Ireland’s Debt Crisis: Roots and Reactions

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Introduction: a pattern of dependency

The collapse of the Irish economy has come as a particular shock to many people, at home and abroad, because of its seemingly remarkable success in the preceding years, the period of very rapid economic growth that saw the country, from the early 1990s onwards, described as the ‘Celtic Tiger’. However, that era in fact consisted of two distinct phases. In the first phase, before 2001, growth was largely based on the attraction of (mainly US) multinationals taking advantage of Ireland’s low corporate profits tax rate (12.5%) and using the country as a base from which to export to the EU and/or artificially inflate their profit levels in Ireland through ‘transfer pricing’ mechanisms. Ireland, accounting for a mere 1% of Europe’s population, managed to attract 25% of all US greenfield investment into the EU in the early 1990s. US investment in Ireland, at $165 billion, is greater than US investment in Brazil, Russia, India and China combined. Multinationals, the majority of them from the US, account for 70% of Irish exports. The continuing importance of (or subservience to) the multinational sector, and this includes a lot of lightly regulated financial services companies, helps explain why Irish governments are committed to maintaining the low corporate tax environment, despite the current budgetary crisis.

Property prices and debt

After 2001, economic growth was based largely on a property price bubble. Investment in buildings accounted for 5% of output in 1995 but for over 14% in 2008. By 2006/07, the construction industry was contributing 24% to Irish income (compared to the Western European average of 12%), accounting (directly and indirectly) for 19% of employment (including high levels of migrant labour) and for 18% of tax revenues (property transaction taxes have now collapsed as construction activity has nosedived). House prices, which quadrupled between 1996 and 2007, are now down 43% from their peak levels and may well have further to fall; vast numbers of houses lie empty.

What was fuelling the property price bubble was a massive rise in household debt, which shot upwards from €57 billion in 2003 to €157 billion in 2008 and which now stands at 180% of household disposable income (compared to 40% in 1993). (It is this trend that caused the last Irish Minister for Finance to claim that “we all partied” – while it is certainly true that many people did borrow increasingly heavily during the boom, the actual benefit, if any, they accrued from this is far from clear). Lending for mortgages rocketed from €44 billion in 2003 to €128 billion in 2008. And the Irish banks were themselves borrowing in order to lend on to their customers: the 6 main Irish banks borrowed €15 billion from abroad in 2003 but this figure had risen to €100 billion by 2007.

The European dimension

This reckless splurge was facilitated by liberalised lending practices across the EU and by lax cross-border regulation of the financial sector. The low interest rate policy of the European Central Bank (ECB) fanned the flames: the ECB variable rate was cut from 4.25% in August 2001 to 2% in June 2003. The argument can also be made that the very design of Economic and Monetary Union (EMU) helped cause the crisis by establishing exchange rates that left peripheral EU countries uncompetitive relative to Germany and encouraged the peripherals to rely on the accumulation of debt to 'compensate' for this. The Irish authorities also contributed to the property bubble with a range of tax incentives to property development.

Bailing out the banks

When the global financial crisis hit, access to credit declined drastically worldwide and asset values tumbled, leaving banks (including the Irish ones) in a parlous position. The Irish government chose to respond to the plight of the banks in an extraordinary manner: on 30th September 2008 all depositers and senior bondholders (creditors to the Irish banks) were guaranteed by the state. As writer Conor McCabe put it, "the Irish people woke up to find that the… government had put up the entire Irish State as collateral for the crushing liabilities of six private banks". The total cost of bailing out the banks is so far estimated to be €70 billion, and this may be an optimistically low figure as various other bills, so-called 'contingent liabilities', are yet to be presented for payment.

An example of a contingent liability arises from the Irish state creating a National Assets Management Agency (NAMA) to buy up some of the worst property loans in the hope of selling them on later – the full cost of this is as yet unclear, though it seems clear that taxpayers will end up subsidising property developers to some extent at least. Another example is short-term liquidity support from the Central Bank of Ireland to the Irish banks (partly to compensate for a flight of deposits), which the state has guaranteed, and which seems to be based on shaky collateral, including prior government promises to the banks of phased recapitalisation payments. A recent audit of the Irish debt notes that "This is a circular arrangement whereby notes given by the state to the bank are then used by the bank to borrow more from the state. The result is that Irish people are guaranteeing loans made to illiquid and possibly insolvent banks on the basis of previous promissory notes issued by the Irish government to the same banks". The potential for this house of cards to collapse is obvious.

Austerity for ordinary people

This money is coming (or will come) from ordinary citizens: we have already witnessed more than €20 billion in 'fiscal adjustment' (spending cuts and tax increases), what economist Karl Whelan describes as "the equivalent of…€4,600 per person… the largest budgetary adjustments seen anywhere in the advanced economic world in modern times". 2011 will see a further €6 billion of cuts and tax hikes; that figure is to be €3.6 billion for 2012 and, on average, €3 billion for each of 2013 and 2014. A loan of €58 billion from the IMF and EU was contracted in December 2010 – at an interest rate of 5.8% (since reduced as part of a deal to lower Greece's debt burden) – as Ireland could no longer borrow at affordable rates from private financial markets. Crucially, this is not a 'bail out' of Ireland. The EU and IMF intervened to ensure that Ireland would continue to pay back the money Irish banks owe to foreign financial institutions with the bulk of the 'bail out' money merely routed through Ireland for that purpose. The conditions attached to this loan stipulate that austerity measures must be continued.

The social price being paid is catastrophic, not least because the austerity policies are sending the economy into a tailspin: national income is already down over 15% from its peak level. Unemployment stands at almost 15%, close to half a million people. The only sector showing some dynamism is the multinational 'export platform' (especially pharmaceuticals and computer services), but the employment pay-off from this is limited. Emigration is estimated to be running at 40,000 per annum. The economy is mired in recession, with investment down from over €48 billion in each of 2006 and 2007 to a little over €18 billion in 2010 – capital, as sociologist Kieran Allen puts it, has gone on strike. Bank loan approval rates fell from 95% in 2007 to 55% in 2010, and Ireland is now rated the second lowest ranking country in the EU for provision of finance to small and medium sized enterprises. Meanwhile, Irish banks, despite their newly cautious lending practices, are highly dependent on short-term loans (as discussed above) of over €150 billion from the ECB and the Irish Central Bank as bank deposits have fallen steadily. If Ireland were to try and return to the private financial markets, it could probably only borrow at a very high rate of interest.

The scale and secretive nature of the debt

Debt as a proportion of national income will likely be 144% in 2012 and will probably still represent 140% of national income by 2015 – despite several years of savage austerity.1 When the aforementioned 'contingent liabilities' are factored in, the Irish national debt stood, according to the recent debt audit, at €371.1 billion on 31 March 2011. This is equivalent to almost 300% of Irish income. Of this, €279.3 billion (over 75%) is accounted for by the state-covered debts of the Irish banks, and this, as the audit notes, is before taking into account the likelihood that much of the direct government debt of €91.8 billion may itself have arisen from the banking crisis. In other words, the audit proves conclusively that the Irish debt crisis is a crisis of private (subsequently socialised) debt, not public debt – the allegedly 'bloated' nature of the Irish public service, or 'generous' welfare entitlements, did not cause this crisis. As the audit puts it, "it is clear that the bulk of Irish government debt has arisen directly from the banking crisis, the decision in September 2008 to rescue all of the Irish banks". Alarmingly, the audit notes that the headline figure of €371.1 billion may be an underestimate. For example, the audit does not count unguaranteed bonds issued by the banks (and therefore not legally the responsibility of the Irish state) as part of the debt but, to date, the Irish government, presumably at ECB insistence, has been repaying these bonds also.

So who then is getting all this money? Another hugely important finding from the audit concerns secrecy, what the audit describes as "the anonymous nature of bonds, and the culture of confidentiality and secrecy which surrounds them". We simply do not know to whom the debt is owed and to whom it is being repaid. (We can safely assume it is European financial institutions as, if it were not, the ECB would not be so vigorously protecting their interests). And yet the bondholders are obviously exerting enormous influence, directly or indirectly, over Irish government policy with attempts to ensure that the bondholders take a 'haircut' (some write-down in the value of the debt) being strenuously resisted by, in the particular, the ECB. The audit argues that "The importance of the holders of the debt in determining policy suggests that their relationship to the Irish state is more controlling than is usual for bondholders, and strengthens the case against their anonymity".

The underlying (illegitimate and undemocratic) agenda, and the need for resistance

At the end of the day, this money cannot possibly be repaid in full – a default is inevitable. But the ECB and other dominant actors are explicitly demanding that the bondholders be paid off to the greatest extent possible, that as much as is feasible of the debt be socialised in advance of any possible default. €4.3 billion was reportedly paid out to bondholders in September 2011 alone. This socialisation of bank losses is the simple logic of what is happening in Ireland (and in Greece and Portugal, and probably soon in other countries also). In the meantime, the Irish people are being asked (or may in the future be asked) to repay a debt that was, overwhelmingly, not of their making and from which they gained little or nothing – this constitutes a prima facie case of illegitimate debt. And the lack of transparency means that faceless market actors are exercising enormous influence over Irish government policy, which violates fundamental democratic principles that power should be exercised in an open and accountable manner.

As if this was not bad enough, the Irish government is also using the excuse of the crisis to drive through other policies that likewise benefit the corporate sector, such as reducing rates of pay for already low paid workers despite the fact that a lack of wage competitiveness is not at the root of Irish problems. This is a classic example of what Naomi Klein calls the ‘shock doctrine’ effect, whereby a crisis is used to ram through policies that restructure societies to the benefit of corporate interests.

In the face of these appalling and glaring injustices, what are the Irish people doing? Sadly, not enough. There have been well attended protest marches, but, for example, in 2010 only 511 Irish workers were involved in industrial disputes. Why the relative inaction? There is a range of answers to this question. Emigration acts as a ‘safety valve’, draining off potential social unrest. The mainstream media predominantly insists that there is no viable alternative to austerity and debt repayment. Furthermore, people invested huge hope in the election of February 2011, believing that a change of government (as occurred) would lead to a change of policies (as the then opposition parties had promised), but instead the same programme of austerity and bank bailouts has been continued. And finally, and perhaps most importantly, there is the quiescent and non-confrontational attitude of most trade union leaders (and civil society leaders more broadly), who maintain (or wish to maintain) a cooperative relationship with government and an aversion to militant protest.

But all is not doom and gloom. The 2011 election did not deliver the policy change the electors anticipated, but it did deliver the election of a sizeable number of left wing members of parliament and a rise in electoral support for left-leaning Sinn Fein – the total Left vote may have exceeded 20%, which is very high by Irish standards. There are also various citizens’ initiatives emerging, including local ‘burn the bondholders’ protests. We may not yet have seen Irish people take to the streets as in Greece and Spain, but the anger is growing and, hopefully, the appetite for action.

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