Restoring Confidence in National Treasuries: Ireland

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Introduction

- The Lessons from the Past
  - Multiple failures
  - Role of the Department of Finance
- Consequences
  - Real economy
  - Public Finances
  - Banking crisis
- Exit from crisis
- Reforms - Prevention

Lessons from the Past - 1

- Seeing it coming?
  - Housing bubble well signalled
  - Inappropriate fiscal policy signalled but no action
  - Financial exposure – communal blindness
- Response of Banks
  - Boards asleep or negligent or both
- Financial Regulation
  - Awful negligence: did not understand risks
- Other players – auditors etc.

Lessons from the Past - 2

- Department of Finance
  - Were dangers in housing market & fiscal policy seen?
    - External report on performance
    - Say they did but….
    - Did not record their concerns
    - Freedom of information V transparency
    - Freedom of Information can give a voice
  - Banking – relied on the regulator
    - Should have seen the risks by end 2007
    - Should have been ready in September 2007

Lessons from the Past - 3

- Department of Finance
  - Tradition of “generalists”
    - Few economists – poor links to outside debate
    - Open thinking frowned upon?
  - End of evaluation culture with end of EU funding
    - Move away from evidence based policy making
    - Hubris?
  - Investment Plans and Budgets
    - Inappropriate from at least 2003.
  - Tax forecasting – exposure to building ignored
  - Same government 1997-2011
    - Ministerial fiscal policy: “If I have it I spend it”

Consequences

- Housing Bust
  - Housing accounted for 14% of GDP
  - Building squeezed out tradable sector
  - Banks funded the boom by foreign borrowing
  - Banks massively over exposed.
- GDP per head falls 11% peak to trough
- Huge effect on budget
- Banks losses
  - No plan for the melt-down
  - Some banks insolvent
  - Loss of confidence and funding for banks
  - Rest Illiquid even if not insolvent

Exiting the Crisis

1. Sort out the banks
2. World demand and competitiveness
   - Export growth - Balance of Payments surplus
   - Not very job intensive
3. BOP surplus and exports
   - Platform for future growth in domestic demand
4. Domestic Demand growth – when?
   - Sort the deficit and the banks
   - Consumer confidence: lower savings rate
   - Return to some building & construction
   - Domestic demand creates jobs
   - Therefore, lagged response of unemployment

Reforms - 1

- Regulation – Central bank
  - One authority, not two
  - New management
- Fiscal Policy
  - Counter-cyclical policy
  - Use fiscal policy to manage property market
    - Tax mortgage interest payments
  - Should run increasing surpluses if overheating
- Institutional Change
  - Fiscal Council
  - Management of banks
  - Improving information flow
  - Reform of Department of Finance

Reforms - 2

- Restructuring Department of Finance
  - Enhancing the skills available to it
    - More economists (also lawyers and accountants)
  - Not just more economists: also how they are used
    - Look at Netherlands, Sweden & Northern Ireland
  - Need to be part of the economic debate
    - Open to new ideas – and able to find them
  - Economics is not just fiscal policy
    - Assessing all other policies: health, infrastructure etc.

Reforms - 3

- Restructuring Department of Finance
  - Two Departments
    - New Department for Public Service Reform & BUDGET
    - Logic?
    - Problems?
  - Respect for Independent Fiscal Council
  - Importance of Public Debate
    - Keeps Department open to outside ideas