NAMA: an Institutional and Operational Failure that Keeps Expanding[1]

Dr Constantin Gurdgiev[2]

Adjunct Lecturer in Finance, School of Business, Trinity College, Dublin,
Head of Research, St Columbanus AG.

NAMA "is a key part of the solution to the current banking difficulties in Ireland," so says The National Asset Management Agency: A Brief Guide from the 30th March 2010[3]. "NAMA is buying loans, at a discount, from the participating banks. These loans come from the riskiest part of the banks' portfolios - loans secured on development land and property under development. In addition, the largest property-backed loans of all the banks in the scheme are being acquired. Taking these riskier loan classes off the balance sheets of the banks concerned will make the banks safer and more secure for depositors and investors and free them to lend again to the productive economy."

Reinforcing the end-objective of restoring functionality to the banking sector, the same document claims, that "Replacing these property-related loans with Government Guaranteed Securities will remove uncertainty about the soundness of banks' balance sheets and make it easier for them to access funds in the international financial markets. Banks cleansed of risky categories of loans will be free to concentrate on their core business of lending to and supporting businesses and households."

A year later, on March 22, 2011 in his address to the Licensed Vintners Association AGM, Mr. Frank Daly, Chairman of NAMA stated: "Essentially, NAMA's function is to cleanse the balance sheets of the participating institutions of their commercial property loans and thereby enable those banks, with the liquidity created by NAMA securities, to refocus their attention on productive lending to businesses and to individuals… NAMA's key objective is to generate a commercial return for the taxpayer over time."[4]

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[1] *Forthcoming in* NAMALab, Dublin School of Architecture, Dublin Institute of Technology, October 2011.

[2] Contact: gurdgic@tcd.ie
All views expressed in this article are those of the author and do not represent the views or opinions of any of his employers, contractors or clients. All errors and omissions are author own.

[3] Available from: http://www.nama.ie/
[4] Available from:
www.nama.ie/Publications/2011/AddressByNamaChairmanToVintnersAssociation22March2011.pdf

In summary, NAMA objectives are explicitly identified as:
1) Acting as a key part of the solution to the current banking difficulties in Ireland;
2) Remove uncertainty about the soundness of banks' balance sheets and free them to concentrate on lending to and supporting businesses and households;
3) Make it easier for the banks to access funds in the international financial markets; and
4) Generate a commercial return for the taxpayers over time.

Failure to Establish the Extent and Benchmarking for the Core Objectives

From the starting line, NAMA was endowed with poorly defined and even contradictory remit.

The first objective implies existence of a comprehensive plan for repairing the banking sector in Ireland of which NAMA forms a key part. Yet, no specific targets or benchmarks for NAMA set out either the expected specific effects of NAMA on the banking sector, nor indeed anchor NAMA performance to the performance of the banking sector. Neither the NAMA-establishing legislation, the NAMA Act 2009[5], nor NAMA Business Plans 1 and 2[6] provide explicit numerical performance benchmarks for either NAMA itself or for any measurable expected impacts of NAMA on the participating banks. No dates for delivery on any of the four above objectives are specified and no quantified assessments made as to the projected effects NAMA is to have on the banking sector or individual participating institutions.[7]

In short, NAMA's first objective remain unsupported by a feasibility assessment. If NAMA were indeed to form a part of the solution to the banking sector crisis in Ireland, it would have direct and measurable bearing on the banking sector performance and health that can and should be integrated into its future performance assessments, pay and bonuses structures. In addition, as a part of the solution, NAMA can be expected to generate risk and benefits spillovers to other areas of the comprehensive banking crisis resolution policies, such as, for example recapitalisation requirements and capital and liquidity adequacy conditions under which the banks, interacting with NAMA, operate. Once again, none are provided in the documents pertaining to NAMA.

Even ex-post NAMA creation and NAMA purchases of the troubled banks assets, with the spilover effects now apparent in the write downs of banks assets as the result of transfer to NAMA, no analysis of NAMA effects on these balance sheets is

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[5] Available from*:* www.attorneygeneral.ie/e**Act**/2009/a3409.pdf
[6] Available from:
www.nama.ie/Publications/2010/NamaBusinessPlan30June2010.pdf and www.nama.ie/Publications/2011/NAMA_BPv2_Introduction_and_Overview_18Jan11.pdf
[7] Constantin Gurdgiev "Economics: Alternatives to Nama", Business & Finance, October 2009 http://www.businessandfinance.ie/index.jsp?p=378&n=383&a=1488

provided by the authorities and no linkages from NAMA targets to banks operational and regulatory positions are developed.

Of course, this is exactly what the IMF has warned the Irish Government about in its note issued back in April 2009[8]. As stated in the Irish Times February 2010 article (cited above): "Speaking at the publication of the Nama legislation last September, Mr Lenihan said Nama would “strengthen and improve” the funding positions of the banks “so that they can lend to viable businesses and households”. Taoiseach Brian Cowen had said the Government’s objective in restructuring the banks was to generate “more access to credit for Irish business at this critical time”" In addition to providing early evidence for the existence of the first three objectives as defined above, these statements also preclude what is to become the extremely characteristic feature of NAMA – its secretive and non-transparent nature.

Per Irish Times report cited above, "In an internal e-mail dated June 6th, 2009, ...senior department [of Finance] official Kevin Cardiff warned against making public any official estimate for the losses faced by the banks, saying that the department had not made this information public. “We naturally shared with the IMF team our informal views on the range of possibilities, but would be uneasy about seeing these formalised,” said Mr Cardiff, who has since been appointed secretary general of the department."

This is uncomfortably close to an admission that the Department of Finance willingly withheld crucial information about Nama from the official communications, including those with IMF, in order to avoid this information being disclosed publicly through future FOI requests. The Government and its officials have thus knowingly engaged in acts of public deception when they were making claims about NAMA's expected impact on credit supply, the banks balance sheets and NAMA's expected costs and losses.

The second objective implies existence of another set of performance targets for the banking sector and, thus – via the first objective – for NAMA. These targets would relate to banks actually restoring lending in the economy via targeted or at the very least measurable increases in credit supply. As with the first objective, this stated goal of NAMA remains un-quantified by the legislation, the regulators and by NAMA itself.

Ditto for the third objective. Almost two years into NAMA operations, we simply have no clarity on what will constitute NAMA success in helping to repair banking system in Ireland or what metric can be used to judge whether the banking sector has actually been reformed and recovery has been achieved.

Both, the second and the third objectives of NAMA preclude participation by the largest NAMA-client, the Anglo Irish Bank in the scheme. As was pointed correctly

[8] IMF warned Nama would not lead to significant bank lending, The Irish Times, February 2, 2010
http://www.irishtimes.com/newspaper/frontpage/2010/0208/1224263954908.html

by the FTAlphaville: “If Nama is indeed intended to free banks’ balance sheets of non-performing assets and induce them to lend to small businesses, why exactly has Anglo Irish Bank been included in the scheme? Anglo Irish does not have a retail branch network — and has no intention of establishing one — and is not a significant source of financing to small Irish businesses. Rather, about half of its business is as a lender to middle-market companies and high net worth individuals, while the other 50 per cent comprises secured lending to property investors.”[9]

Incidentally, the obscure, undefined nature of NAMA objectives and timings is carried through to the NAMA auditors work. The Comptroller and Auditor General (CAG) October 2010 assessment of NAMA’s first year of operations[10] can be best described as inadequately defined in terms of references, lack of disclosure of the audit approach, poorly structured results, weak and ad hoc conclusions and a complete lack of any substantive recommendations for operational improvements. The CAG report also fails to provide any timings for both the past performance that was assessed or the future targets to be achieved. Neither does it provide a rigorous risk analysis of the current operations or future performance.

As discussed in more details below, NAMA has resoundedly failed to deliver on all three top objectives, in part due to the inherent contradictions between objectives 1-3 and objective 4 (as shown in the next section), but in part also due to the fundamental flaws in Government policy on banks crisis resolution. The 2010 assessment of NAMA effectiveness vis-à-vis the banking system by the Lombard Street Research strikes the right chord here:
“The further turmoil that engulfed the Irish banking system in September and October 2010 is clear evidence that, in so far as NAMA’s brief was to rescue the Irish banking system, it has been at best a very qualified success. This is partly due to circumstances beyond NAMA – or even Irish – control, namely the fall-out from the sovereign debt crisis in Greece and the rest of southern Europe over the spring and summer. But, importantly, the impact of those issues has been exacerbated in part due to a flaw in the idea of NAMA. Rather than following the Swedish model and nationalising the failing banks, removing impaired loans to a bad bank and then re-privatising the now healthy banks, the Irish government attempted to keep the banks (with the exception of Anglo Irish, which was nationalised early on in the crisis) as going concerns. This failure to ring-fence ‘good’ loans and so boost the health of the banking system, laid part of the groundwork for the secondary problems.

To quote Mr. Michael Somers again: “Namaism was supposed to take toxic loans off the banks’ balance sheets to free them up and it would be funded with cheap money from the ECB. So what actually happened? Namaism has created a monster that has done the opposite to what was intended. With its haircuts and discounts and its

[9] “[Ireland's Bad Bank] NAMA, SPVs and other Irish magic”, by Stacy-Marie Ishmael, November 04, 2009. http://ftalphaville.ft.com/blog/2009/11/04/81221/nama-spvs-and-other-irish-magic/
[10] Available from: http://audgen.gov.ie/documents/vfmreports/76_NAMA_Acquisition_of_Assets_Rev1.pdf

immediate crystallisation of losses, it has wrecked the balance sheets of the banks and has ensured that there will be no net new lending by them."" [11]

Inherent Contradictions and Internal Inconsistencies of Poor Institutional Design

The fourth objective stated above represents a direct contradiction to the first three objectives – severely and jointly.

For NAMA to generate any (non-negative) commercial return for the taxpayers requires applying deep discounts to the assets purchased – something that NAMA has largely (albeit incompletely, due to an artificial valuations cut-off date of November 30, 2009, as outlined below) has achieved. This automatically meant that the transfer removed from the banks' balance sheets a number of cash- and profit-generative assets. In other words, some of NAMA assets are yielding positive commercially-benchmarked risk-adjusted expected returns and these returns were transferred from the banks balance sheets to the benefit of NAMA and to the detriment of the banks. Similarly, some of the assets purchased by NAMA are revenue-generative and could have been used by the banks to secure repo funding.

Removal of these assets from the banks balance sheets required supplementary recapitalizations of the banks by the Exchequer on top of the funds extended to them by NAMA. In effect, pursuing the fourth objective, NAMA acted to undermine banks balance sheets by taking over performing loans alongside 'bad' assets, thereby violating objectives one through three. De facto, NAMA reduced, not enhanced, banks ability to raise funding from external sources and potentially distorted banking sector assets valuations – the effects that had to be corrected by placing additional burden on taxpayers.

Government-commissioned research unequivocally shows that NAMA has resulted in a direct charge on taxpayers to the tune of €41.8 billion through realized losses on banks balance sheets post-NAMA transfers.[12]

From day one of its existence, NAMA had an intrinsic interest in underpaying banks for the good assets is was acquiring and overpaying for the bad ones. In words of Lombard Street research: "By acquiring unimpaired – ie, 'good' – loans as well as impaired – 'bad' – NAMA undermines the Irish banking system that it is ostensibly set up to save".[13]

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[11] NAMA one year later – A Lombard Street Research Report for the Construction Industry Federation, November 2010, page 10

[12] Misjudging Risks: Causes of the Systemic Banking Crisis in Ireland, Report of the Commission of Investigation into the Banking Sector in Ireland, March 2011 (The Nyberg Report), Figure 2.16

[13] NAMA one year later – A Lombard Street Research Report for the Construction Industry Federation, November 2010, page 6

In return, NAMA allocated to the banks own debt securities which are guaranteed by the State, but which carry risk inherent in any sovereign-guaranteed instruments. As the result, banks' starting capital base in the form of NAMA notes and bonds was subject to several downgrades by rating agencies and is now largely recognized as being of sufficient quality for capital purposes, primarily by the ECB and the Central Bank of Ireland, but not by market funding sources.[14]

However, the problems with NAMA last objective go well beyond the implied conflict between the need for generating commercial returns to the taxpayers and repairing banks' balance sheets.

Nowhere in the NAMA documents is there a stipulation of what the 'commercial' returns that NAMA is supposed to generate for the taxpayers will look like. Will NAMA target a 5% annual return or 2% annual return? Are these returns inflation-adjusted or nominal? Are these returns net of capital and operating costs, or gross? In effect, NAMA is free to achieve a loss of €X billion and a gain of €Y billion and anything in between, where, implicitly (but not legislatively) €X is the amount of the total of the promissory notes and NAMA bonds issued, less €1.5 billion subordinated debt, and €Y is any number above zero.

In fact, there is no referencing in either terms or objectives of NAMA, or in the deployment of the concepts of returns, profits or losses to the fact that under Section 50(3) of the NAMA Act 2009, there is an allowance for NAMA to issue additional €5 billion of debt for considerations other than purchases of assets. In September 2, 2010, NAMA has, in fact, completed the establishment of a €2,500,000,000 Euro-Commercial Paper Programme to cover 50% of this allowance[15].

Adding to the confusion about NAMA 'returns' targets expressed above, Mr Daly stated in the aforementioned presentation on March 22, 2011 that [emphasis is mine] "…NAMA had paid €30.5 billion for its acquired loan assets to date. That consideration, by and large, represents *the current market value* of the property and other assets securing the loans. NAMA's task, over the next seven to ten years, is to recover that amount for the taxpayer through debt repayments by debtors or asset sales."

Note that Mr Daly sees 'commercial returns' to be achieved by NAMA under the objective (4) above as being equivalent to 'recovering the amount paid'. In other words, NAMA Chairman is either altering key NAMA stated objective at will in his own statements or believes that a gross return of zero percent represents a 'commercial return'.

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[14] For example see: http://www.zerohedge.com/article/europe-prepares-bloodbath-open-after-ireland-lowered-sp-aa-aa-outlook-negative, http://namawinelake.wordpress.com/2010/10/06/fitch-now-sees-nama-breaking-even-doesn%E2%80%99t-stop-them-downgrading-nama-bonds-though/ and http://trueeconomics.blogspot.com/2010/07/ecoinomics-19710-moodys-downgrade-redux.html

[15] See http://www.nama.ie/NAMAECP.php for details

Also note that in fact, as of 2 March 2011, NAMA had acquired EUR 71.2 billion of loans for a consideration of €30.2 billion, representing a discount of 58%[16]. Clearly, NAMA chairman has no problem rounding up his figures by hundreds of millions. But more importantly, the 58% discount reflects NAMA anticipated long term economic value uptick.

The claim that NAMA paid 'current market value" for the assets acquired is, therefore, patently wrong and clearly contradictory to the objectives of repairing banks balance sheets and the operational realities of NAMA. In fact, according to NAMA legislation, NAMA valuations of the assets cannot factor-in any changes in values that took place since November 30, 2009 – the cut-off date for NAMA valuations under Section 73 of the NAMA Act 2009[17]. However, NAMA is yet to finish the process of purchasing a number of assets, and since November 2009, Irish property markets have suffered significant declines (see below).

In addition to assessing the current market values of loans by reference to 30th November, 2009 NAMA had also applied a premium, reflecting the expected long-term economic value uplift on the assets, with the average premium paid by NAMA estimated to be around 10-15%. NAMA paid for the assets using NAMA bonds which accounted for 95% of the total value of the assets, as assessed by NAMA plus expected long-term economic value premium, with the remaining 5% covered by subordinated NAMA debt, redeemable only if NAMA makes a profit. So far, NAMA allocated ca €30.2 billion for the banks assets, of which €1.5 billion is subordinated debt.

According to the CSO, "NAMA have been advised that, while there may be some short-term fall in Market Values after assets are purchased, 'based on capital values, the bottom has been reached in the US, UK and Europe', and in Ireland 'the market expects that the bottom may be reached in the last quarter of 2009 or the first quarter of 2010.' Based on the available expert advice, NAMA and the Department of Finance have concluded that NAMA will be profitable over its expected 10-year lifetime, estimating its net present value at some €6 billion."[18]

Of course, the bottom for the Irish markets – land, residential and commercial – remains unattained more than 17 months since the end of 1Q 2010, as the figures below clearly indicate.

Taking into the account the data on Tranches 1 and 2 transfers of assets to NAMA and the declines in values of commercial and residential properties since November 30, 2009 through today, NAMA total consideration of €30.2 billion extended to the

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[16] DBRS Downgrades National Asset Management Limited's Guaranteed Senior Debt to A (low), Trend Neg. August 18, 2011 http://www.dbrs.com/research/241674/dbrs-downgrades-national-asset-management-limited-s-guaranteed-senior-debt-to-a-low-trend-neg.html

[17] See http://namawinelake.wordpress.com/2010/03/21/namas-valuation-date-costs-taxpayers-upto-e5bn/

[18] Annex 2 Methodological paper for Eurostat on classification: ESA95 accounting treatment of the National Asset Management Agency (NAMA) and related majority privately owned SPV, CSO, September 2009

banks underlies the assets base currently worth less than €24 billion, with implied current book loss of €6 billion gross, or €3.5 billion, net of €1.5 billion subordinated bonds that are not redeemable in the case of a declared loss.

Hence, either NAMA did not pay close to the market value of the assets it purchased from the banks – in which case NAMA obtained a direct subsidy for its balance sheet from the banks, and ultimately, from the taxpayers providing capital cover for the banks. Or NAMA is nursing a massive 20% loss rate on its assets against a 10% expected long-term economic value uplift. One way or the other, NAMA leadership statements and its own accounts are either providing incorrect information or concealing losses.

Per CAG report of November 2010 (cited above), NAMA estimations of the long-term economic value premium were developed by London Economics back in 2009 with assumed 2010-2016 uplift in commercial and residential property values as follows: Ireland +17.7-28.8%, UK +14.7-20.3%, US +10.5-23.7%. Since November 30, 2009 valuations cut-off date, Irish residential property prices have fallen by ca 17.7% according to the Central Statistics Office Residential Price Index through May 2011. Commercial properties have declined in values by 18.1% between Q4 2009 and Q2 2011 according to the Jones Lang Lassalle Quarterly Commercial Property Index.

These figures imply that just to break even, gross of costs and legal fees and cost of NAMA bonds interest charges, NAMA valuations will require a 2012-2016 uplift of some 45-50% in Ireland, or the expected annualized rate of growth in residential and commercial prices of 6-8% from 2011 forward.

The extremely low likelihood of these projections becoming a reality suggests that NAMA is engaged in a risky gamble with tens of billions of taxpayers money. The lack of clarity on NAMA core performance targets suggests that this gamble has undefined payoffs. The inability of the NAMA-establishing legislation to clearly identify the forms in which any returns can be remitted from NAMA to the Exchequer and further on to the taxpayers, implies that the returns, were they to materialise, are subject to an arbitrary utilization by the Exchequer. In effect, Irish taxpayers have been forced by the State and NAMA to play a very expensive lottery with undisclosed prizes and no independent oversight over the lottery draws and payouts.

Fighting a Rising Tide of Unmanaged Risks and Losses

The latest set of accounts for NAMA cover the operating year of 2010[19] and 1Q 2011, and were released in August. In a surprising move, NAMA published both at the same time – a practice normally associated with the Department of Finance, which prefers to publish adverse data in bulk, thus complicating analysis and de facto restricting media coverage of the specific details. To the extent we know about NAMA

[19] www.nama.ie/Publications/2011/NAMAAnnualReport2010.pdf and http://nama.ie/ for 1Q 2011 Section 55 Quarterly Report 31 March 2011 and Section 55 Quarterly Accounts 31 March 2011.

operations, the organization made a profit of €91 million in Q1 2011, against the declared loss provision of €1.485 billion for 2010 as a whole.

Of course, quarterly profits are not offset against any capital charges, which are reserved for annual reports, and thus do not reflect changes in asset base valuations. Nor do these numbers reflect the true cost of running NAMA and related undertakings which are associated with maintaining excessively high (compared to credit issuance levels and assets valuations) levels of employment in the banks.

We also know that Nama interest income on its assets has fallen from €330.3 million in Q4 2010 to €276.2 million in Q1 2011. In best traditions of NAMA, we were not told why such a reduction took place. NAMA also generated ca €254 million in repayment of principal and disposal of assets.

According to the latest quarterly results, NAMA holds €17 billion of performing assets as referenced to the original book value of assets purchased, or 23% of all loans. This implies that 77% of NAMA assets are under water.

Now, let us do some simple calculations that NAMA and its auditors refuse to contemplate. In Q1 2011, NAMA current annual cash yield potential, based on performing assets base, runs at around €588 million. Nama cost of financing its bonds runs at 1.5% per annum and amounts to annual interest bill of €427 million. This means that at this stage, NAMA projected net cash flow surplus – before costs and disposals – is in the region of €161 million. However, over time, the performing assets share of total assets pool is likely to decline as performing loans are being paid down and better assets are being sold.

It is worth noting that NAMA has entered into the interest rates swaps that, per CAG report imply that the agency will see its interest income fall below the cost of interest on financing its bonds if the Euribor were to rise above 3.8%[20]. Historically, since January 1999, 12 month Euribor average monthly rates were in excess of 3.8% in the periods of December 1999-June 2002 and again in October 2006 through November 2009. So far, 2011 daily maximum rate has reached 2.201%. This implies that NAMA is hedged against adverse movements in the interest rates with probability of 0.58 – a surprisingly high risk exposure for an entity with an allegedly conservative mandate, as stipulated in the fourth objective above.

In addition to the pay down of performing loans, NAMA is facing a host of potential future headwinds. For example, of the remaining 77% of assets – the non-performing ones, some 86% are loans that are overdue 120 days and longer. These types of loans are unlikely to ever swing back into performing assets category and will require costly winding up process. These come on top of administrative expenses that are so hefty, the agency paid €46 million in 2010 and €18 million in 1Q 2011 to cover these.

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[20] See http://audgen.gov.ie/documents/vfmreports/76_NAMA_Acquisition_of_Assets_Rev1.pdf Annex B, Figure 5.3

Operational Failures are Nested in the Inadequate Institutional Design

All of this suggests that NAMA is currently working against the rising tide of costs, held back by a shrinking retaining wall of interest revenues. It is virtually inevitable that the agency will run into negative interest generation over the next few years. The headwinds pushing for this date forward are:

- Potential increases in non-performing loans pool due to new insolvencies of developers behind the currently performing assets,
- Higher costs of financing,
- Increased rates of amortization and depreciation on unfinished and unoccupied properties, and
- Deterioration in credit ratings.

Yet, once again, there is no expressed concern neither by the agency itself, nor by the auditors, nor by the Government officials about these risk considerations, with exception of currency and interest rates risks. “Don’t ask, don’t tell” seems to be the modus operandi when it comes to NAMA performance assessments and risk analytics.

This is hardly surprising. In addition to being established by a legislative fiat which imposes no clear, transparent, defined and benchmarked objectives, NAMA was set up as a vehicle to conceal the extent of the Irish state involvement in the banking sector bailout.

Nama is owned by a complex and non-transparent structure of quasi-private Special Purpose Vehicle – an undertaking with 49% state shareholding offset by the 51% private sector participation.

Private sector owners of NAMA SPV are in a league of their own when it comes to bizarre financial structures bestowed on the world over the centuries. NAMA SPV is majority-owned by the divisions of and entities controlled by the very same banks that transact with NAMA in sales of assets and assets management. Per statements in NAMA Business Plan 2 and the earlier statement from the Minister for Finance (April 2010) that NAMA SPV is majority (51%) owned by the Irish Life Investment Managers – the asset management company of the Irish Life & Permanent, plc (now itself in the state-ownership), the New Ireland Assurance (a part of the Bank of Ireland Group which ahs a sizeable state shareholding), and the Allied Irish Banks Investment Managers (part of the AIB Group which is state-owned following 2010 recapitalizations of the bank).

NAMA technically retains veto power over the SPV decisions and the state guarantees 95% of the funds extended by NAMA. Yet, despite that, as long as the 51% share of NAMA SPV is held by ‘private’ investors, NAMA bonds and subordinated debt are not counted officially as a part of the Irish Government General Debt.

Even more strange twists of NAMA SPV structure emerge when one considers the two facts that:

1) NAMA SPV was created to avoid NAMA debts being counted as public liabilities by assuring majority private ownership of the SPV and thus creating

a semblance of NAMA ownership being held at arms-length from the State, yet

2) According to the official documents filed with the Eurostat: “The Master SPV will have its own Board, with members appointed by NAMA and the Private Sector equity investors. However, since the State is guaranteeing the securities issued by the Master SPV, the NAMA representatives on the Board will maintain a veto over all decisions of the Board that could affect the interests of NAMA or of the Irish Government.”[21]

In other words, Irish Government has decided to have the cake (keep NAMA SPV at arms-length from the State control) and eat the very same cake (endow NAMA with veto rights over SPV decisions exercisable in the name of “the interests of NAMA or of the Irish Government”). Just how, exactly, these two contradictions managed to escape the Eurostat is an entirely different saga.

In an ironic twist, the Government’s objective to use NAMA SPV to prevent NAMA liabilities being recognized as sovereign debt was another failure. As of today, all ratings agencies recognize NAMA debts as a part of sovereign liabilities with resulting cross-links between NAMA and Government debt ratings and the knock-on effect of NAMA debt onto Exchequer position.[22] It is also telling that in its legal opinion concerning NAMA, the ECB explicitly recognized NAMA bonds as Government-own bonds, with the opinion, of course, preceding the SPV creation.[23]

NAMA is a Vehicle Behind the Failed Banking Crisis Resolution Policies

This farce does not end with the Irish state bizarre merger with the banks it controls via NAMA. It extends to the point of Irish Government explicitly admitting that NAMA SPV structure was created for the sole purpose of evading recognition of NAMA debts as state-own obligations. The then Minister for Finance, Brian Lenihan stated in October 2009 that: “The preliminary decision of Eurostat means that the acquisition of the assets from the financial institutions by Nama may be treated as off-balance sheet in the budgetary arithmetic under European national accounting rules. In other words, it will not increase the general government debt ratio, and neither will our budget balance be directly affected by the Nama initiative.”[24]

However, there is much more to the SPV structure than complex accounting chicanery. At the time of its establishment, NAMA SPV was mandated to issue up to €54 billion of debt to cover expected €81 billion of assets it was about to purchase.

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[21] Annex 2 Methodological paper for Eurostat on classification: ESA95 accounting treatment of the National Asset Management Agency (NAMA) and related majority privately owned SPV, CSO, September 2009

[22] See: http://namawinelake.wordpress.com/2011/05/23/why-do-ratings-agencies-regard-nama-bonds-as-part-of-our-national-debt/

[23] Opinion of the European Central Bank of August 31, 2009 on the establishment of the National Asset Management Agency, CON/2009/68, article 1.1.

[24] Sunday Business Post: “Private sector role vital to keep debt ‘off balance sheet’”, 25 October 2009, by David Clerkin http://www.sbpost.ie/newsfeatures/private-sector-role-vital-to-keep-debt-off-balance-sheet-45217.html

The total capital held by NAMA SPV was €100 million shareholders equity. This, of course, implied that NAMA SPV was set up with upfront leveraging of 54,000 percent, well in excess of any other financial undertaking known to man. With actual debt issuance of €30.5 billon against the said capital base, NAMA was leveraged more 'modest' 35,000 percent which is still well ahead of 10,000 percent leverage reached by LTCM in early 1998 on the cusp of its collapse.[25] In effect, therefore, Irish Government has committed taxpayers funds (via a state guarantee of NAMA debts) to the entity that is providing extremely leveraged profit opportunities to the clients of the very same institutions the Irish state controls after directly bailing them out using taxpayers funds.

As Nassim Taleb recently remarked: "The core of the problem [with banking sector crisis resolution] is that asymmetry in payoff socializing losses and privatizing gain and the generator of that inequity is still there, worse than ever."[26] NAMA SPV is the living proof of this conjecture.

From Non-Transparent Origins to Remit Creep

Which brings us to the core reasons for creation of NAMA and the endowment of this institution with the powers well outside the limits of democratic mandate of any modern state. In Ireland, the real business of the nation leadership is preservation of the status quo – at the state level, political level, and since August 2007 – in banking.

NAMA is a focal point of all three. Through it, even in the midst of the current historic crisis, Ireland's political and executive elites continue to inhabit a parallel universe where responsibility and accountability are for the commoners, and transparency and governance are decorations for EU summits.

Aptly, in its current form, NAMA reigns supreme as the most non-transparent financial institution in the developed world. Its 'independent' directors are being selected behind the closed doors by those who count in their ranks 'specialists' and 'authorities' that presided over the systemic failures of our regulatory and supervisory regimes. Its risk, audit and strategy functions will be fully contained within the secretive and unaccountable structure of the organization itself. Its key employees were recruited from the incumbent banks, valuers and asset management firms with deep links to the Irish property bubble and to the very same lenders who's loans are now being 'restructured' under NAMA remit.

NAMA will not publish a full register of properties against which it will hold the right of seizure. Instead, the agency decided to publish only the list of properties subject to enforcement. This restriction was intended to protect privacy of the developers involved. Withholding this information from the markets, however, induces extreme

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[25] LTCM Speaks, by Joe Kolman, Derivatives Strategy, April 1999, http://www.derivativesstrategy.com/magazine/archive/1999/0499fea1.asp
[26] Transcript of Nassim Taleb's interview with BBC Newsnight, August 2011: http://rebel-alliance.org/2011/08/23/nassim-nicholas-taleb-the-banks-today-have-hijacked-the-government-banks-should-not-be-a-machine-to-generate-bonuses/

degrees of uncertainty as to the returns potential for any future commercial and residential development in the state. This uncertainty is only reinforced by the continuous declines in property values.

As a holder of the largest property-related assets portfolio in the history of the State, even under the constraints of full disclosure, NAMA would induce significant distortions to the markets for years to come. This concern was consistently advanced by a number of independent analysts, but also by the EU Commission[27].

NAMA accounting and audit functions will not comply with the requirements imposed by our regulators on public companies. Its directors, management and consultants enjoy a blanket indemnity that is unparalleled by the standards of any public office or company law. Their remuneration does not face even the farcical constraints that senior banks executives face. In fact, NAMA second year in operations saw the agency disbursing numerous performance bonuses, despite the fact that it has posted a net loss and despite the fact that there is no clarity as to what performance is being rewarded and how this performance is being assessed.

NAMA owner – the NAMA SPV – as outlined above is a fictitious shell entity with ghost investors and a minority shareholder (the state) in charge. Its board has no effective strategic or operational powers beyond those of rubber-stamping NAMA own decisions. Its executive does not have any tangible role to play in NAMA itself. That this scheme has been concocted with an explicit purpose of evading proper recognition of public liabilities arising from the state guarantee of NAMA debts, not in a distant shady off-shore location, but by an EU member state in the name of its taxpayers, and with our money under the blessing of the EU Commission adds a series of insults to the injury of de-legitimisation of the Irish State's democratic and governance credentials. This problem is only compounded by the lack of transparency in its operations.

As if the existent shortfalls of the legislation establishing NAMA were not enough, even after the entity approval by the Dail, the goalposts for its operational performance continue to drift.

Since its creation, the agency has engaged in the process of preparing for issuance of top up mortgages to entice buyers to the properties it seizes[28]. These top up funds will only be available to the customers of the Bank of Ireland and AIB, in effect providing state support for the duopoly system of Irish banking that is emerging under the Government plans. These top up mortgages will result in a very distortion to the markets for residential property in Ireland that are partially to be blamed for the previous debacle – higher LTVs extended to the buyers backed by artificially-low cost of financing. This time around, the Irish state, via NAMA, will be the sole driver of this risk mispricing.

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[27] EU Commission: State aid N725/2009 – Ireland: Establishment of a National Asset Management Agency (NAMA): Asset relief scheme for banks in Ireland, Brussels, 26.2.2010 C(2010)1155

[28] See: http://www.irishtimes.com/newspaper/finance/2011/0413/1224294555413.html

Mortgages insurance against the negative equity will be the next step – already announced by NAMA[29]. Once again, the agency appears to be entirely unconcerned with risks and the liabilities arising from such an undertaking in the markets that continue to decline.

Top-up development completion loans is the third pillar of NAMA strategy for embedding itself in the long-term structure of Irish property markets. The entity, that itself was incapable of producing a credible business plan, having to publish two versions of the document and having failed to convince any independent analysts in the functionality of both, has been engaged in business plan reviews with the developers whose loans it acquired from the banks. Expanding on the already farcical situation of a blind leading the blind, NAMA does not even manage directly the loans of the said developers. Instead, management of the assets is retained within special units housed in the banks, which originated the loans. In effect, NAMA role in approving business plans of developers, therefore, is simply a double cost exercise conducted on the same side of the balance sheet. First, the failed banks lenders, then the inexperienced and poorly staffed NAMA, both go over the developers' plans. Doubling the effort and costs at performing exactly the same process, then, in the view of Irish authorities, is expected to yield a different outcome from the original failures.

From Failure to Enlargement

The NAMA debacle, instead of repairing the banking sector in Ireland, has fuelled the ongoing run on the banks shares and contributed to the flight of corporate and residential deposits out of the insured banking institutions. In part, as the result of NAMA operations, Irish banks are now more dependent on ECB and Central Bank of Ireland funding than before the process of loans transfers started. Credit supply continues to fall off the cliff, while the banks are aggressively pushing up interest charges on the more vulnerable younger households with adjustable rates mortgages. The markets for foreclosures, as well as bankruptcy law reforms, have stalled, with the resulting lack of price discovery and turnover in the property markets at large.

Yet, perhaps the most worrisome feature of NAMA operations since mid-2010 is the evolving nature of the institution itself. NAMA's explicit unwillingness to surrender to proper democratic oversight of its operations, its continued expansion of own remit and inability to define specific numerically verifiable objectives, the lack of proper communications between NAMA and the Oireachtas, all suggest that NAMA is no longer an agency of the State.

The organization is so pathologically unable to face up to responsibility that as early as November 26, 2009, in an official NTMA presentation[30] the organization stated that "NAMA, with 67% of its prospective assets based in the Republic of Ireland and

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[29] See: http://www.independent.ie/business/commercial-property/nama-open-to-partnerships-in-property-funds-2656463.html

[30] NAMA Modus Operandi, see www.nama.ie/Publications/2009/NAMAPresentationNov2609UCD.pdf

an additional 6% in Northern Ireland, is heavily dependent on a sustained economic recovery on the whole island. This, in turn, will be dependent on the respective Governments' management of the economy and the restoration of competitiveness. As an open economy, Ireland should also benefit from growth among our large trading partners if economic fundamentals are restored." Thus, in the view of NAMA, exogenous factors of economic policies and environments, put the complete bound under NAMA responsibility for any future returns or losses.

Since its formation, however, the organization has moved on from the operational paradigm of development to the bureaucratized survival. NAMA no longer serves any purpose beyond the purpose of self-sustaining its own existence. The assets it owns are managed and maintained by the banks. The banks it was designed, allegedly, to restore to health are now zombie-fied to the point of no return for five out of six guaranteed institutions. The economy it was supposed to help is lumbering on with no credit supply and growing pressures on debtors from creditors.

NAMA, like a malignant cell, having anchored itself institutionally has now entered the stage of aggressive operational and remit metastasis – reaching out into residential lending, risk insurance, development finance and business holdings – all in an attempt to anchor itself into the real economy to avoid or evade policy-implied constraints on its own existence.