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Oireachtas

# **Joint Committee of Inquiry into the Banking Crisis**

## **Witness Statement of**

**Maria Woods**

**Strictly Private & Confidential**

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- “(a) with the prior consent in writing of the committee,
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Serious sanctions apply for breach of this section. In particular, your attention is drawn to section 41(4) of the Act, which makes breach of section 37(1) a criminal offence.

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<sup>1</sup> See s.37 of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013

# **Joint Committee of Inquiry into the Banking Crisis**

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**Strictly Private and Confidential-For purposes  
of the Oireachtas Banking Inquiry only**

**Oir Ref: MWO01 [MWO-i-03b]**

## **Introduction**

I set out below my written statement in compliance with the direction under section 67(1) of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013 (“the Act”) of 16 July 2015. I have regard to core documents provided to me by the Joint Committee in preparing this written statement.

## **Career and Background**

I begin with some background on my career within the Central Bank of Ireland (Central Bank) during the time period covered by the Joint Committee’s Inquiry since this informs the nature and extent of my replies to the various questions put to me in “Document 1” as part of the direction issued under the Act. I believe that quite a number of questions are outside my professional knowledge and scope. In that regard, I thank the Joint Committee for the removal of questions under the following themes and lines of inquiry:

- R1a;
- some questions in relation to R1b;
- R2c; and
- R3b.

I joined the Central Bank in October 2004 as a Research Assistant in the Monetary Policy and Financial Stability Department. This role involved providing research assistance to economists within the department, maintaining databases of national and international financial stability indicators and contributing to financial stability analyses and briefing, as required. From November 2005 to July 2011, I worked as a Financial Stability Economist. My primary role during this period was to produce analysis on various topics within my area of responsibility. These could be produced as sections of Financial Stability Reports (FSRs), analytical signed articles, internal papers, briefing notes for senior management, or presentations on my area of expertise. Depending on my area of responsibility or grade, I also represented my division or the Central Bank at meetings, either internally with other divisions or with external stakeholders, or at European working groups. From August 2011 to date, I have worked as a Senior Economist.

From November 2005 through 2008, I focused on the analysis of residential and commercial property issues. Between 2009 and 2013, I focused on the financial stability assessment of the domestic banking sector and in particular, funding issues. Since September 2013, I have worked on macro-prudential policy issues.

Between the time that I joined the Central Bank in 2004 and 2011, I held relatively junior positions within the Central Bank. Even as a Senior Economist, I am not and never have been a member of either its local or senior management structure.

In terms of the Central Bank's internal structure, Economists generally report to Senior Economists (or if the team is relatively small, directly to local management). The role of Senior Economist can cover two grades (i.e., Bank Professional 2 and higher again, Bank Professional 1). I am currently Bank Professional 2. The Senior Economists in turn, report to local management (i.e., Deputy and Head of Division or Department) who in turn, report to senior management. In the Economics Directorate, at present the Chief Economist is at Director level, just below the Deputy Governor of the Central Bank, who just below the Governor. Although the internal structure of the Central Bank has changed over the time period covered by the terms of reference of the Committee (i.e., 1992 to 2013), a hierarchical structure similar to the above has been a feature of my entire time with the organisation. Therefore, the direction of my work agenda, the content of analytical pieces and any briefings all need to be signed-off by more senior members of staff. Generally, until you are a Senior Economist, you do not contribute to strategic discussions. Since I did not attain the position of Senior Economist until August 2011, I was not involved in strategic discussions up to that point.

At no stage in my career did I work as a Micro-prudential Regulator or in a Division with responsibility for micro-prudential issues. Apart from a brief period between March 2009 and July 2009 where I worked in the Financial Markets Division on funding issues, my entire career in the Central Bank has focused on financial stability issues within the Economics Directorate.

As noted in the Central Banks' various Annual Reports, financial stability is concerned with ensuring that the various components of a financial system (i.e. financial, payment and settlement systems and financial intermediation) can perform their core function and are resilient to shocks. In addition, since the recent global financial crisis, greater emphasis has been placed on the analysis of macro-financial linkages (i.e., links between the macro-economic environment and the financial system). Systemic stress occurs when a shock disrupts the smooth functioning of the financial system which in turn, can lead to a financial crisis with negative consequences for economic activity. Macro-prudential policy aims to mitigate the risk of such systemic stress. Macro-prudential or financial stability risk assessments aim to inform such policy discussions. By contrast, micro-prudential regulation focuses on the financial soundness and solvency of individual financial firms such as banks and other regulated financial institutions or funds.

Between 2003 and 2010, the Central Bank existed as the Central Bank & Financial Services Authority of Ireland ("the CBFSAI"). It had a statutory mandate to contribute to overall financial stability. The



Financial Stability area<sup>1</sup>, in which I worked, sat within the central banking arm of the CBFSAI. The Irish Financial Services Regulatory Authority (“the Financial Regulator”) existed within the CBFSAI as an independent entity and had a mandate for the micro-prudential supervision of individual financial institutions. To the best of my knowledge, there was co-operation on financial stability matters between the Financial Regulator and the Central Banking arm of the CBFSAI through various committees and high-level groups such as the Financial Stability Committee (FSC) and CBFSAI joint Board meetings. I was not a member of any of these committees and my attendance at such meetings up to 2010 was limited to discrete presentations on my analytical papers prior to their publication in the Financial Stability Report, the provision of data updates and ad hoc notes on financial stability issues.

With the coming into force of the Central Bank Reform Act 2010 (“the 2010 Act”), the Central Bank became a unitary organisation, responsible for both central banking and financial regulation. The 2010 Act introduced a new model of financial regulation and an enhanced assessment of financial stability. This change resulted in increased co-operation between micro-prudential and macro-prudential/financial stability areas of the Central Bank. Such interaction helped to implement required crisis management actions and to deepen the risk assessment of the domestic banking sector. With the Act of 2010, the role of the FSC was strengthened and the Central Bank Commission was formed (see Central Bank of Ireland 2010 Annual Report). I am not a member of either of these bodies but would as required, present policy and analytical notes/papers on financial stability issues relevant to my area of responsibility.

#### **Questions arising from the Direction issued pursuant to the Act**

***Question 2. One of the statutory objectives of the CB was ‘the promotion of the financial services industry in Ireland’. In your view was there a conflict between this objective and the Financial Regulator’s responsibility for prudential supervision?***

I understand that this question focuses specifically on the role of the Financial Regulator and the potential conflict with the statutory mandate of the CBFSAI to promote the financial services industry in Ireland.

Between 2003 and 2010, the Central Bank existed as the Central Bank & Financial Services Authority of Ireland. The Financial Regulator existed within the CBFSAI as an independent entity and had a mandate for the micro-prudential supervision of individual financial institutions. During the existence of the Financial Regulator, I worked within the central banking side of the CBFSAI. At no stage did I

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<sup>1</sup> The department was called Monetary Policy & Financial Stability in 2004. From 2008 the department was the Financial Stability and Payment Systems Oversight Department and from 2010, the Financial Stability Division.

work as a micro-prudential regulator within the Financial Regulator. Therefore, how the statutory mandate derived from the Central Bank and Financial Services Authority of Ireland Act 2003 (“the Act of 2003”) concerning the promotion of the financial services industry and how this might have impacted on the day-to-day regulatory tasks of the Financial Regulator are outside my direct professional knowledge and scope. This lack of professional insight also applies to discussions at a senior level on the strategic implementation of this mandate for the Financial Regulator and any associated impact on financial stability matters given my grade at that time. On this basis, I cannot offer a professional assessment on whether there was a conflict between the Central Bank’s promotion of the financial services industry in Ireland and the Financial Regulator’s responsibility for prudential supervision.

***Question 4. In your opinion, did the Financial Regulator, as suggested by Patrick Neary at his Hearing, have the power to stop banks to pay out dividends? If so, would it have been appropriate for the FR to use those powers in view of the potential market impact? And why?***

I understand that this question focuses on comments made by Patrick Neary at his Hearing in front of the Joint Committee on 28 May 2015 which related to supervisory powers held by the Financial Regulator to direct banks not to pay dividends in 2008.

As previously stated, during the existence of the Financial Regulator, I worked within the central banking arm of the CBFSAI. At no stage did any of my roles within the Central Bank cover the area of micro-prudential regulation or legal issues. I understand that the first part of the question asks whether, in my opinion, the Financial Regulator had the power to stop the banks paying a dividend. I do not have a legal background and cannot offer an informed or professional opinion on whether the Financial Regulator had this power or not under the CBFSAI Act of 2003 or any other relevant pieces of legislation.

In terms of the second part of the question, to give a full assessment of the appropriateness of such a measure in 2008, a number of factors need to be considered.

Firstly, one would need to know if such a measure was legally feasible and/or enforceable. Secondly, one would need to ascertain whether or not there were any conditions that should be taken into account for operationalizing this action. Both of those aspects are outside of my professional knowledge.

Thirdly assuming that the Financial Regulator had the power and that there were no conditions inhibiting the exercise of that power, in order to assess if such a measure were warranted one would need to have a comprehensive knowledge about the financial soundness of the individual banks concerned, at the time in the context of the prevailing macro-financial environment. Lastly, one would



need to fully understand the potential for any spill-overs effects to other banks and to the real economy from the announcement of such a measure in order to express an informed opinion on whether it would have been appropriate for the Financial Regulator to use those powers.

Since I did not work in a regulatory area or on the financial stability risk assessment of the domestic banking sector until later, I am not in a position to assess the financial position of individual banks at that time, especially in the context of information that may have been available in 2008. Therefore, I cannot offer an informed opinion on whether it was appropriate for the Financial Regulator to use such powers, if they existed in the context of the potential market impact in 2008.

***Question 5. Apart from the publication of Financial Stability Reports, how did the Central Bank ensure that the Government was at all times well informed about the current macro-economic situation and trends?***

I understand that this question focuses on the provision of advice on macro-economic issues by the Central Bank to the Government.

I believe there were interactions between the Central Bank and the Department of Finance on macro-economic issues, particularly at a senior level. It is my understanding that a pre-budget letter has been submitted annually to the Minister for Finance from the Governor expressing the views of the Central Bank/CBFSAI Board as well as highlighting relevant macro-economic and financial issues that are considered relevant in any budgetary discussions. In light of my role and grade, I am not personally familiar with the internal process underpinning such pre-budget letters.

I have worked mainly on financial stability issues during my time in the Central Bank. I have never worked in the department within the Economic Directorate which focuses on domestic macro-economic issues and which coordinates the completion of the Central Bank's Quarterly Bulletin; the Central Bank's regular publication on macro-economic issues. Therefore, there may have been other interactions in relation to purely macro-economic issues, at different levels between the two organisations during the time period under review that are outside my knowledge or remit.

With regard to macro-financial/financial stability issues I understand that there were a number of interactions between the Central Bank and the Department of Finance. It is also my understanding that the scale of this interaction increased during the domestic crisis. As already noted, the findings of the Financial Stability Report were presented to the CBFSAI Joint Board prior to its publication and for discussion in the case of the interim Financial Stability Reports: the Secretary General from the Department of Finance had a seat on this Board. Since 2012, the Central Bank has published semi-annual Macro-Financial Reviews ("MFRs"). As part of the pre-publication process, the MFRs are



presented to the Central Bank Commission for information and I believe the MFRs are also sent to the Department of Finance.

In 2006, I understand that a Domestic Standing Group (“the DSG”) was established to ensure co-operation on financial stability issues among national authorities. These included, the Department of Finance, the Financial Regulator and the Central Bank. I was not a member of this group but I understand that they discussed crisis management issues as well as prevailing market conditions. According to the Honohan Report 2010<sup>2</sup>, the National Treasury Asset Management Agency (“the NTMA”) participated in the DSG during the crisis. It is my understanding that the DSG is no longer in operation. I understand that there is currently a “Principal’s Group” in place, where senior officials from the Department of Finance, the Central Bank and the NTMA meet. Cooperation between the Central Bank and Department of Finance on issues related to the financial system is outlined in the 2011 Memorandum of Understanding between the two organisations.

Outside of meetings such as those outlined above, I am aware that the Governor and other members of senior management wrote to the Minister for Finance presenting views on various financial stability-related matters during the crisis. Also during the crisis I am aware of interaction between national authorities on funding matters from 2010.

***Question 6. In your recollection what were the reasons for the CBFSAI Board/Department of Finance in favouring a soft landing scenario for the property market over a hard landing? Were these reasons ever discussed in detail? Honohan points out that the FSR cites no quantitative analytical evidence for this conclusion.***

My understanding is that question relates to the central expectation of the Central Bank’s 2007 Financial Stability Report with regard to the likely future path of Irish house prices and in particular, senior management discussions within the Central Bank on this issue.

I am of course familiar with the rationale as presented in the 2007 Financial Stability Report for the assessment of a “soft landing”. However, the simple answer to the question 6 is that I do not have direct insight into senior management/CBFSAI Board discussions on this topic, based on role and grade at that time.

As noted in my opening commentary on my career and background, I held a relatively junior position within the Monetary Policy & Financial Stability Department, during the production and publication of the 2007 Financial Stability Report. My role was to prepare the initial commentary for the private-sector credit and property price section of the main body of the Financial Stability Report. This involved updating and reviewing the relevant financial stability indicators, drawing on international

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<sup>2</sup> See page 115, in Honohan (2010), “The Irish Banking Crisis. Regulatory and Financial Stability Policy 2003-2008” for more detail.

experience/other research/current events to expand the analysis, as required, and drafting an initial risk assessment for these sections. I was not part of the editorial team for this particular Financial Stability Report and did not draft the executive summary.

My understanding is that key findings of such Central Bank Reports need to be agreed and approved by senior management prior to publication. Based on the 2007 schedule, earlier drafts of the Financial Stability Report were initially discussed at the FSC meeting of 12 June 2007 and at the joint CBFSAI Board meeting of 21 June 2007. I did not attend either of these meetings therefore I cannot give any insight into the discussions that took place.

Following these meetings, revisions to drafts of the Financial Stability Report were taken on board. Over the summer, signed articles were completed and the main revised text of the Financial Stability Report was updated with any new data. For example, I updated the data and related text within the sections on private-sector credit and property prices.

The pre-publication Financial Stability Report and signed articles were then discussed at a Board meeting of 27 September 2007. I attended this Board meeting for the sole and discrete purpose of presenting and collecting comments in respect of my signed article "*A Financial Stability Assessment of the Irish Commercial Property Market*" (This article was published in the 2007 FSR and I believe the complete 2007 FSR would have been provided to the Joint Committee from the Central Bank). At the time, my main focus was on presenting my own paper and as such I do not recall specific discussions that took place in relation to future house price developments or the main findings of the Financial Stability Report. I understand that the minutes of this meeting have been furnished to the Joint Committee. As mentioned previously, I was not a senior member of staff nor was I in an editorial position at this time therefore I have no direct or specific knowledge of any additional discussions that may have taken place with senior member of staff on the key findings of the 2007 Financial Stability Report prior to publication.

***Question 7. Could you describe the nature and extent of the co-operation and exchange of information between economists in the Department of Finance with colleagues in the Central Bank, ESRI and other external economic forecasters during your tenure at the Central Bank/Department of Finance?***

As I understand it, this question relates to cooperation between economists in the Department of Finance with economists in other organisations. I focus my answer on cooperation with the Central Bank given my background.

Most of my professional interaction with economists in the Department of Finance during the period under review centred on meetings or information requests on crisis-related financial stability issues



and papers. This interaction mainly occurred after 2009, when I started work on the financial stability assessment of the domestic banking sector. Such interaction, therefore, was mainly with officials in the Department of Finance working on domestic banking sector issues. Such meetings would be on funding issues or as part of the national engagement with the International Monetary Fund, ECB, EU Commission with regard to Ireland's Programme for External Assistance. In line with my grade, my role was to merely intervene as necessary based on my professional knowledge and to report the findings to the appropriate senior member of staff, either at local or senior management level when I returned from the meetings. As noted in question 5, I understand there has been increased cooperation between the Department of Finance and the Central Bank since the domestic crisis on financial stability matters. Given my role at the time, I am also aware of interaction between national authorities on funding issues from 2010. In terms of those meetings that I attended, I generally found the level of cooperation to be good with each representative bringing useful insights from their respective organisations.

***Question 10. After 2004 the IMF, OECD and ECOFIN all clearly recommended a tighter fiscal stance and the building up of a 'cushion' for the time when income from property related transactions would fall. Can you discuss why in your view the Central Bank's recommendation to the Minister did not more forcefully alert to this issue?***

It is my understanding that this question focuses on the nature and tone of policy recommendations on fiscal matters by the Central Bank to the Minister for Finance in the pre-crisis period. I am aware of the content of the Financial Stability Reports from 2005 which highlighted the potential vulnerabilities associated with the unbalanced nature of the growth in the domestic economy and over-reliance on the construction sector in the pre-crisis period<sup>3</sup> and analyses since the crisis<sup>4</sup> which discussed the highly cyclical nature of government revenue in the pre-crisis period. However, to date, I have not been involved in structuring policy recommendations on fiscal matters.

As noted in my reply to question 5, it is my understanding that a pre-budget letter was submitted to the Minister for Finance from the Governor expressing the views of the Central Bank/CBFSAI Board and highlighting relevant macro-economic and financial issues that were considered relevant in any budgetary discussions. I am not personally familiar with the internal process underpinning such pre-budget letters, nor was I involved in drafting such letters. Furthermore, I never worked in the department within the Economic Directorate which focuses on domestic macro-economic issues and coordinates the completion of the Central Bank's Quarterly Bulletin. Between 2004 and 2011, I held relatively junior positions within the Central Bank. Even now as a Senior Economist, I am currently

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<sup>3</sup> See CBFSAI Financial Stability Reports (2005 through 2007) and McGuire and Smyth (2005), "The Implications of a Construction Sector 'Correction'" in *Financial Stability Report* 2007, CBFSAI.

<sup>4</sup> Honohan (2010), "The Irish Banking Crisis. Regulatory and Financial Stability Policy: 2003-2008", A Report to the Minister for Finance by the Governor of the Central Bank. May.



not a member of either its local or senior management structure. Therefore, matters such as determining the nature and tone of communication between the Central Bank and the Department of Finance, especially during the pre-crisis period and on macro-economic/fiscal matters are outside my professional scope and expertise

***11. Morgan Kelly published an article on a potential house price bubble in the Irish Times end of 2006 and later published a report on the same theme as part of the ESRI bulletin in Summer 2007. Can you recall if any discussions were held at senior management level in the Central Bank afterwards? Were Morgan Kelly's concerns given serious consideration?***

I understand that this questions focuses on the response of senior management within the Central Bank to certain publications by Morgan Kelly at end-2006 and in Summer 2007 on Irish house prices. Similar to my reply for question 6 above, the simple answer to this question is that I do not have direct insight into senior management discussions on this topic based on role and grade at that time.

The Financial Stability Report, 2007 had a section (known as a “box”)<sup>5</sup> discussing the methodology found in the 2007 ESRI paper and other similar international studies on house prices. This box was then referenced in the assessment section of the main body of the text. The box presented certain methodological qualifications that need to be considered when reviewing this strand of the house price literature. Although I initially drafted the property section in the main body of the Financial Stability Report, I did not write the box reviewing this literature in 2007. That said, I was aware of the contents of the ESRI paper and general discussions on this area and note that the 2007 article by Morgan Kelly was part of the general economic debate on Irish house prices at the time.

In terms of specific senior management discussions on this paper I do not have any direct insight into or recall such discussion given my role and grade at the time. In 2007, an overview of the forthcoming Financial Stability Report along with possible boxes was tabled at the FSC meeting of 12 June 2007 and again at the Joint CBFSAI Board meeting on 21 June 2007. I understand that the box on international house price literature was proposed at this meeting. I did not attend either of these meetings, and therefore, I have no insight into the nature of any discussions that took place.

Prior to publication in November 2007, the main findings of the draft Financial Stability Report, including boxes and articles, were presented at the FSC and the CBFSAI joint Board meetings in September. My attendance at the FSC meeting and joint CBFSAI board meeting, held in September 2007 in which the pre-publication draft of the Financial Stability Report was tabled, was for the sole purpose of presenting the findings of my signed article “*A Financial Stability Assessment of Irish Commercial Property Prices*”, which was subsequently published in the 2007 Financial Stability Report. I do not recall the specific discussions on the Morgan Kelly paper at these meetings outside of

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<sup>5</sup> Box C entitled “The Economic Literature on International House-Price Cycles”.

what is recorded in the minutes of the meeting. I understand that the minutes of the meeting have been furnished to the Joint Committee by the Central Bank.

*12. Do you judge the IMF country reports and OECD reports as an important information instrument to aid banking regulation, banking supervision and financial stability issues? If yes, why, if not, why not?*

I will focus my answer on the financial stability perspective based on my professional knowledge within the Central Bank as previously outlined. I believe that reports by international organisations such as the IMF and the OECD on financial stability issues at national level are useful. During my time as a Financial Stability Economist, I have found such reports helpful in preparing my own analysis of domestic issues, both in terms of gaining a different perspective on the risk assessment and as a cross-check that I was not missing any potential risks. My engagement with the process of the preparation of such country reports has been the review of pre-publication drafts for any factual inaccuracies at the request of a country coordinator or from a more senior member of staff, within the Central Bank. Comments are coordinated and then sent to the IMF or the OECD for consideration.

I have also attended some meetings with the IMF with other staff members from the Central Bank which covered topics within my area of responsibility. In such meetings, the Central Bank Economists and the IMF representatives would exchange views on the conjunctural outlook. Numerous meetings take place between the Central Bank and the IMF on a range of topics both with staff from the various departments dealing with the respective topic and separately with senior members of staff. I understand that the IMF also meet with a number of other external authorities when preparing their analysis.

Since the crisis, methods for financial stability assessments have been, and continue to be enhanced both by the Central Bank of Ireland and by the wider international financial stability community to reflect insights gained during this episode.

### Conclusion

I have outlined above that my position within the Central Bank was of a relatively junior nature, especially up to 2011. Also I worked predominately on financial stability issues. Therefore, I have provided answers to the specific questions to the best of my ability, knowledge and involvement for the relevant period.

I hope this is of assistance to the Inquiry.

Signed: Maria Woods (30/7/2015)

Maria Woods