Irish government organises massive support package for banks

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The Irish government announced on September 30 a plan to guarantee all deposits in the country's six major domestic financial institutions, a move whose cost could approach the sum the US will make available to bail out Wall Street.

The potential total cost of the proposal will amount to €420 billion, around five times Ireland's GDP, and the taxpayer will have to foot the bill.

The announcement came on the back of a number of banks collapsing across Europe--Bradford and Bingley in Britain, Hypo Real Estate in Germany and Fortis in Belgium, to mention only the most prominent. The impact of the turmoil in Europe had been felt particularly on the Irish stock market, with shares plummeting on September 29. Anglo Irish Bank, one of the largest financial institutions, was down 46 percent, while Bank of Ireland and the Allied Irish bank also suffered double digit decreases.

The threat of an Irish bank being the next to go under had the government taken no action was very real. Announcing the decision to guarantee all deposits, the government stated that it "has decided to put in place with immediate effect a guarantee arrangement to safeguard all deposits (retail, commercial, institutional and interbank,) covered bonds, senior debt and dated subordinated debt (lower tier II,) with the following banks: Allied Irish Bank, Bank of Ireland, Anglo Irish Bank, Irish Life and Permanent, Irish Nationwide Building Society and the Educational Building Society ... It has done so following advice from the Governor of the Central Bank and the Financial Regulator about the impact of the recent international market turmoil on the Irish Banking system."

The proposal passed both houses of Ireland's parliament, the Dáil and Seanad in the early hours of October 2. Despite some criticisms from the opposition parties and a number of amendments tabled, there was virtual unanimity on the fact that the banks had to be helped for the good of Ireland's economy.

The proposal is crafted for the wealthiest sections of Irish society. A government scheme adopted last month guarantees €100,000 of individual savings and protects 97 percent of all savings. The €400 billion package now adopted is aimed at those three percent who have investments exceeding this level.

Justifying the need for the government to step in, Finance Minister Brian Lenihan attempted to shift the blame for the current crisis onto ordinary people. He commented, "You know, we've got to be honest about this as a people. We decided, as a people collectively, to have this housing boom. We decided not to have property taxes, to demand reductions in stamp duties, to demand interest for those who bought to-let properties, and there was no questioning in any part of the political system about that."

In fact this says more about the established political parties and the interests they serve than it does about ordinary working people who have no influence over the speculative activities of the banks.

During the course of the Dáil debate, it became apparent that the initial figure of €420 billion may be increased. Lenihan pointed out that the government had received applications from banks operating in Ireland who are controlled by institutions based in other countries. Originally excluded from the legislation, he left open the possibility that such banks could be included if the government gave its consent. In a further insult to those struggling to get by in the current climate, an amendment to the bill proposing that the funds to be made available should be conditional based on a limitation of executive and CEO pay was defeated.

The decision to open the proposal to other banks received the enthusiastic support of the opposition Fine Gael. Finance spokesman Richard Bruton commented, "This move will hopefully help to deal with the equity, fairness and competition issues raised by Fine Gael relating to this matter. It is also hoped that this move will help remove one of the potential barriers to the operation of the scheme as outlined."

The reality is that it will only worsen the plight of ordinary working people as they struggle to cope with the economy in full recession. In stark contrast to the process by which the government is to make hundreds of billions available to the banks, it has been over the course of the past few months attempting to prepare public opinion for comprehensive spending cuts in the forthcoming budget.

In a special cabinet meeting on September 28, proposals for slashing funds for all government departments in the budget to be unveiled on October 14 were discussed. With the government continuing to see an on-going reduction in tax returns, Lenihan is reportedly seeking to make cuts in spending of over €3 billion. A report in the *Irish Times* revealed that the exchequer shortfall, following the latest figures, was €9.4 billion. It added that cuts of around 7 percent would be made in some areas. Many major capital spending projects, including the metro system in Dublin, appear certain to be scrapped.

Further proposals being considered include scaling back child benefits and ending universal health care for those reaching 70. While determined to avoid increasing income tax rates to raise funds, Lenihan is quite prepared to dip into public funds to continue certain investment projects considered vital. As the *Sunday Business Post* noted last week, "Serious examination is being given to using money from the National Pension Reserve Fund to pay for some key investments, notably the electricity interconnector with Britain."

The pension fund has already suffered substantial losses over the past year as a result of the credit crisis.

Even if it manages to make the cutbacks demanded by the ruling establishment, the government will still have to increase its borrowing which is expected to exceed 5 percent of GDP. This could prompt action from the European Union, which stipulates that member states' borrowing should not exceed 3 percent. But the government has little option. As Pat Leahy commented in the *Sunday Business Post*, "the government's financial position is deteriorating every week. It's getting worse because revenues from taxation are slowing all the time, and the government is constantly having to revise its forecasts for how much money it will have to spend this year and next."

These circumstances have led some commentators to denounce the recklessness of the guarantee of bank assets, given the economic problems Ireland is facing and the instability of the banks.

Morgan Kelly in the *Irish Times* noted, "The reason that foreign banks started to shun Irish banks is that international investors have gradually become aware of the scale and recklessness of Irish bank lending to builders and property speculators. Irish banks are currently owed €110 billion by builders and developers. Of every €100 that Irish residents have deposited in banks, €60 has been lent for property speculation."

He continued, "As the property bubble has burst, it is looking increasingly unlikely that banks will get back more than a fraction of this. In particular, very little of the €25 billion lent to builders to construct the ghost estates and vacant apartment blocks that now blight the landscape will ever be seen again... Irish banks were facing potential losses on their property lending of the order of €10 billion to €20 billion. Thanks to Brian Lenihan's master stroke it looks as if it will be you, rather than bank shareholders, who will be taking the loss."

In spite of this precarious situation, the government has rushed through a guarantee to the banks of all their assets without a second thought. There could not be a more graphic illustration of whose interests are considered important.

While Ireland's banks are to be handed a blank cheque guaranteeing their vast assets, earlier in September the government took part in negotiations between employers' organisations and trade unions which imposed a pay pause in the public sector for 11 months and pay freezes and cuts across the private sector. These pay pauses were initiated by the government in July and before a final agreement was reached Taoiseach (prime minister) Brian Cohen urged negotiators to remain "realistic" with their pay claims given the economic conditions.

The deal also exposed the important role played by the trade unions in ensuring that workers will be forced to deal with wage freezes at a time when prices for everyday goods continue to rise. Labour Party spokesman Willie Penrose maintained that workers could not expect better: "The proposals on wage increases are probably the best that the trade union movement could have secured in the current climate, but clearly for many workers it will mean that they will only stand still and will experience no real improvement in their living standards, particularly if the government fails to bring inflation under control."

In reality, many will see their living standards eroded as inflation worsens. Added to this, the government's spending cuts across the board will hit already meagre social services.

The fact that the original proposal only included Irish owned banks created a backlash among foreign-owned institutions with a substantial presence in the Irish market. Ulster Bank, owned by RBS (Royal Bank of Scotland) and the National Irish Bank (owned by Dansk Bank), were just two of the banks excluded from the scheme. It was pointed out that the legislation would leave one in five Irish customers outside the guarantee scheme. These institutions pressured the government into stating it would be willing to expand the package on a "case by case" basis.

Foreign governments have also criticised the legislation for hampering competition. In particular, the British government has been heavily critical on the basis that many of the Irish banks who will enjoy support from the guarantee have operations on the UK high street. In the days following the guarantee many British depositors have begun moving their money into Irish banks. British Chancellor Alistair Darling reportedly made it clear to Lenihan that he saw the guarantee as a serious problem for Britain. The British Bankers' Association wrote to the Brown government expressing its concern about the distortion in competition which the Irish move will cause. Some are even using the situation to urge Britain to adopt similar measures and guarantee the assets of all UK-based banks, in a move which would cost the taxpayer trillions.

Criticism has also come from other European states, in particular France, which on Wednesday had floated the idea of united action by the EU to tackle the on-going crisis. As the *Financial Times* noted in a comment on the Irish government's guarantee, "The move is causing ructions in Brussels, where there is concern the Irish move shatters any hope of pan-European regulatory response to the turmoil."

The Irish government has hit back at such criticism, claiming it is the duty of each "sovereign state" to look after their own banks. Speaking hours after the legislation passed on Thursday, Cohen attempted to reassure that the banks would have to pay a "high price" for the state guarantee and that banks seeking to profit unfairly from the scheme would not be tolerated. Lenihan reportedly was in contact with the financial regulators after it emerged that an email had been sent from Irish Nationwide to its employees urging them to seek new deposits. Basing itself on the state guarantee for the institution's funds, the email stated that Irish banks were "the safest place to deposit money in Europe."