulated the flow of capital to keep it out of property and mortgages?

**Mr. David McWilliams:** The first quote on this was in an article in 2000, where I stated we could create a simple rule which would make sure the banks did not over-lend. At the moment, if an individual's house price increases, the bank can loan more against it. That is a built-in inflationary mechanism. In 2000 I came up with a backward looking house price index whereby the last house price increase was divided by the average of the index and then multiplied by the loan-to-value ratio, which means that the increase in prices reduces the amount of money that can be lent. It would be a dynamic system which could regulate itself. That is how one should do it. It is a simple statistical rule and it would be unbelievably easy to put in place. It would strangle house price inflation because house price inflation would limit the amount of money that could be lent. That is the sort of regulation we need.

**Senator Sean D. Barrett:** What could we have done about commercial property? We have heard evidence that commercial property was even more toxic.

**Mr. David McWilliams:** The most important thing for me in the Irish banking system was that we were running liability and asset risk, which is a terrible cocktail. The liability risk was the hot money coming in seeking a higher yield and financing commercial property. One stops commercial property prices rising by managing liability risk, that is, both sides of the balance sheet. If, for example, the regulator saw that a bank had just issued a short-term liquidity instrument of €500 million, which was happening all the time, it could have said, "Hold on a second, you cannot do that." The regulator would manage the bank's liabilities, which are the source of its delinquency, and as a consequence the bank would not be able to lend for commercial property. That is what we have to do in an open economy. Instead, however, we were looking at the asset side of the balance sheet and praying it would be okay but then panicking.

**Senator Sean D. Barrett:** Mr. McWilliams liked Sweden and Switzerland. I ask him to tell us what they did.

**Mr. David McWilliams:** Sweden did exactly the same as we did at the beginning. I told the then Minister that he had reached the last resort. Sweden had reached the last resort in 1992. When it had a similar boom-bust cycle, it introduced a blanket guarantee of all deposits, excluding subordinated debt, and by this means it stopped a bank run. Our objective was similarly to stop a bank run. Sweden quickly realised it would have to set up a bad bank and it did so extremely quickly. It wrote down the assets very quickly and minimised the cost. However, it also devalued its currency by 40%. Once a country devalues its currency, it is back to life. What happened in Ireland's banking crisis was that, amazingly, not only did we not devalue our currency, but it actually increased in value between 2008 and 2010. Sweden cut its interest rates to zero, but our interest rates went up after the crisis. We had an extraordinary set of policies that even a student taking leaving certificate economics would know was wrong.

**Senator Sean D. Barrett:** I would still like to ask Mr. McWilliams about Switzerland.

**Deputy Michael McGrath:** I thank Mr. McWilliams for coming before us. The warnings he gave from 2000 onwards have been well ventilated. I would like to discuss further his thoughts about the crisis period of autumn 2008. Irrespective of what he believes should have been done subsequently, does he believe the decision taken at the end of September 2008 to guarantee the banks was the right one?

**Mr. David McWilliams:** Yes, not only was it the right decision, it was the only decision that could have stopped a bank run. Over the last five years an amazing number of scenarios have been painted about what could have been done if, could, must, blah blah. Hindsight is a great luxury. At the time we had a banking system that had been set up to fail. It was not a matter of “if”, it was a matter of “when”. The combination of hot money and a bank run is the most vicious and contagious financial episode one can imagine. It is the financial equivalent of Ebola. One needs to come in with all possible interventions to reduce the perceived risk in the minds of people that their money will not be there when they go to the bank tomorrow. That is crucial. Much of my testimony has been about how, in God’s name, did we let it get to that situation. Once one is in that situation, however, one has to ask whether one knows the facts and, if one does not, whether one should take the risk that not knowing the facts might imperil the banking system. There is absolutely no way one can do that. It is in black and white in all my writing that the guarantee needed to be temporary in order to give us time to get into the banks to investigate the situation.

**Deputy Michael McGrath:** Mr. McWilliams referred to a period of two years.

**Mr. David McWilliams:** I said: “Let us say two years.” The phrase “let us say” is hardly a scientific formula. I told the then Minister that the period had to be sufficiently long to assuage the fears of Irish depositors but sufficiently short not to encompass everything. I said to the Minister it has to be sufficiently long to assuage the fears of Irish depositors but sufficiently short not to encompass everything. I said to him that is what auditors and civil servants do, they make those decisions.

**Deputy Michael McGrath:** Can I tease out your train of thought at the time and what you believed should have happened but maybe did not happen? On 28 September you said the only option is to guarantee 100% of all depositors, creditors in the banking system. After the guarantee on 1 October you described it as a masterstroke, a practical blueprint for the new financial architecture that will emerge from this global crisis but 18 days later you were critical of the Government’s approach. Why? What changed in the interim given that at that stage PwC was already in the banks assessing the balance sheets of the loan books? What did not happen in that 18 days that you believe should have happened?

**Mr. David McWilliams:** It is a very fair question. If the objective was to stop a bank run and that was achieved, that was a very important achievement. Had it not been done and had the Government gone down the road of allowing banks to go bust where would that have left us? That is a risk I do not believe any government can take.

The second idea is that the bank run had been stopped and the Government was beginning to take its own hands off its throat and breathe again to the extent that it had some calm. PwC was in the banking system. I do not think it is speaking out of school to say its report was not really worth much. It said the banks were quite okay.

**Deputy Michael McGrath:** They had not reported from 19 October.

**Mr. David McWilliams:** In that three week period, I had come through seven years of being ignored, seven days of being listened to and starting seven years of being ignored again. I was back on the outside for whatever reason. When I heard about the subordinated debt I thought this does not sound right.

**Deputy Michael McGrath:** You had earlier written about 100% of creditors being guar-

anted.

**Mr. David McWilliams:** I said shareholders do not get covered. In any receivership subordinated debt is regarded as equity. That is absolutely clear from what I said. It is an equity style instrument, not a debt instrument.

**Deputy Michael McGrath:** Approximately 1 billion of those were repaid during the guarantee. That is €1 billion.

**Mr. David McWilliams:** It is important because it shows a way of thinking. I write from my desk in my office. It struck me that we were moving towards using the guarantee not as an emergency measure but as a full payment mechanism in the event of bankruptcies.

**Deputy Michael McGrath:** In practical terms what did you expect to happen over those two or three weeks that did not happen?

**Mr. David McWilliams:** I expected the Government to make the guarantee more conditional. Brian Lenihan told me he liked speaking to me sometimes because I spoke English not economics and “economicese”. I told him to regard it as being like writing an insurance policy. If one writes an insurance policy for a young fellow to drive there will be small print to the effect that if he is drunk or taking drugs, etc., the policy is null and void. I told him to put in conditions to protect himself because we were still buying time. Everything was calm, amazingly, given what had gone before.

**Deputy Michael McGrath:** For a while, yes.

**Mr. David McWilliams:** I told him to use this to make sure he had enough wriggle room because that would give him the chance to do something permanent once he had the facts.

**Deputy Michael McGrath:** Absolutely. Do you believe that at that time, in September 2008, the value of the liabilities in the Irish banking system exceeded the real value of the assets?

**Mr. David McWilliams:** That the bank capital was gone?

**Deputy Michael McGrath:** That the banks were insolvent.

**Mr. David McWilliams:** They were definitely illiquid and were moving towards insolvency.

**Deputy Michael McGrath:** The guarantee resolved the liquidity issue in the short term at least but one could argue, and it is a fact, the banks were still insolvent.

**Mr. David McWilliams:** It is a fact, and we not only had the guarantee but also ELA. At the time of the guarantee the collateral in the banks was not regarded as worthy of collateral by the ECB. The Government could not go to the ECB and say it had a parcel of land in Westmeath which it reckoned was worth €10 million and ask for €10 million in cash because the ECB would not take it. There had to be negotiations with the ECB to say the Government needed emergency liquidity. It then began to emerge that the black hole in Anglo Irish Bank was enormous.

**Deputy Michael McGrath:** Do you believe with the benefit of hindsight that the banks were insolvent at the end of September 2008?

**Mr. David McWilliams:** I think some of the banks were insolvent. I discussed with Brian Lenihan the possibility that they could be. I said they would definitely be insolvent if he did not give them liquidity.

**Deputy Michael McGrath:** They got that and they were still insolvent.

**Mr. David McWilliams:** The interesting thing is they were all insolvent. All Irish banks needed a Government bailout in some shape or form.

**Deputy Michael McGrath:** They were all insolvent.

**Mr. David McWilliams:** They all needed help. None of them could survive on their own.

**Deputy Michael McGrath:** I know but insolvency is a very particular term with a particular meaning.

**Mr. David McWilliams:** Now we know that certainly the two smaller banks were insolvent. That became apparent-----

**Deputy Michael McGrath:** Can you name them for the record?

**Mr. David McWilliams:** This is why I said to the Minister he should have this savings and loan option, the debt for equity swap.

**Deputy Michael McGrath:** To clarify, for the record of the inquiry, who do you believe was insolvent at that time?

**Mr. David McWilliams:** It is obvious now that Anglo Irish Bank was insolvent.

**Deputy Kieran O'Donnell:** I want to deal with an area you can shed light on. Much of what we have dealt with to date is already in the public domain. I want to refer to your book, *Follow the Money*, where on page 17 you write the first encounter prompted a series of events in which the Minister began by peeling garlic and drinking tea in your kitchen and ended with the announcement of the bank guarantee less than two weeks later. I want clarification on several issues in that intense two week period. How many times did you meet Mr. Lenihan?

**Mr. David McWilliams:** I met Brian Lenihan twice in my life.

**Deputy Kieran O'Donnell:** You met him on 17 September.

**Mr. David McWilliams:** Yes and I met him on 4 October, which was a Saturday. I had been in China for seven or eight days.

**Deputy Kieran O'Donnell:** You had not met him-----

**Mr. David McWilliams:** I had never met him before and I never met him since.

**Deputy Kieran O'Donnell:** Between 17 September and 4 October how many telephone discussions did you have with him?

**Mr. David McWilliams:** As I told Deputy Doherty, I would say ten.

**Deputy Kieran O'Donnell:** In those conversations over that two week period what did you discuss? You were speaking to him daily.

CONTEXT PHASE

**Chairman:** In the interests of time management if there is new information that has not already been given in the testimony this morning or if you have nothing further to say please let us know because then we can move on.

**Deputy Kieran O'Donnell:** I have a line of questioning and I ask the Chairman to allow me-----

**Chairman:** My job is to ensure there is no repetition.

**Deputy Kieran O'Donnell:** I want to get the chronology of the events and discussions.

**Mr. David McWilliams:** As I told Deputy Doherty when I was in China I had no idea what was really going on here. There was an eleven hour time difference.

**Deputy Kieran O'Donnell:** That was from the 23 September. Give me an idea of the telephone calls you would have had.

**Mr. David McWilliams:** He was asking me, particularly when I was away, what were international financiers, economists and bankers saying about Ireland because this was part of the international financial crisis. I tried to tell him what I was hearing but on many occasions I had to tell him that with the collapse of the American financial system we were not that high on their radar screen.

**Deputy Kieran O'Donnell:** Mr. McWilliams wrote two defining articles. In the article of 21 September he wrote about guaranteeing deposits and made reference to a complete blanket guarantee for two years. Then on 28 September his article appears to be almost a carbon copy of the actual guarantee that was announced a few days later. When did Mr. McWilliams write that article of the 28 September?

**Mr. David McWilliams:** I wrote that one when I was in China.

**Deputy Kieran O'Donnell:** It is almost identical to what was in the guarantee.

**Mr. David McWilliams:** This is the very interesting thing. At no stage was I an adviser to the Irish Government. At no stage was I a senior civil servant. At no stage was I a central banker advising. At no stage was I in the regulator's office. I was one individual writing from my desk about what I saw going on. I have to be very clear about this. There were dozens of paid advisers deep in the system writing reports and advising. What struck me as interesting was that despite having dozens of advisers they missed the whole thing. I was writing on my own, as I had been since 2000, about what I felt was going on in the economy, and I still write on my own about what I think goes on in the economy.

**Deputy Kieran O'Donnell:** On page 26, the Minister asked Mr. McWilliams, "Are you sure about this, David?". This was only a few days before Mr. McWilliams's article of 28 September; when this article was being written was he aware of the direction the Minister for Finance was taking?

**Mr. David McWilliams:** No, at no stage did the Minister give any indication that he was thinking one way or the other, and this is what I would fully expect. He was emphatic about that. If the Deputy reads on from that note, the Minister said, "Are you sure about this?" What did I say? Will the Deputy read on?

**Deputy Kieran O'Donnell:** Mr. McWilliams said: "No, Brian, I am not sure it will work



but I am sure of one thing, we have no alternative.”

**Mr. David McWilliams:** And that is exactly what I felt, that we had allowed a banking crisis to engulf the State because we had not listened to the warnings that people like me gave at various stages. We had no reason to be in that situation at all but we got there.

**Deputy Kieran O’Donnell:** How does Mr. McWilliams reconcile that position with a blanket guarantee when his view, which he articulated over a long period of time, was effectively to burn the bondholders?

**Mr. David McWilliams:** There is absolutely no inconsistency. It is an important question to answer. What is written everywhere is that a temporary guarantee should be introduced to give Government, civil servants and monetary authorities time to find out the facts. Nothing permanent can ever be done without the facts.

**Deputy Kieran O’Donnell:** I know that.

**Mr. David McWilliams:** Does the Deputy believe that the Irish guarantee is long or short?

**Deputy Kieran O’Donnell:** Mr. McWilliams gave a two year guarantee.

**Mr. David McWilliams:** Let us be very clear.

**Deputy Kieran O’Donnell:** Mr. McWilliams articulated a two year guarantee.

**Mr. David McWilliams:** Let us be very clear. I did not give any guarantee to anybody.

**Chairman:** I will allow Deputy O’Donnell back with a final question but he should allow Mr. McWilliams to answer.

**Deputy Kieran O’Donnell:** No, but Mr. McWilliams articulated a two year guarantee.

**Mr. David McWilliams:** I will read out what the history of guarantees is to the Deputy. It is quite interesting.

**Deputy Kieran O’Donnell:** I have limited time. I am asking a very specific question.

**Chairman:** Mr. McWilliams spoke about a two year guarantee in his article and the guarantee itself worked out to be two years; Deputy O’Donnell is asking Mr. McWilliams what the correlation is between that.

**Deputy Kieran O’Donnell:** My question is a more specific one. Mr. McWilliams always articulated in the past that bondholders in a free market are risky capital. The blanket guarantee that was put in place guaranteed risky capital and subordinated debt. He articulated this in his article of the 28th of September and in his book at page 22, where, speaking to the Minister, he said, “However, I argued because the Irish banks funding has become so unstable, if we did not guarantee the funding as well as deposits the banks would come crashing down.” That is at variance with his previous articulation. Did the blanket guarantee cover bondholders?

**Mr. David McWilliams:** The Deputy has really mixed things up. I will tell him how. He is talking about the difference between a panic in a financial market and a period of calm. The whole point of a temporary guarantee is to make sure that everything is calmed right down by doing what has to be done, because the banks are going to go to wall, for no other reason than the fact that people will take their money out. That is the first thing.

## CONTEXT PHASE

The second thing is that during the period of calm when the liquidity issue has been addressed the Government must establish what is in the best interests of the State. Is it in the best interest of this State to pay out into perpetuity every single creditor of insolvent banks or is it in the best interests of this State to do what I said, which is to introduce a temporary guarantee and then move against the creditors?

**Deputy Kieran O'Donnell:** Two years is not a temporary guarantee. What happened at the meeting between Mr. McWilliams and the Minister on 4 October that caused the relationship to go sour?

**Chairman:** Mr. McWilliams should deal with the second question please.

**Mr. David McWilliams:** There are 14 examples of blanket guarantees given in bank crises around the world. The Irish guarantee is the third shortest. Can I explain that to the Deputy again? It is the third shortest. So it is as close to the minimum that has ever been given in the OECD and that involves Denmark, Ecuador, Finland, Germany, Honduras, Iceland, Ireland, Indonesia, Japan, Malaysia, Mexico, Nicaragua, Sweden, Thailand, and Turkey. That is the first thing.

The second thing is what happened to our relationship. Nothing. Brian Lenihan and I always got on quite well. What happened was I kept saying to him:

Make it conditional. Make it conditional. Don't be open ended. Make it conditional. You are in the driving seat now. You own them. You are the boss. Make it conditional so that we are not in a situation where we end up paying off risk capital. You have to stop the crisis, which is absolutely essential. Once you have done that you are in the driving seat. You do what you want.

That was what the opportunity was. We could have done what we wanted. Napoleon said, "to govern is to choose". A Government has to make choices.

**Chairman:** We are now going back into another century. We will stay with the crisis period.

**Senator Susan O'Keeffe:** What happened? Did the Minister not take Mr. McWilliams's advice to make the guarantee conditional?

**Mr. David McWilliams:** Yes.

**Senator Susan O'Keeffe:** How did Mr. McWilliams feel about that?

**Mr. David McWilliams:** Was I surprised? It was terrifying. The articles that I was writing in the weeks afterwards were all warning "hold on a second, we have to make this conditional, we have to make this temporary, this has to be holding, it is doing its job in the sense that my Mum is not taking her money out of her bank account". We have that period of calm. Thereafter I suspect that there was almost a sort of a banking *coup d'état* in policy. It seemed to me that the interests, not so much of the banks but the bank owners, the creditors, were being elevated, and I had been told that the ECB had said that no bank can go under. I believe the inquiry has different information now.

**Chairman:** The best way to describe it is as assembling information.

**Mr. David McWilliams:** I had been told at the time that the ECB was saying that no European bank could go under at any stage. I wrote at the time that if that was the ECB's directive,

it should pay for the consequences of this policy. If one thinks about it, in the case of a bank going under, only four groups or institutions can pay for it: the taxpayers of Ireland, the taxpayers of Europe, the ECB itself, by injecting a promissory note-type instrument, or the creditors. We had the choice and we did not seem to negotiate. I have no idea why. I think this is the European element, which I am sure the committee is coming up to, as to what the ECB involvement in all this was.

**Senator Susan O’Keeffe:** In the years that Mr. McWilliams was writing all his warnings, did anyone ever come up to him at a conference, on the street, in the pub, or anywhere at all? Did they write to him or telephone him and tell him he did not know the half of it, or something similar? He says he was the outsider and that he wrote 1 million words, that he was issuing warnings and nobody came to him or called him-----

**Mr. David McWilliams:** No, that was-----

**Senator Susan O’Keeffe:** -----in the official arena. I am asking whether there were people who said to him quietly that he was right.

**Mr. David McWilliams:** No. It is still gratifying when I am in a pub and so many people come up to me and say, “Thanks. We were going to buy this house but we watched one of your programmes and we didn’t”. The public and the establishment had totally different views. The members of the public thought I was saying things they thought in their gut was right. I never had any conversations with anybody in the political process, the big banks, the regulator or the Central Bank. In 2005, Deputy Enda Kenny asked me to address the Fine Gael parliamentary party in Portlaoise. Were any of the Fine Gael committee members there?

**Chairman:** We do not need to know who was there, we just need to know what was said.

**Mr. David McWilliams:** I am on tricky business with this language. I talked about a concept I have come up with, “deckland”, which was this part of Ireland that was emerging. Deputy Enda Kenny said it was interesting. That was the only time. Deputy Higgins invited me in to have a discussion with him and his party in the Teachers’ Club in Parnell Square in 2006 or around then. Only the extreme right and the extreme left consulted with me.

**Senator Susan O’Keeffe:** When the Minister left Mr. McWilliams’s house that night, having had the garlic and the tea, how would Mr. McWilliams describe what he was feeling on a scale on one to ten, if one was very concerned and ten was very comforted?

**Mr. David McWilliams:** That is a very interesting question. It was very strange for me, because having been ignored for seven years, suddenly your man was in our kitchen. That was a very strange feeling. I have always said that I felt incredibly sorry for Brian Lenihan the individual, because I felt that here was a good man in the middle of an enormous financial storm, having been put into the job in recent months. He was really trying to get on top of things and he was really open. That was the interesting thing. He never closed himself off. He was always saying, “That could work, that might work”. How did I feel? I felt that if something was not done in order for him to appraise himself of the facts, we would have a monumental crisis.

**Senator Susan O’Keeffe:** Is Mr. McWilliams saying that there was still a significant shortage of facts available to the former Minister?

**Mr. David McWilliams:** It was total. When one goes to find out what is going on, one needs facts. One needs the hard numbers. Is it 1 million or 10 million? The impression I got

was that he and the people around him - the paid advisers and all these people - were not in possession of the facts at all. Therefore, they could not do anything permanent. They had to do something temporary because they had to calm it down in order to find the facts. As a former investigative journalist, Senator O’Keeffe knows that one needs to dig.

**Senator Susan O’Keeffe:** Mr. McWilliams talks about reading and watching credit swaps, repo spreads, figures and facts, I suspect, to say that he was not just saying these things, he knew them. Is he saying that he was the only one doing that? Were other people doing that exercise, or was he just pursuing and digging?

**Mr. David McWilliams:** All these things are online. If one wants to see the prices that AIB is paying investors to borrow money from it-----

**Senator Susan O’Keeffe:** One has to look .

**Mr. David McWilliams:** Yes. One goes online. There is a thing called Bloomberg, which is a sort of financial market survey. It was there all the time. The price of Irish credit default swaps - for example, if one wanted to buy Bank of Ireland shares and bought insurance to protect against the risk that Bank of Ireland would go bust - was going through the roof, so people were thinking that this bank was in trouble.

**Senator Susan O’Keeffe:** Most people were not looking at that.

**Mr. David McWilliams:** They did not seem to be. This is public information.

**Senator Michael D’Arcy:** Is Mr. McWilliams satisfied that the Minister was on top of his brief when he was discussing those matters with him in early September?

**Mr. David McWilliams:** He was on top of the brief he was given. This is an important distinction. At a time of crisis, there is a massive move for institutional self-preservation. It is a general rule. It is human nature. If there is a recurring theme in this process, it is that reality was denied at every stage. People did not want to look into the vista and admit that it could be that bad. This may be the pinnacle of that process.

**Senator Michael D’Arcy:** Can I ask Mr. McWilliams about the telephone call he received from John Gormley? When was that? Was Mr. McWilliams in China at that stage?

**Mr. David McWilliams:** I was in China. I did not know John Gormley particularly well. The thought that went through my mind at one stage was, “Why didn’t they ring their own bloody advisors? Why are they ringing me?” I never got paid a cent for all this. If I had actually billed out all this, I would be a reasonably wealthy man. John Gormley called me and asked what I thought. I told him I was in Tianjin, which is a city in China that I had never heard of, but Senator D’Arcy said it has 11 million people in it. There was a sense of “I think this is happening, I’m not too sure”. What struck me was why they had to telephone a bloke in China to find out what was going on right under their noses.

**Senator Michael D’Arcy:** Did Mr. McWilliams ask him?

**Mr. David McWilliams:** I did, jokingly.

**Senator Michael D’Arcy:** What was his response?

**Mr. David McWilliams:** The response was that up until now, everything they had been told

had been wrong. That is true. They were told there would be a soft landing. That was wrong. They were told the banks were well-capitalised. That was wrong. They had been told prior to that that the Irish economic boom was based on fundamentals and that was wrong too. Eventually, if one consistently gets advice that is wrong, one says, “There is one dude over there who is writing all the time. He seems to have a fairly good handle on it. We’ll ring him”.

**Senator Michael D’Arcy:** Did Mr. McWilliams get the impression from his conversations with two Ministers at a crucial time that there was an inability within-----

**Chairman:** Question the ability, not the inability.

**Senator Michael D’Arcy:** Was the ability available within the Department of Finance, the Central Bank, the Regulator’s office-----

**Mr. David McWilliams:** I do not think the Senator needs me to answer a question whose answer is so self-evident.

**Senator Michael D’Arcy:** We touched briefly on the PwC analysis carried out on behalf of the Department of Finance. Did Mr. McWilliams have sight of any reports?

**Mr. David McWilliams:** No. I must reiterate that during the period from 2000 right up to now, I did not have sight of any data. As I told Senator O’Keeffe, what I was doing was looking at what was publicly available.

**Senator Michael D’Arcy:** So it was Mr. McWilliams’s analysis-----

**Mr. David McWilliams:** It is not always analysis. In Ireland we have what I term the “nose-tipping” approach to conversation, whereby someone says “Ah, you wouldn’t know now what I know”.

**Senator Michael D’Arcy:** Is it instinct?

**Mr. David McWilliams:** It is not instinct, it is knowledge. There is nothing instinctive about this. It is about having worked in the system, understanding the system, looking back at the academic literature - Senator Barrett would be aware of the historic aspects - or going back as far as the bloody Incas if we have to in order to find repetitive cycles.

**Senator Michael D’Arcy:** What is Mr. McWilliams’s view on the PwC report, which was published early in 2009 following the completion of the fieldwork relating to it in December 2008? How does he tally what it contains with what happened when NAMA was established some 13 months later with a 50% writedown?

**Mr. David McWilliams:** I cannot tally the two of them. Can the Senator?

**Senator Michael D’Arcy:** I am asking Mr. McWilliams.

**Mr. David McWilliams:** No, I cannot.

**Chairman:** Next question.

**Senator Michael D’Arcy:** Mr. McWilliams is a very experienced broadcaster and commentator. He does not give away much by his body language but I did detect some dissatisfaction on his part regarding the use of the term “unpatriotic” in respect of him and other contrarian commentators. What is his view on the put downs that were placed in the public domain

regarding him and others?

**Mr. David McWilliams:** It is very hurtful. It is designed to hurt.

**Senator Michael D’Arcy:** Intentionally?

**Mr. David McWilliams:** We are all adults. It was difficult for my wife and other people around me, particularly my mother. Irish mummies read all that stuff. Really nasty things were written all the way through with regard to ability, motives, etc. Sometimes people write things they do not really mean. If one looks back at some of the comments, they were very personal and quite nasty. However, I am the sort of person who becomes emboldened by that kind of carry on. Maybe it is something deep in my psyche. There is the really nasty stuff and then everyone pretends that they are on one’s side all the time. The put downs and all those quite slanderous articles were difficult to take but we are big boys and that is the cut and thrust of life.

**Senator Michael D’Arcy:** Mr. McWilliams clearly has analysis based upon the 14 blanket guarantees that were extended internationally at various times. How does the Irish blanket guarantee rate in terms of its expense in the context of GDP?

**Mr. David McWilliams:** It is an interesting question and I have the hard data relating to it here. The average fiscal cost for the whole thing in Turkey, Thailand, Sweden, Nicaragua, Mexico, Malaysia, Korea, Jamaica, Indonesia, Finland and Ecuador was 26.8% of GDP. Those countries range from the highly developed, namely, Sweden and Finland, to the underdeveloped, namely, Indonesia. When all the numbers are done and when NAMA is closed down, I think the Irish case will be somewhere around there.

**Chairman:** It will reflect that average, yes?

**Mr. David McWilliams:** It seems that way.

**Deputy Eoghan Murphy:** I thank Mr. McWilliams for attending. One area the inquiry is obliged to examine is the relationship between developers and politicians. In Mr. McWilliams’s view, is there a relationship between political donations and political decision making?

**Mr. David McWilliams:** Is there a relationship? I cannot imagine that one would give money to anyone and not expect something back. Let us consider the position of children. When one gives money, sweets or a present to somebody, does one now expect to get something back?

**Chairman:** I must advise the witness and the questioner that we are moving into generalities. We could have a conversation about how someone thinks something happens over a cup of tea. We must discuss specific matters.

**Mr. David McWilliams:** That is fair enough.

**Deputy Eoghan Murphy:** Mr. McWilliams touched upon this matter quite a few times in his book, *Follow the Money*, and stated that politicians could not make decisions that might inconvenience builders and bankers. He proceeded to relate two stories, one about Bertie Ahern and the second about a golf classic hosted by Brian Cowen. Was he making an implication when he made that statement and followed it up by relating those two stories?

**Mr. David McWilliams:** As far as I know, I did not think we are in the business of mentioning names here. So I think it is impossible for me to answer that specific question.

**Deputy Eoghan Murphy:** In his book Mr. McWilliams stated that, in the context of the 2007 general election, 71% of donations to political parties came from people involved in property development.

**Mr. David McWilliams:** Yes. I was making a Galway tent connection between a political party and a very significant industry. I do not think that anybody will refute the fact that proximity of a political party - or of many political parties - to certain parts of industry probably means they are going to be treated differently. This is not exclusive to Fianna Fáil. I did a one-man show in the Abbey Theatre and I was always intrigued as to how the former leader of Fine Gael, for example, got gambling or speculative debts written off by AIB-----

**Chairman:** Mr. McWilliams should not stray into the area of identifying individuals. I already pulled him up in that regard.

**Mr. David McWilliams:** It always seems to me that maybe this stuff goes on. My point is that I think one is right to get windy when one sees donations coming from one sector. However, I really cannot elaborate on this because of what the Chairman has said.

**Deputy Eoghan Murphy:** This matter is interesting, particularly in terms of the idea for a guarantee that Mr. McWilliams was promoting and the fact that the actual guarantee that was implemented was different to that.

**Mr. David McWilliams:** Yes, it was extremely different.

**Deputy Eoghan Murphy:** Professor Edward Kane, who came before us previously, has indicated:

A government's willingness to rescue different firms lies on a continuum and is influenced by several variables. In particular, a firm's access to political elites grows with its interconnectedness, geographic footprint, and the number of employees and creditors that can be persuaded to contribute on its behalf to re-election campaigns.

He was making a statement about the American situation.

**Mr. David McWilliams:** Yes and that is a fair point. The committee has one of the very few guys, namely, me, who spent nearly ten years issuing warnings about all of this, including the nexus between bankers and developers and how this was sucking away the resources of the country. Although I made all of those connections, my major concern, as an economist and a commentator, lay in the fact that if one sees all that stuff emerging, it only reinforces the need to have really strong, independent regulation. People do what people do and this constantly underscores the need for strong, independent, highly vigilant regulators. The most important point about regulation is that one can have the best regulation in the world but if one does not police it, it is not worth the paper on which it is written. As such it is better to have fewer points of regulation which are well policed rather than to have pages and pages of unpoliced regulations. What the Deputy has painted is a picture which underscores absolutely the need for strong, independent, unimpaired, almost loner-type figures. There is no problem with being a loner and not having a gang to hang out with in order to police what the Deputy speaks of.

**Deputy Eoghan Murphy:** Does what Professor Kane talks about in terms of rescuing different firms bear any relationship to how Mr. McWilliams's proposal for a guarantee evolved?

**Mr. David McWilliams:** What the Deputy is suggesting is that the guy who was most

against the bankers ends up in a situation where a consequence of what he thought absolutely necessary was that certain banks would be saved. If the Deputy looks at my writings-----

**Deputy Eoghan Murphy:** No, sorry. Mr. McWilliams had an idea which was not implemented in the way he thought it would be.

**Mr. David McWilliams:** Yes. I would have thought - and I said it in all my writings - that the normal rules of corporate finance should apply in the case of insolvency. Therefore, the guarantee would have been rescinded as the liquidity problem was already plugged. Then one would have lined up all the creditors in a room and had a bank resolution mechanism as that is the system whereby we as a society deal with bad banks. At the very top, one would have what I call “trust creditors”. They are creditors in trust, which is to say depositors. When my mum goes to put her savings into the bank, she does not realise that technically she is lending money to the bank. In her head, it is a nest egg, something for grandchildren and what she has put away for a rainy day. She does not have any realisation that technically in the event of a bankruptcy, she is a lender. Therefore, my solution, as I wrote at the time, was that as simple depositors trust the system, they should be regarded as trust creditors and encircled. Under that, one then has the normal hierarchy of creditors which everybody understands. It happens every single day in this country in receiverships. That is the system we could still have. That answers the Deputy’s question. If there were massive insolvencies, they would have been dealt with in the normal way.

**Deputy Eoghan Murphy:** I come then to resolution measures. In his writings, Mr. McWilliams makes implications around some of the resolution measures that followed the guarantee, for example the design of NAMA.

**Mr. David McWilliams:** I was very in favour of the Swedish approach as it looked like a good blueprint from a country that does not get much wrong. Over the years, the Swedes seem to be very good at public administration. What they did was to write down their loans incredibly quickly, which had the effect of allowing the banks that were good to begin to lend again very quickly. This materialised rapidly in the significant growth of the Swedish economy in the 18 months after their banking crisis. My feeling was and to a degree still is that the NAMA process was so slow in writing down and it never freed up the banks that had got the stuff off their balance sheets to begin the process of lending. We remained in what Keynes would have described in a traditional liquidity trap for a long time. Irrespective of how low the interest rate was, people had too much existing debt and did not want to borrow any more while the banks had too much bad debt and did not want to lend.

**Chairman:** I need to move towards wrap up. This is way over time.

**Deputy John Paul Phelan:** Deputy McGrath asked questions earlier about insolvency versus liquidity and Mr. McWilliams indicated that on the night of the meeting on 17 to 18 September, he did not have any evidence that there were insolvency issues within some of the-----

**Mr. David McWilliams:** I did not have any evidence, but I said that if one let them go illiquid, they would become insolvent. The interesting thing is that the best banks, if they are margin driven and have heavily exposed one side of their balance sheets to short-term debts, will go insolvent if one lets them be illiquid.

**Deputy John Paul Phelan:** I put a quote to Mr. McWilliams from *Follow the Money*. It states: “The Minister indicated that the problem was more acute. The most revealing thing



about our conversation was that it was AIB not Anglo Irish that had the most severe funding problems”.

**Mr. David McWilliams:** That is the one that put the wind up me. I was asking if it was just Anglo Irish Bank and he mentioned all the banks. I will explain what happens when things are going well. Let us say I am good for my money and Deputy Phelan gives me €100 and I say I will give it back in 100 days. Deputy Phelan will say that is fine. If he then hears that I have given €80 of that €100 to someone to whom I owe money and that fellow has given money to someone he owes, he will say he is only giving me the money for a week.

**Deputy John Paul Phelan:** What I want to ask is whether it raised the fact that there were solvency issues rather than a liquidity issue in AIB. He has said it did.

**Mr. David McWilliams:** No. What the Minister was saying was that one of the bigger banks had a short-term liability profile which would have made it illiquid. The Deputy should think about the bank he is talking about. It was the biggest bank in the country.

**Deputy John Paul Phelan:** I understand. My final question relates to an article I have just found from the *Irish Examiner* on Monday, 2 November 2009, which was written by Seán Conolly, the political correspondent. The article was on a war of words that erupted between Mr. McWilliams and the late Minister, Brian Lenihan. It was a year and a bit after the guarantee. I refer to a specific quote from the late Brian Lenihan who said, “He contacted me through my brother, Conor, and said he wanted to meet me and I happened to be meeting another friend in that part of the city that evening who lived further up the road”. That is a direct contradiction of the outline of the initial contact Mr. McWilliams had.

**Mr. David McWilliams:** On the contrary, it is not a contradiction at all. Brian Lenihan scribbled down a number to me. I went to look for it that night. I looked for it but could not find it. I had his brother’s number because I had been the breakfast presenter at Newstalk and the brother had been a regular on the show. I telephoned the brother and said “Listen, your brother gave me his number. I have not got it. Can you give it to me?” and he said “Yes”.

**Deputy John Paul Phelan:** He indicated furthermore that he really did not go out specifically to meet Mr. McWilliams and said he happened to be in that part of the city.

**Mr. David McWilliams:** Come here. If someone rocks up in your kitchen, he wants to meet you. I did not rock up in his kitchen.

**Chairman:** I note to Deputy Phelan and Mr. McWilliams that the entry of late information into an inquiry towards the close of a session is not usually how we go about our business. We usually inform witnesses before coming in. I would not expect Mr. McWilliams to deal in detail with documentation presented at the end of a hearing.

**Deputy Pearse Doherty:** Mr. McWilliams mentioned that this was obvious to anybody that was trained, which is important. I want to take Mr. McWilliams through 28 January 2008. His former employer, UBS, had issued a recommendation at that time. It issued a sell recommendation on AIB and Anglo Irish Bank as a result of mounting fears that they might suffer a rise in bad debts due to their exposure to falling commercial property markets. UBS estimated a 30% possible decrease with rents remaining the same.

**Chairman:** That needs to be supported.

## CONTEXT PHASE

**Deputy Pearse Doherty:** It is the factual note. Ian Keogh reported on 24 February that within two hours of this call being made, 34% of the value of the Irish banks was stripped away. Mr. McWilliams said that this was obvious to anyone who was trained. What information did UBS have to be able to make such a strong recommendation on AIB and Anglo Irish Bank that the Department of Finance, the Regulator, the Governor or politicians could not see?

**Mr. David McWilliams:** That is a very good question. A bank like UBS will have a bank analyst whose job is to look at banks all the time. The analyst would have been able to see the complexion of the loans given out by the Irish banks; how much was for tracker mortgages and how much was for commercial property, etc. The person at UBS was doing what I had been doing for years previously, namely, trying to value the commercial property for which these banks were lending enormous amounts of money. One values such an asset by estimating the stream of income that will come from it and multiplying it by a multiple. UBS probably saw that the stream of income coming from Irish commercial property was falling because much of it was empty, similar to the ghost estate situation. UBS was saying if the stream of income from the commercial property goes to zero, the loan goes bad immediately. The only way the loan can be made good is if one continues to lend money against it, which is what happened in Ireland. This is the type of analysis UBS would have come up with and it would have said a chunk of the balance sheet could go bust. UBS would have asked what the share price of the company was and realised it was very high. Given UBS was not being paid to take such a risk, it would sell it.

**Deputy Pearse Doherty:** Mr. McWilliams said it was obvious to the trained eye.

**Mr. David McWilliams:** It is totally obvious.

**Deputy Pearse Doherty:** Even at this stage, could any excuses be made for those in the institutions and the Department who were trained but who did not find it obvious and did not see it?

**Mr. David McWilliams:** It is very difficult to suggest. If a medic or immunologist misses a plague, what would people suggest about his or her competence?

**Deputy Pearse Doherty:** In an article of 25 May 2008, Mr. McWilliams wrote:

The boom in Ireland was little more than a scam. Ireland was the victim of a financial *coup d'état* whereby a cabal of the banks and developers, with the blessing of the Government and cheer-led by various vested interests who were getting their grubby cut, took over our economy.

Does Mr. McWilliams stand by this statement and, if so, how can he back up the statement that it was done with the support of the Government of the day?

**Mr. David McWilliams:** I will play a recording of comments I made during a debate in 2003:

*(The joint committee heard an audio recording)*

The Irish housing market is a scam. It is an enormous financial swindle that could potentially confine an entire generation of young Irish workers to years of bad debt. Far from being a reflection of economic vitality and fundamental demand, the housing bubble is, in the main, a vacuous financial confidence trick that has been foisted upon us by an alliance of banks and landowners. Today in Ireland, the price of the average house is close to ten times

the average wage. This represents an economic failure on a monumental scale. Behind this nonsense is excessive and irresponsible lending from our financial institutions. The situation would be laughable-----

**Deputy Pearse Doherty:** My specific question was how Mr. McWilliams can say definitively that the Irish Government supported this financial *coup d'etat* by the bankers and developers. What is the evidence to back up the statement?

**Mr. David McWilliams:** Because there was no evidence of a push back from a way of managing our economy which was happy, at the top of the boom, for 88% of every loan, €88 of every €100 given out, to go to property. One cannot run a modern economy or a democracy like that.

**Chairman:** I return to the issue of the guarantee. In a newspaper article of 28 September 2008, entitled State guarantees can avert depression, Mr. McWilliams discussed the costs of various options that could be taken regarding nationalising banks and stated:

There is another reason for not nationalising, and it is taxpayers' money. Once you start using taxpayers' money, you have to be careful. The lesson from the US in the past week is that using taxpayers' money is unsuccessful and deeply unfair. The beauty of guaranteeing deposits is that you use no money – not a penny.

With the benefit of hindsight, do you believe these comments underestimated the potential cost of the State guarantee?

**Mr. David McWilliams:** The comments were about the immediate cost. At the time, the options before the State were to incur many billions of euro of costs immediately with the notion of crystallising losses. The article explicitly said it would not cost a penny at that moment. The idea was to buy time by doing it temporarily. No banking crisis can be dealt with without cost. At the time, major discussions were taking place about budget deficits-----

**Chairman:** While I do not believe in pushing people to “Yes” or “No” answers, with the benefit of hindsight, do you think your comments underestimated the potential cost of the State guarantee?

**Mr. David McWilliams:** No, because they were about the immediate cost of a guarantee. The idea of a temporary holding guarantee was to prevent a bank run which would destroy people's savings. When one is in government, one can do these things, it is one's decision for one's country. The Government could have minimised the cost.

**Chairman:** In your opening statement, you said you had published 2.5 million words.

**Mr. David McWilliams:** I have published 1.2 million words, and I have read nearly all of them during the past three weeks.

**Chairman:** Excellent, because I have a question on them. Did you ever get it wrong?

**Mr. David McWilliams:** We all get lots of things wrong.

**Chairman:** What did you get wrong?

**Mr. David McWilliams:** Wow. This is a trick question.

**Chairman:** It is not.

## CONTEXT PHASE

**Mr. David McWilliams:** While we all get lots of things wrong, I do not think I got anything wrong during the period we are discussing. I am an economic commentator. I am an independent economist and have never been paid by the State for advice.

**Chairman:** I had many professions before I came here and I have got things wrong in those professions. It is not just politics.

**Mr. David McWilliams:** Of course one gets things wrong.

**Chairman:** Give us an example of something you got wrong in 1.2 million words.

**Mr. David McWilliams:** I get things wrong every day.

**Chairman:** Give us an example. In the 1.2 million words you have written about the economic crisis in this country, did you get anything wrong?

**Mr. David McWilliams:** It is an unfair question. One gets things wrong every day and one hopes to learn from them.

**Chairman:** In terms of getting things right for the future, what is your assessment of the Irish Government's level of preparation for the banking problems that emerged in September 2008? How well was the State prepared? Are Irish policy making authorities better prepared today, particularly regarding the regulation of the property and banking sectors?

**Mr. David McWilliams:** We were totally unprepared in 2008 because we had not listened to any of the warnings. I am not sure I see anything now that would prepare us again for such an eventuality. The most important thing is to be hyper vigilant on a sector which, if managed well, can serve the needs of the economy very well but, if managed badly, can lead to a financial catastrophe.

**Chairman:** Is there anything else you would like to add before we conclude?

**Mr. David McWilliams:** No.

**Chairman:** I thank Mr. McWilliams for his participation today. It has been a very informative and valuable meeting which has added to our understanding of the factors.

*Sitting suspended at noon and resumed at 12.15 p.m.*

## **Professor Terrence McDonough**

**Chairman:** I welcome Professor Terrence McDonough and apologise for the late commencement of session B, which is to discuss issues relating to the international, EU and domestic policy contexts to the banking crisis in Ireland. Professor McDonough is professor of economics at NUI Galway and has a PhD in economics from the University of Massachusetts at Amherst. Before joining NUI Galway in 1995, he held posts at the Institute of Industry Studies at Cornell University, Canisius College, Buffalo, and Dublin City University. He has published numerous books and academic articles, was on the editorial board of the Review of Radical Political Economics and is currently on the editorial board of the International Journal of Pluralism and Economics Education. His current interests include globalisation, American and Irish economic history, political economy, the history of economic thought, and economics education for labour and community groups.