The Pathology of a Residential Real Estate Bubble and its Dramatic Consequences: An Emotional Rollercoaster

Between the mid- 1990's and the mid- 2000's, in a period characterized as the Celtic Tiger, the Irish residential real estate market experienced a boom. During the period from January 1994 to early 2007 house prices rose in excess of 500% and then in April 2007 they started to collapse with a sustained decline continuing for almost six years eventually stabilising in March 2013. From peak to trough this fall was in excess of 50% and in modern times is second only to Japan in terms of magnitude.

This series of years of steady price rises accompanied by sustained price declines constitutes a classic speculative bubble which was exacerbated by *groupthink* behaviour on the part of all the major actors in the drama: property developers, bankers, politicians, regulators, the media, economists, estate agents as well as property investors and homeowners themselves. When the property bubble finally burst it had disastrous consequences not only for the housing market, but also for the banking system and critically the entire Irish economy eventually triggering a €64bn bailout from the IMF, European Commission and European Central Bank in November 2010.

We argue that the models developed by standard economic theory, though highly mathematical and complex in nature, find it difficult to explain asset pricing bubbles and financial crises in any convincing way, and, in such models, the role played by emotions and social and group processes are largely ignored or consigned to the irrational.

We suggest that repeated asset pricing bubbles can be viewed on one level as the inevitable consequence of investors' unconscious search for transformational phantastic objects (Tuckett and Taffler, 2008) and the consequent emergence of *basic assumption* group behaviour. If the phantastic object itself pervades all the economic actors in society there may be no effective counterbalancing force to counter its emergence and, importantly, not be able to prevent its potentially dramatic wider economic consequences when the bubble it generates bursts. This happened in the case of the Irish residential property market bubble.

We explore the role that emotions, in particular *unconscious phantasy,* may have played in firstly escalating and eventually pricking this bubble. This view of the world is consistent with Kindleberger and Aliber (2011), who though they couch their model of market bubbles in terms of human emotions, they do so without providing an underlying theory of the mechanism by which these emotions oscillate as the phases of their model unfold.

Keywords: Emotional Finance; bubble, real estate

Introduction

In November 2010 the Irish Government was forced into seeking a €64bn bailout from the IMF, European Central Bank and European Commission as Government bond yields became unsustainable and credit dried up. The origins and magnitude of this bailout can be directly linked to the bursting of a classic speculative residential real estate bubble. During the period from January 1994 to early 2007 house prices nationally rose in excess of 500% and then in April 2007 they started to collapse with a sustained decline continuing for almost six years eventually stabilising in March 2013. From peak to trough this fall was in excess of 50% and in modern times is second only to Japan in terms of magnitude.

We argue that though residential real estate prices were increasing since 1994, post mid-2003 these real estate prices became increasingly detached from *fundamentals* and the market entered a period of *euphoria* or *mania*. During this period in particular, banks' loan portfolios grew geometrically relative to GDP growth rates whilst becoming increasingly concentrated in real estate lending activity. Much of this lending was financed by borrowing on international wholesale markets rather than domestically, and credit conditions were relaxed by increasing loan –to-value (LTV) limits and by term extension (including mortgage terms up to 40 years). As a consequence, once the residential real estate market started to cool it triggered a banking crisis as banks sources of funding dried up ultimately leading to a blanket guarantee by the Irish government on all six of the major Irish banking institutions in September 2008. This guarantee was for a sum of €400bn, more than twice the country's GNP. However, following the introduction of this blanket guarantee, the share price performance of these institutions continued to deteriorate as the concentration on real estate became more "apparent" eventually declining to such an extent that the banks were effectively (with the exception of temporary short- term ECB funding) cut off from the capital markets. As a result, these institutions, with one notable exception, progressively became nationalised[1]. This process of nationalisation in effect socialised the debt of the financial system creating a large government funding requirement to fill the regulatory capital shortfall arising from real estate losses which had to be financed by both taxation and government borrowing. However, given the bloated size of the banking sector that was effectively nationalised and its concentration in real estate related activities the ability of the government to absorb this burden became unsustainable with the yields on government bonds ultimately peaking at 7% in October 2010 precipitating the bailout in November 2010.

How can we make sense of a real estate bubble of such magnitude occurring and sustaining itself for such a long period of time and why when it burst did it have such "unforeseen" and "unpredicted" consequences for the entire banking system and ultimately the entire

[1] The only financial institution not to be eventually nationalised was Bank of Ireland, which thanks to its capital raising activity kept the proportion of state ownership to 36%.

economy? Why given the large macroeconomic imbalances and the domination of the real estate sector in banks' portfolios did no corrective actions take place prior to the bubble bursting? Why did the economics profession in general and those employed in government or quasi government institutions (notably the Central Bank) in particular, not warn of the implications of these macroeconomic imbalances, or indeed adequately signal that there was a property bubble prior to the bubble bursting? Why did government, the media, the Central Bank, top management in the banks, developers, economists, estate agents, property investors, senior civil servants and homeowners "collude" almost in the sense of mass psychosis and let this exposure continue to such an extent that when it burst it had extreme and prolonged implications not only for the property market itself but also for citizens, the banking sector and the viability of the Irish economy itself? We argue that existing models (economic and behavioural) are incomplete in their understanding and analysis of bubbles and that the role of *unconscious phantasy* and *emotions* in general can potentially provide an explanation.

We argue that repeated asset pricing bubbles can be viewed on one level as the inevitable consequence of investors' unconscious search for transformational phantastic objects. Our arguments are couched in terms of the "phantastic object" (Tuckett and Taffler , 2008), which has its basis in psychoanalysis, whereby individuals are in their lifetimes in a state of flux between the rational mind that tolerates risk and uncertainty and that part of the mind that is hotwired to pursue pleasure eschewing all negativity. The phantastic object fulfils the individual's deepest pleasurable desires to have exactly what they want when they want it. In such a setting in the early stages of an asset bubble this latter state of mind dominates distorting reality and all negativity in relation to the asset is either filtered out or split off into the unconscious and a *basic assumption groupthink* emerges. Eventually, however, this becomes unsustainable and reality intervenes ultimately triggering, after a period of denial, the re-emergence of the rational mind that reassesses values generating massive price declines. This view of the world is consistent with Kindleberger and Aliber (2011) who though they couch their model of market bubbles in terms of human emotions, they do so without providing an underlying theory of the mechanism by which these emotions oscillate as the phases of their model unfold.

We argue that in circumstances where the object emerging as a phantastic object is so hotwired into the psyche of the society where it is present it will potentially have disastrous consequences, as the pervasiveness of *basic assumption* group thinking may be such that no effective countervailing force emerges as a counterbalance. We suggest that such circumstances emerged and presented themselves in an Irish context and as a result the magnitude of the residential real estate bubble once it started to unravel had consequences not only for the Irish residential real estate market but also for the banking system and ultimately the solvency of the entire economy. There were even arguments made that the actions taken by the Irish Government at the time of the blanket bank deposit guarantee in September 2008[2] potentially had destabilising influences across the entire European Union with adverse

[2] The blanket guarantee was largely driven by initial denial and lack of prior remedial action > argue here about denial.

commentary by both the ECB and the British authorities amongst others. [3] We also argue that given the pervasiveness of the group think behaviour that it was difficult for society to embrace the guilt associated with getting caught up in the wish fulfilling phantasy and has caught itself up in assigning and allocating blame with the result that the phantastic object may continue to stay in the minds of market participants and hence history may repeat itself.

The remainder of the paper is structured as follows: In the next section we discuss economic theories of bubbles and the behavioural finance perspective. We also introduce emotional finance and its key tenets. The "official" reports on the (economic, banking, real estate) crisis are briefly reviewed but, though these reports are detailed and comprehensive, they only *describe* and really do not explain *why*. In the following section we set out our methodological approach and describe the data used in the study and how it was collected and analysed. Next we present our empirical analysis in the form of three distinct subsections. First, we divide the Irish residential property price bubble into the stage model of Kindleberger and Aliber (2011) to use as a basis for our subsequent empirical analysis, concentrating in particular on the euphoria stage. Second, we present evidence on residential real estate as a phantastic object and the detachment of residential real estate from *fundamental values* with this occurring in particular as market participants enter the euphoric (manic) state. Third, we present our evidence in relation to *groupthink* and how it pervaded the economics profession as well as other economic actors, including individual property purchasers, investors, developers, banking institutions, the Central Bank, politicians, and the media whereby the collective actions of all players propped up the bubble and lead to a manic defence (denial), when reality intruded and the bubble started to unravel. Finally, we discuss our findings raise public policy issues, and offer suggestions for further research.

Economic and Behavioral Paradigms, Emotional Finance and the "Official" Reports on the Crisis

Traditional finance assumes financial decision-makers are "rational". *Homo economicus* dominates and emotions are reduced to the irrational. In this system enshrined in the EMH the market is efficient and reflects available information and prices will only change if unexpected new information arrives in the market. In particular these models are predicated on *rationally functioning markets* where the collective *independent* actions of *rational* individual market participants ensure that prices are in equilibrium and reflect economic fundamentals. In such models groupthink is either ignored or regarded as irrational.[4] The

[3] By introducing such a generous blanket guarantee much more favourable than that in other countries it generated significant controversy with one senior finance official saying "*He (Alistair Darling) was fuming,* saying Ireland was reckless and irresponsible, he raged as to why we didn't tell them" Sunday Independent, 11 April, 2010

[4] Since the Global Financial Crisis, more recent economic models allow market participants to be *irrational* in stylised ways typically around "trend chasing" but typically without seeking to explore the underlying group

literature on bubbles itself is controversial (O'Hara 2008). At one level there is even a tendency to regard bubbles as unavoidable implying trying to understand their causes makes little sense (Shulman, 2014). In fact, there is even no general agreement on the definition of a bubble as economists may disagree on the fundamentals driving market prices, though as O' Hara notes, economists generally agree on the "*less controversial approach*" adopted by Brunnermeier (2007) in the New Palgrave Dictionary of Economics where bubbles are defined as being "*typically associated with dramatic price increases followed by a collapse"*.[5] In addition, some economists argue that even if bubbles exist nothing should be done to prevent them as the bursting of a bubble will simply involve a transfer of wealth from one economic agent to another. However, if bubbles occur and are financed by borrowing, the banking system, and even in extreme cases, the economy itself may be adversely impacted and there is agreement amongst economists that to prevent contagion actions should be taken (e.g. Jorda, Schularick and Taylor, 2015, Mian and Sufi 2009; Borio and Lowe, 2002). However, even in such circumstances there are disagreements over the types of policy actions to be employed and whether they should be employed ex- post or ex- ante. (e.g. Bernanke and Gertler, 2001, Cecchetti et al 2000).

Standard behavioural finance, on the other hand, recognises that investors are prone to bias and are fallible in their judgments recognising that an individual's ability to make complex decisions is limited and that decision making can be improved by recognizing that he/she can be prone to biases and errors of judgment. However, behavioural finance simply catches emotions in one catch- all heuristic, *affect*, characterised as the feelings of positivity/ negativity felt in decision making (Slovic, Finucane, Peters and MacGregor, 2002). Nonetheless, the premise is still that if only investors could learn to be less biased, then they would be more rational. (e.g. Shiller 2000, 2005, 2007, 2008).[6]

However, despite all market participants experiencing directly how emotion-laden the investment process is, emotions, and particularly those of an unconscious nature, are ignored by both paradigms. In this paper we adopt a more formal psychological perspective which has also led to valuable insights into the understanding of the recent parallel internet bubble (e.g., Taffler and Tuckett, 2005; Tuckett and Taffler, 2008). Specifically, we draw on the insights of a new area in behavioral finance known as emotional finance. This seeks to explain some of the unconscious processes driving individual investment decisions, and market behaviors.[7] We suggest that acknowledging the role of unconscious fantasy in all

processes at work. (e.g. Scherbina, 2013; Ling, Ooi and Le, 2015; Glaeser and Nathanson, 2015; Towbin and Weber, 2015).

[5] The controversy can arise because the definition of a bubble is inextricably linked to its possible causes and effects, matters on which there is no general agreement. As O'Hara (2008) notes some economists deny that bubbles exist, others that it is only possible to identify a bubble ex post, whilst the causes of bubbles themselves are disputed even by those who agree that asset prices can deviate significantly from intrinsic values.

[6] Shiller (2005, pp. 159-160) sets speculative bubbles taking place in the context of herding behaviour, information cascades and the "greater fool theory" which have also been modelled in economic theory in rational terms (e.g. Hirshleifer and Toeh, 2003)

[7] Though Tuckett and Taffler (2008) were the first to coin the concept of the phantastic object, it is rooted in psychoanalysis, and relies on widely accepted clinical thinking about the working of the *unconscious* mind in which reality is sensed differently in different mental states. As Eric Kandal (1999, p. 505) Nobel Laureate psychiatrist and neuroscientist points out*" psychoanalysis still represents the most coherent and intellectually*

human activity can help us explore aspects of investor behavior that cannot be explained using more conventional approaches. In particular, here, this can help us make sense of the drivers of the Irish residential real estate bubble, and its different stages as it unfolded and importantly why the spillover effects to the banking sector and ultimately the macroeconomy were either ignored or underplayed.

Drawing on the psychoanalytical understanding of the human mind emotional finance explicitly recognises that investing involves an emotional attachment and *ambivalence* (Tuckett and Taffler, 2008). The inherent uncertainty in the predictability of future outcomes generates powerful feelings of *excitemen*t and *anxiety* associated with an asset and hence shapes reaction to news. When a phantastic object emerges the *pleasure principle* which Freud (1908) argues is innate in all human beings overrides the *reality principle* meaning that all potential negativity is split off or repressed and rendered unconscious.[8] The manifest cover story (Tuckett and Taffler, 2008) that "*this time it's different*" dominates (Kindleberger and Aliber, 2011, p. 29; Reinhart and Rogoff, 2009) enabling this departure from reality whereby possession of the phantastic object leads to unconscious feelings of omnipotence and wish fulfilment in the sense of Aladdin and his lamp to have "*what you want when you want it*" (Tuckett and Taffler, 2008). In this *psychic reality* the desire for trust in the asset dominates anxiety and all negativity is suppressed (Shapiro, 2012).

Groupthink and the factors generating groupthink lie at the heart of emotional finance, unconscious fantasy and the emergence of the phantastic object. Groupthink and its role in the unconscious relates back to Bion (1952) whereby when a phantastic object emerges, a *basic assumption* group will emerge acting as a support group whereby all negative news is unconsciously split off and repressed (and those expressing contrarian views may be dismissed or indeed vilified) and the group exists to accentuate and reinforce the positive so as not to disrupt the unconscious phantasy. The purpose of the group (or market) then becomes to provide comfort to the group members (investors) through the unconscious defences the group as a whole adopts against anxiety, and what its members don't want to know. In this way, continued wishful thinking and the good exciting (pleasurable) feelings

satisfying view of the mind". Bargh and Mosella (2008) show that the activities of the unconscious mind precede their experience, explanation and ownership by the conscious mind and point out that "*Freud's model of the unconscious as the primary guiding influence over daily life, even today, is more specific and detailed than any to be found in contemporary cognitive or social psychology*" (p. 73).

[8] Freud (1908; page 144) argues "Hardly anything is harder for a man to give up than pleasure which he has once experienced. Actually we can never give anything up; we can only exchange one thing for another. What appears to be a renunciation is really the formation of a substitute or surrogate." Freud's pleasure principle is based on the omnipotence of the child at play in early childhood. In normal development a child moves from this sense of omnipotence towards a more or less developed awareness of the facts of life (e.g. Klein, 1935; Milner, 1945, Sandler and Joffe, 1965). The child comes to recognise his dependence on others for satisfying wants and the limits to his personal capacity. But Freud (1908) argues that this development towards a more realistic sense of ones capabilities is always " more or less of a compromise and is always only more or less believed by the individual" (Tuckett and Taffler2008, p. 399)

can be promoted. This can easily lead to "herding" or positive feedback trading reflecting the appearance of unconscious wish-fulfilling fantasy initially being self-fulfilling.[9]

Such a process whereby the perception of reality may be altered by the state of mind in which investment judgements are made is consistent with Klein (1935). Klein distinguishes between the *depressive* state of mind (D), and the *paranoid schizoid* (PS) state of mind. In the D state of mind people see the world essentially as it is, complex with good and bad characteristics. The D state is consistent with standard economic models and is referred to by Bion as the *work group* philosophy, whereby information is used by individuals in the service of real thought. In such circumstances the "rational" actions of independent individuals will drive prices towards equilibrium.[10] In the PS state of mind financial actors are operating in a black and white world where the psychic pain of dealing with undesirable reality is avoided by mentally separating good and bad feelings which are now disowned.[11] Thus throughout life there is a constant tension between judgments grounded in reality, made in a D state of mind, and the more phantastical judgments made in a PS state of mind. The PS state of mind dominates when the phantastic object is unleashed. Any adverse potential consequences are lost sight of and unconscious wishful thinking dominates.

In such circumstances an asset pricing bubble will emerge as a path dependent model of investor emotions which is consistent with the five stage model of Kindleberger and Aliber (2011): *Displacement, Boom, Euphoria, Denial and Blame*. In the displacement phase, arising from some exogenous shock, assets can start to be perceived as transformational phantastic objects in the minds of investors. In the boom phase these unconscious mental images can become entrenched assisted by the media and other parties and become self-fulfilling prophecies. In the next stage, euphoria, prices may depart substantially from fundamentals eventually becoming unrealistic and unsustainable. In such circumstances the *basic assumption* group strives to sustain and maintain the wish fulfilling phantasy. In the next stage (denial) reality intervenes perhaps triggered by some external event and the basic assumption group vigorously fights off external reality until emotional logic is no longer sustainable and the bubble starts to implode. In the final phase (blame) the search for scapegoats dominates.

Kindleberger and Aliber (2011) in characterising bubbles give examples of the various emotional terms used to describe the euphoric state[12] that arises at the peak of a speculative

[9] The concept of groupthink has interesting parallels in terms of *The Wisdom of Crowds* (Surowiecki, 2004) which is consistent with efficient markets and standard economic models whereby the *individual* actions of rational utility maximisers will result in unbiased efficient prices versus *Extraordinary Popular Delusions and the Madness of Crowds* (Mackay, 1852) whereby crowds may make systematic "rational errors", consistent with inefficient pricing and the emergence of bubbles. MacKay wrote… "*Men, it has been said think in herds, it will be seen that they go mad in herds, while they only recover their senses, slowly and one by one*". Economists in their models generally assume that the *Wisdom of Crowds* paradigm describes reality.

[10] This is in contrast to the activities of the basic assumption group whereby the accumulation of information is not used for thought but rather to feel good (Bion, 1952, p. 245)

[11] *Schizoid* refers to the splitting and projection process where the good or bad experiences are disowned and projected onto others who are either idealised or feared as a result. *Paranoid* refers to the outcome of the splitting when one feels unconsciously persecuted by the recipient of these bad feelings.

[12] "*Manias…insane land speculation…blind passion…financial orgies…frenzies…feverish speculation…epidemic desire to become rich quick… wishful thinking… intoxicated investors… turning a blind eye.. people without ears to hear or eyes to see…*" (Kindleberger and Aliber 2011 p.41)

bubble and the panic[13] that ensues when the bubble bursts but importantly their model only *describes* and does not explain *why* investors behave in such a fashion.

We argue that residential real estate emerged and manifested itself as a phantastic object in the Irish context for a variety of reasons post early 2003 with the seeds sown from much earlier and that this *property obsession* pervaded Irish society to such an extent that all parties "colluded" in *basic assumption* groupthink behaviour, such that there was no effective countervailing force to prevent the bubble growing, or acting to prevent its devastating macroeconomic consequences before it eventually burst.

The severity of the Irish economic collapse precipitated the commissioning by the Irish Government of three reports into the crisis, all commissioned in February 2010 and written by authors from a predominantly economic background (Honohan, 2010; Regling & Watson, 2010 and Nyberg, 2011). In general they acknowledged that the overheating of the residential real estate sector lay at the epicentre of the banking collapse and tended to attribute *blame* to low interest rates arising from membership of the Euro, a favourable taxation regime, breaches of corporate governance in the banking system, relaxation of credit standards, breakdown in the implementation of risk management processes, overreliance on international wholesale deposits, the auditing and accounting profession being too accepting of banks accounting practices, benign government and politicians, pro-cyclical fiscal stance by the government, favourable media commentary, and the overreliance on a laissez- faire "principles – based" regulatory supervisory environment by the Central Bank. Interestingly, though these reports tended to largely agree on the potential causes they did not really explain *why* so many professionally adept bankers (including Central bankers), the body politic, senior civil servants, property developers, media, economic experts, auditors and households collectively and simultaneously come to make assessments and decisions that later proved seriously unsound in a considerable number of ways.

From our perspective of the three official reports only the Nyberg (2011) Report explicitly mentions behavioural issues as a possible driver of the crisis and specifically mentions "Group think" but even then only *explains* such behaviour in the context of a widespread belief in the efficiency of the markets:

" … the Commission frequently found behaviour exhibiting bandwagon effects both between institutions ("herding") and within them ("groupthink"), reinforced by a widespread international belief in the efficiency of financial markets" (Nyberg, 2011, page i)

Given that these reports did not explain *why* this perfect storm of potential and mutually reinforcing failures happened the Irish Government set up a Public Inquiry formally called the *Commission of Inquiry into the Banking Crisis* which had its first meeting in December 2014, has conducted oral hearings with in excess of 140 witnesses including the authors of the aforementioned reports as well as bankers, regulators, politicians, media commentators, newspaper editors, property developers, estate agents, economists, banking experts, academics and civil service officials and the former governor of the ECB, Jean Claude Trichet. The Inquiry is due to produce a formal report by Spring 2016 though media reporters

[13] "*Uneasiness, apprehension, tension, stringency, pressure, uncertainty, ominous conditions, fragility*" (Kindleberger and Aliber 2011 p. 91)

on the Inquiry have tended to state that no real new facts have emerged and that nothing meaningful will come out of the Inquiry.[14] We agree with the idea that it is unlikely that *new facts* will emerge and that there is a yet unobserved *smoking gun* in terms of an identifiable single culprit to assign the blame to. We will argue that the diffusion of blame in the existing reports and in media commentary is in theatrical terms what would be called a *classic misdirection* which will prevent *all* participants coming to terms with their participation in the *excitement* associated with residential real estate ownership and their unconscious repression of any corresponding anxiety reinforced by the activities of the basic assumption group. In such circumstances of searching for scapegoats learning will not be facilitated and there is a danger of repetition through a failure to come to terms with the collective guilt of participation in the manic dance to destruction. (Laplanche and Pontalis 1973, page 488)[15]. It is interesting to note in that regard that the OECD in April 2015 argued that there are warning signs that the Irish residential real estate market is starting to overheat again!

Data and Methods

This study was conducted using a combination of qualitative research techniques in order to study phenomena in naturally occurring environments enabling researchers to explore what people have to say through a textual analysis of newspaper articles, official reports, annual reports, television programmes, academic papers, literature (plays, novels and poems) and books written on the crisis which then allows us to explore the complex reasoning and nuanced arguments and themes behind these discourses to establish if they are corroborative and mutually reinforcing. (Kaczynski, Salmona and Smith (2012). Qualitative research can potentially offer insights into how social experiences are created and sheds light on how naturally occurring but poorly understood phenomena take place (Maquire et al (2004).

Our research uses both quantitative and qualitative aspects of content analysis (Krippendorff, 2004) to analyse text. Specifically qualitative aspects of content analysis uses such techniques as theme development, within case and between case comparison to enable the generation of insights from large volumes of textual data and to draw insights from the richness of the data and data sources. Quantitative approaches include using frequency counts of themes and extracting and analysing published data (e.g. OECD and Irish Government statistical databases) to establish trends and differences across time and to corroborate the qualitative data analysis.

Overall the use of various data sources offering convergent insight into the investigated phenomenon enhances the robustness of our results through data triangulation, thereby increasing validity (Jick, 1979).

[14] E.g. Banking Inquiry is slowly sinking into a political bog: it is a very Catholic Inquiry, a confessional for politicians, bankers, and civil servants that will change little, *Irish Times*, 28 July, 2015

[15] This potentially has interesting parallels in terms of what happened during the Global Financial Crisis as Citigroup's then CEO Chuck Prince's now infamous words highlight: "…*when the music stops in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing.*" (Nakamoto and Wighton, 2007).

In the first empirical section we trace out the trajectory of the Irish residential real estate bubble from the start of the Celtic years in 1994 up to the peak of the property bubble in April 2007 and its systematic decline until prices rebound post December 2012. We use the pattern of residential property price changes to separate time periods into the various stages of the Kindleberger and Aliber (2011) model identifying breakpoints by reference to patterns in residential real estate price changes themselves as well as by reference to key economic events which may be indicative of a change in the stage e.g. boom to euphoria etc. In this section we then use the Factiva database to map all articles over 1000 words (proxy for importance) written in the *Irish Times* newspaper (principal daily Irish national daily newspaper) that mention "real estate" or "property" or "house" or "housing" in their headline or lead paragraph. The purpose of this empirical section is to set the scene for subsequent empirical subsections by (1) mapping out the trajectory of the Irish residential real estate bubble and subsequent banking and economic collapse by reference to key events and, (2) explore the broad content of articles written during this period to see if these themes on a prima facie basis are supportive of our arguments. These articles will be referred to in the subsequent empirical sections as appropriate.

In subsequent subsections we draw from a broad range of quantitative and qualitative sources. As well as the aforementioned *Irish Times* we draw on articles written in the other leading national daily newspaper, the *Irish Independent* as well as other daily national, Sunday and local papers where appropriate. We also draw on, inter alia, official reports into the Irish economic and banking crisis, television programmes, books written on the crisis, academic research, think- tank reports, OECD, IMF and other extra- national reports, Central Bank reports and announcements, the annual reports of banks and property developers, and statistical data from various government and international sources (e.g. Irish Central Statistics Office (CSO), Department of Environment, OECD, European Commission etc.).

Results

Trajectory of the Irish Residential Real Estate bubble

In this section we map out the trajectory of Irish residential real estate prices from the start of the Celtic Tiger[16] in 1994 until December 2013 and attempt to map these price movements onto the stages of the Kindleberger and Aliber (2011) model. Figure 1 presents a graph of house prices, House Prices to income and House prices to rent over this period.

Figure 1 about here

We set out in Table 1 significant news items and events in the (1) Irish residential property bubble, (2) banking implosion and (3) Irish economic collapse as all three we argue are inextricably linked and we will refer to this table as we progress through our empirical sections.

Table 1 about here

[16] Kevin Gardiner a Morgan Stanley analyst was credited with coining this phrase in a report published in 1994.

As can be seen from Figure 1 between January 1994 and April 2007 the Irish residential property market was on an upward trajectory with no quarter over that period registering a price decline. Separating out the various stages in terms of clear turning points can be difficult[17]

We classify the period January 1994 to December 1999 as the *displacement* period and the period January 2000 to June 2003 as the *boom* phase. Many economic commentators commenting on the Celtic Tiger boom and bust (e.g. Brawn (2009), Donovan and Murphy 2013, O Riain, 2014, Clinch, Convery and Walsh (2002) report that in the period 1994-1999 the Irish economy was undergoing a catchup from the recession of the 1980's and was characterised by high growth, low unemployment, budgetary surpluses and a falling debt to GDP ratio on the back of success in attracting export oriented FDI and the benefits of the Europeanization of the economy culminating in Ireland's participation in the launch of the euro in January 1999.

Post this period FDI started to slow down in part driven by the Dot.Com crash in March 2000 and growth became more reliant on domestic demand. Notably in December 2001 the government introduced a number of property related incentives including stamp duty reductions and increase in the tax deductibility of interest on borrowings.[18] In addition the ECB in May 2001 started on a programme of successive interest rate reductions continuing until March 2006[19]. We classify the period January 2000 to June 2003 as the *Boom period*.

Starting in mid- 2003 the *Economist* (May) and the IMF (August) report that the Irish residential real estate market is overvalued by 42% and 20% respectively though Roche (2003) argues that the IMF and Economist ignored certain "supply factors" in their fundamental valuation models and that the true overvaluation was smaller and in the order of 5%. Given the differences in the magnitude of the potential overvaluation predicated on modelling differences we will adopt a conservative approach and use mid- 2003 as the start point of the euphoria phase whereby prices may have started to move from their underlying fundamentals.

We classify the period April 2007 to December 2010 as the *Denial phase*. March 2007 was the point where residential property prices reached their peak. At this stage (as we have argued and will show in our empirical analysis) the fate of the entire domestic banking system and the Irish economy itself was tethered to the fortunes of the property market and we shall use the date when the Irish government was forced into the IMF, European

[17] As Kindleberger and Aliber (2005) page 151 point out "Dating the onset of an asset pricing bubble is always complex because asset prices will already be increasing rapidly before the transition to the bubble period."

[18] It is noteworthy that tax incentives in relation to property development had been firmly established for many years prior to 2000 and included many property related incentives including those relating to urban renewal, rural renewal, town renewal, holiday cottages, hotels etc. Many of these earlier tax incentives were meant to be phased out at the end of 2004 but due to lobbying by the construction industry and developers their lifespans were extended. In June 2006 Brian Cowan, the Minister for Finance, signed an order to phasing out urban and rural renewal. Most reliefs would end by December 2006 but transitional arrangements would remain in place until June 2008, 5 ½ years after they were originally to be phased out!

[19] This sequence of interest rate reductions as well as the confluence of other factors may have ultimately lead to residential real estate emerging as a phantastic object. We will argue below that residential real estate is for historical reasons potentially hotwired into the Irish psyche as having a particular significance making it a likely candidate to emerge as a phantastic object.

Commission and European Central Bank in late November 2010 as the date when reality dawned.[20]

Finally we will classify the period December 2010 to December 2012 as the blame phase. The length of this final period is quite conservative (and is likely to be an underestimate) with the latter date coinciding with the period when property prices started to systematically rebound.[21]

Next we extract using *Factiva* all articles in excess of 1000 words published in the *Irish Times* during the period January 2000[22] to December 2014 that mention "real estate" or "property" or "house" or "housing" in their headline or lead paragraph. The headlines and lead paragraphs of these articles are examined by two independent researchers and then assigned to broad themes to identify significant themes and changes in these themes over time. In addition, these articles were examined as to their tone (positive or negative) [23] We report in Table 2 our results.[24]
Table 2 about here

A number of interesting patterns emerge. Those articles expressing a view (*view*) on the property market or on individual properties or property developments dominate across all phases never falling below 20% of the articles published and are almost exclusively positive in tone. Interestingly, it is only in the denial phase that the proportion of articles that are more negative in tone increases but is still exceeded by those with a positive tone. Interestingly after this period (blame phase) and subsequently the tone turns substantially positive again suggesting that blame and a positive outlook on the future for property can happily co-exist!
Articles on carrying out renovations and improvements to property (renovations) never fall below 8% of the total articles in any of the phases and are exclusively positive in tone throughout.
There is a dramatic increase in those articles extolling the virtues of the purchase of foreign properties (foreign) in moving from the Boom to the euphoria phase[25] [26] and interestingly

[20] Such was the uncertainty and panic at the time of the bailout that even Government ministers (O' Dea (Defence) and Dempsey (Environment)) were on the steps of the Parliament Building denying that the IMF were over to discuss a bailout at the same time as The Prime Minister, Minister for Finance were in active negotiations.
[21] We will argue later that the process of blame has not fully worked itself out and …
[22] We commence our article search at the "approximate" commencement date of the *boom* period.
[23] Initially a sample of 100 of these articles covering the entire period was extracted and independently assessed by each researcher and allocated to a theme. At that stage the researchers compared results and agreed on a set of broad themes (news categories) associated with these articles that could be used for the full sample. After allocating each of the articles to a theme the researchers met again and agreed on each others categorisation as well as introducing new themes where potential new themes emerged in the full sample. In the event of a disagreement (less than 1% of cases) a third researcher adjudicated. A similar process was followed in relation to the determination of the tone of the articles.
[24] There were in fact 19 themes that emerged during the analysis. In Table 2 we report only those themes that generated in excess of 7% (proxy for importance) of the total number of articles during at least one of the phases (enabling comparison across phases). A full set of the themes is available on request.
[25] E.g. Irish Investors in Leeds Buy in bulk, *Irish Times*, 12 February 2004; Investors swoop overseas as local options dry up, *Irish Times* 9 April, 2004; Irish Lead the accession goldrush, *Irish Times,* 1 May 2004; Irish people big players in Costa del Sol property boom, *Irish Times,* 16 July, 2004; Bratislava a great place to buy once you find it, *Irish Times*, 7 April 2005; Big adventure in the Balkans for Investors, *Irish Times,* 1 September 2005; Conference extolls Irish property, *Irish Times,* 30 November, 2005.
[26] In one such article: Property can you really talk the talk, 7 September, 2006 overseas purchase was even dressed up as the virtual creation of a 21st century Irish empire "*O is for overseas property- a current national*

positive mentions of foreign property acquisitions are higher in the denial phase than in the boom phase and continues to be higher through the blame phase and beyond as the virtues of foreign property investment replace domestic property investment[27]. We will argue in the subsequent empirical section that such patterns in relation to views, renovation and foreign property investment are consistent with residential real estate emerging as a phantastic object in the eyes of investors.

Those articles discussing housing affordability (affordability) never fall below 6% of the total articles in any of the phases though the tone of the articles differs across the phases. In the boom phase the tone is predominantly negative with articles arguing that prices are becoming beyond buyers reach (including articles encouraging homeowners to buy now before prices escalate further!) whereas in the euphoria phase the tone of these articles turns slightly more positive due to inter alia more favourable interest rates and longer credit terms and unlocking equity from parents' loans, availability of tax breaks and those articles on affordability that are negative during this phase argue that stamp duty should be reduced further [28] Interestingly, in the denial phase the tone of the affordability articles are also positive arguing that with price declines and ECB interest rate reductions housing is now more affordable and urging investors to get back again on the property ladder.[29]

Those articles discussing property sales prices achieved (sales) represent in excess of 16% of the articles during the boom phase reducing slightly during the euphoria phase (in effect being displaced somewhat by those articles extolling the virtues of acquiring overseas properties) and are almost exclusively positive in tone. Interestingly, in the denial phase this drops to less than 3% of articles published again with the tone of the articles being positive. This drop may potentially be consistent with the non – reporting of negative news as the prices achieved for property sales prices were dropping during this and the subsequent (blame) period. Negative news is not what newspapers want to publish (consistent with repression as a psychic defence)!

Some interesting patterns emerge in relation to banks, politicians and developers over the various phases. The politicians news category (politicians) generates in excess of 11% of the news articles in the denial phase (predominantly negative in tone) basically criticising the politicians for not making housing more affordable by cutting stamp duty etc. whereas in the blame phase the tone of the articles becomes more positive and the blame tends to shift to developers. Those articles discussing banks are almost exclusively negative in tone in both the denial phase and the blame phase.

Finally, it is only in the phase subsequent to the blame phase that experts (experts) as a news category generates articles in excess of 7% (being 11%) of the total for that phase and the

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obsession with Irish investors virtually colonising vast swathes of Eastern Europe and Spain- and even venturing into such outposts as Cape Verde, Shanghai, Barbados and Brazil".

[27] E.g. Good time to buy as French property prices fall by up to 25%, *Irish Times*, 25 September, 2008; Silver lining for survivors of eastern Europe's property storm, Irish Times, 20 November 2008; Buyers looking for value tune into Tunisia, *Irish Times*, 17 September 2009

[28] Interest only mortgages Irish Times 14 February 2003; Mortgage packages offer cheaper alternatives, Irish Times, 5 December, 2003; Home reversion schemes raise lump sums at expense of equity, *Irish Times*, 7 October, 2005; Buying for the kids is complicated, *Irish Times*, 10 October, 2005; Temples of Boom, *Irish Times*, 25 February, 2006; Failure to reform stamp duty will do lasting damage to property market, *Irish Times*, 7 December, 2006.

[29] Battle- hardened buyers bite back- and sellers get real, Irish Times, 6 December, 2007; Turmoil ahead but opportunities if ECB rates fall, *Irish Times*, 24 January, 2008;

tone of the articles is exclusively positive. These articles are presenting a positive trajectory for the future performance of property.

A couple of comments are worthy in relation to the number of articles published in each phase and the tone of these articles. The average number of articles published per quarter increased moving from the boom to the euphoria phase (22 vs 20) and dropped in both the denial and blame phases (19.8 and 12.8 per quarter respectively) . Whereas in excess of 70% of the tone of the articles in the boom and euphoria phase is positive this drops to approximately 60% in the denial and blame phases.

Interestingly, though the IMF, OECD and the Economist gave a number of warnings (Table 1) about the overheating of the residential property market over the period the Irish Times did not have a single article over 1000 words mentioning these reports and their associated warnings. In fact, there were only eight articles in total over the period published by the Irish Times mentioning these reports with seven of these articles actually questioning whether there was a bubble!

In summary we find a massive increase in the number of articles extolling the virtues of overseas property in transitioning from the boom to the euphoria phase and overseas property investment appears to act as a substitute for domestic property investment as the bubble starts to burst. The large and consistent number of articles on renovations throughout all phases as well as the proportion of articles expressing a favourable view on the property markets is at least consistent with property as a phantastic object. Even in the denial phase where the number of articles that are not expressing a favourable view on the property market increases articles on property renovations and improvements as well as those articles saying that property is now more affordable increase as do those suggesting that overseas properties are still a worthwhile investment! The oscillation of blame for the property market decline from politicians to property developers between the denial and blame phases is consistent with psychic defence as investors seek to transfer their negativity to politicians who are not doing enough to make housing more affordable by cutting stamp duty or resolving the banks inability to lend and also is consistent with the difficulty in separating the various stages of the property bubble into watertight compartments as blame can transcend phases. Indeed who is to be held to blame can change over time though banks are consistently held to account during both phases. The articles discussing improved affordability in the denial phase is also consistent with this thesis. The non- reporting of sales transactions where prices are low in the denial phase is also consistent with the psychic defence as is the decline in the average number of articles published, where such negative news is not reported.

In the next section we explore the circumstances whereby residential real estate may have emerged as a phantastic object in the eyes of investors and homeowners setting the conditions for the emergence of a euphoric (manic) state and the departure of prices from fundamentals.

Residential Real Estate as a Phantastic Object and Investor Euphoria

In this section we explore residential property and how it is viewed including its role in Irish cultural history. Is there a potential obsession with land and property in general that may override economic considerations? Is property viewed as a place to live or a status symbol, as an investment opportunity or as a speculative asset?

Tuckett and Taffler (2008) coined the term phantastic object which is derived from two psychoanalytical concepts. Object is used in the same sense as used in philosophy, as a mental representation (symbol) of something but not the thing in itself. The term phantasy refers in an imaginary sense in which the inventor of the phantasy is a protagonist in having his/her latent (unconscious) wishes fulfilled.[30] Klein (1936) views the whole of an individual's psychic life as dominated by phantasies originating in the earliest stage of emotional development: "infantile feelings and phantasies leave, as it were, imprints that do not fade away but get stored up, and exert a continuous and powerful influence on the emotional and intellectual life of the individual" (p. 290) . In such circumstances we argue that property itself and its possession is hotwired into the Irish psyche and may take on an emotional meaning as its possession may "appear to break the normal rules of life and turn aspects of 'normal' reality on its head" (Tuckett and Taffler, 2008, p 396).[31]

The Irish people's obsession with land and property ownership is pervasive in media reportage[32] One book on the Irish economic crisis by David Lynch (2010)[33], a senior writer for Bloomberg news agency "with a detachment that comes from a distance of five generations"[34] states that the economic collapse was aggravated by the Irish obsession with owning land "because of the history of dispossession and forced emigration".

This notion of property obsession is firmly rooted in Irish literature, poetry and drama (Maher and O'Brien (eds), 2014) The following excerpt from the play The Field by the playwright John B. Keane, which was turned into an Oscar nominated movie in 1992 illustrates in a discourse between the "Bull" McCabe, who is bidding to buy a field in which he has been a tenant all his life, and the local priest:

"Bull" McCabe*: There's another law, stronger than the common law.*
Father Doran*: What's that?*
"Bull" McCabe*: The law of the land. When I was a boy, younger than Tadgh there, my brothers and sisters had to leave the land, because it couldn't support them. We wasn't rich enough to be priests or doctors, so it was the emigrant ship for all of them. I were the eldest, the heir. I were the only one left at home. Neighbours were scarce. So my father and I, we had our breakfast, dinner, and tea, working in that field without a break in our work. And my mother brought us the meals. One day, one day my father sensed a drop of rain in the air and my mother helped us bring in the hay before it was too late. She was working one corner of the field, and I was working in the other. About the third day, I saw her fall back, keel over so to speak. I called my father, I run to her. My father kneeled beside her. He knew she... he*

[30] The term 'ph' rather than 'f' is used to distinguish from fantasies associated with conscious wishful thinking or daydreaming.
[31] The role of emotions in playing a role in real estate purchase decisions is not well explored in the extant real estate literature with only a small number of notable exceptions (e.g. Levy, Murphy and Lee, 2008)
[32] Psychologists urged to analyse property's lure, Irish Times, 14 November, 2014; A home at any price: why are the rest of us obsessed with buying?, *Irish Times*, June 8, 2006; Call for Ireland to end property obsession, *Irish Times*, 18 September, 2009; A species in soundbites, *Irish Times*, 17 December, 2005; Legacy of Famine still holding us back, *Irish Times*, 21 May 2013; Are the Irish different ? that's a loaded question, *Irish Times*,18 April, 2015; The landed class who blew the bubble, *Irish Times*, October, 2009; Postmortem for celtic tiger predicts that Ireland can rise again, *Irish Times*, November 13 2010.
[33] When the luck of the Irish ran out: The world's most resilient country and its struggle to rise again.
[34] Postmortum for celtic tiger that predicts that Ireland can rise again, *Irish Times*, 13 November, 2010.

knew she was dying. He said an act of contrition into her ear and he asked God to forgive her her sins. And he looked at me, and he said, "Fetch a priest." Fetch a priest... And I said, "Let's - let's bring the hay in first. Let's bring the hay in first." My father looked at me with tears of pride in his eyes. He knew I'd take care of the land. And if you think I'm gonna face my mother in Heaven or in Hell without that field, you've got something else coming. No collar, uniform, or weapon will protect the man that stands in my way.

Land and land ownership are perennial themes in Irish history (Bartley and Kritchen, 2007; Dooley, 2004; Lee, 1973)[35]

This view of property was manifest in the emotional terms that property was presented in property supplements in all the newspapers with expressions such as "living the dream", living the lifestyle", "opulent living" , "show stopper", "sheer opulence", "the spirit of gracious living" " a perfect setting, "a perfect lifestyle" abound. For example, in one such advertisement published in the Sunday Independent on 10th September 2006 advertising a large scale residential property development in South Dublin the following was the descriptor: *Select living, from Paris to Milan, to Barcelona and New York, the discerning city dweller understands the importance of contemporary living- Location, luxury, lifestyle.*

A number of articles even provided part of the lifestyle! For example, in the Sunday Business Post on 5th November, 2006 the following advertisement appeared: *Free boat with special price house. Close to Lough Allen, a select development of 20 homes offering a 17- foot Star craft with every purchase*

Such terminology was most manifest during the euphoria period but was also present during the boom period, though in the euphoria stage there was, as discussed in the previous subsection, a noticeable increase in the encouragement of overseas property ownership in addition to domestic opportunities using similar embellished descriptions.

The prices achieved for properties and the pace of their change, particularly during the euphoria period were such that even property developers did not know how to pitch the price for new developments. Sheridan and McDonald (2008) quoted one property developer on the shift in the idea of a 'phase' in relation to new property developments: Before the boom, it used to be phase 1 this year and Phase 2 the next. Now there was a day between them if that. Thus developers would set a price and then decide the price was too cheap. What happens then is that you call the next bunch of exact same houses "Phase 2", and the price is hiked maybe 15 per cent. And that could all happen in a few days or in an afternoon"

Such rapid and significant changes in real estate prices was also apparent in the auctioning of second hand properties whereby individual property purchasers got caught up in the frenzy of property purchases and that prices moved above fundamentals and that emotions played a role in decision making on real estate transactions. Figure 2 (a) and (b) provide data on two sample residential real estate auctions. Both of these houses were originally sold at auctions in 2005 and both were subsequently minimally renovated with the cost of refurbishment/ enhancement included as the "upgrades" cost in both instances in Figure 2. Both were sold again at auction within one year at substantial profits. In the case of the first property the

[35] Interestingly, Dooley (2004) recounts that the archives of the Land Commission that was established, inter alia, to oversee the distribution of land and the settlement of land disputes and boundaries in the years following Irish independence are exempt from the normal rule of making its documentation available to researchers and the public perhaps due to the sensitivity of matters relating to the land, its ownership and its role in Irish society.

profit margin was almost 120% and in the second case the corresponding profit margin was 50%. Neither of these large price increases could realistically be justified by changes in "fundamentals" during the short period between the two transactions.

Figure 2 (a) and (b) about here

It also became common practice particularly in the case of house auctions where the property was previously auctioned to compare property investment versus alternatives implying that property investment was a one way bet. For example, it was reported in April 2006 that a 5 bedroom semi at Ashton Lodge, Stepaside (outlying suburb of Dublin) sold after auction for more than €2.17m, the same house was last on the market in December 1999 for €890000 a 272% profit compared to shares in Bank of Ireland over the same period of 189%[36] In a similar a house in 8 Frascati Park, Blackrock, Dublin sold in March 2005 for €850000 and sold for in excess of €1.43m in February 2006 a return (shown in bar chart format) of 68% vs 3% for cash and 27% for the Irish share index (ISEQ) over the same 11 month period.[37] It also became common practice in newspapers to present tables of how much auctioned properties achieved over their advertised guide prices. It is also noteworthy that in many postal districts, in the Dublin market in particular sales by auction rather than by private treaty became the norm.[38] [39]

Research by Branigan (2010) using multi-criteria decision making to track in real time individuals and couples making home purchase decisions in 2005 finds that they tend to place weight on hedonic housing characteristics in screening for possible house purchase alternatives to buy but tend to be disproportionally influenced by emotional factors and being overly influenced by a property's aesthetics in making their final decision amongst alternatives unjustified by the price differentials. In addition Branigan and Ryan (2012) find in a sample of residential property auctions conducted in the period September 2004- January 2006 that "expert" property developers tend to overpay more in an auction setting relative to their "less experienced" counterparts , which they potentially attribute to overconfidence (Shiller (2007, 2008) arising from a pattern of past successes[40] and contrary to extant research on financial markets they find that women are equally prone to the winners curse in their bidding behaviour as their male counterparts. [41] It can be argued from an emotional finance perspective that past price movements may satisfy an emotional need for market prices to have already moved up for investors to have confidence to trust in and commit to "risky" investments. In such a context a sustained trajectory of price increases may indicate that real estate is already viewed by others as a good investment and may thus provide reassurance and help alleviate the anxiety associated with making a purchase decision.[42]

[36] *Irish Times*, 9 April, 2006.
[37] *Sunday Independent*, 26th February, 2006
[38] *Daft* , a property website reported in 2005 that in certain areas of Dublin, auctions had become the norm with up to 80% of properties being offered for sale via the auction mechanism.
[39] In the economics literature auctions are appropriate for the sale of assets where there is a substantial private value component e.g. paintings or other works of art (Goeree JK & Offerman T, 2002) versus those assets which have a substantial common value component, where values are driven by quantifiable characteristics and are thus capable of being valued by hedonic asset pricing models.
[40] Overconfidence is learned through past successes (Shiller, 2008). If a decision turns out to be good it is attributed to skill and ability (self- attribution bias). During a bull market investors may attribute too much of their past successes to their own abilities, contributing to their overconfidence.
[41] Barber and Odean (2000); Li, Sullivan, et al (2013)
[42] Interestingly, recent research by economists tends to suggest that past price movements play a role in the formation of bubbles but the explanations tend to be highly stylised (e.g. Glaeser and Nathanson, 2015) and tend to revolve around the "greater fool" theory.

It was even argued that part of the motivation behind overseas property investors, and by the big property developers in particular was a revenge against the British empire and an attempt to establish their own empire. This point is made by Fintan O' Toole, a lead columnist with the Irish Times:[43]

Most weirdly of all, the mania of our feudal property- developing class was fuelled by a hunger to show the English that we were all grown up and that we are as good as them anyway. Sean Dunne told us that his insanely expensive project would turn Ballsbridge into the new Knightsbridge. Irish property developers outbid Saudi sheiks for trophy English buildings such as the Savoy hotel in London and flew the tricolour from their roofs, like the Russians capturing the Reichstag.

In this latter case the developer Derek Quinlan said: I cried. My poor father, who was in the Irish army, would have loved to have seen this.[44] In a similar way Paddy Kelly, another major property developer who spoke about his great grandfather being evicted from his land in Laois, and of his belief that his ancestors had their land seized during the Plantation of Laois-Offaly and commented "*All that suffering in a sense is all part of what we are"* [45]

Interestingly these property developers themselves were also adulated as phantastic objects and there was a fascination with their social lives, lifestyle, personal relationships and their property deals in the media.[46] They even attracted sobriquets such as "Paddy the gent", "low-profile Liam", "High- flying Johnny", "King of Ballsbridge", "the Buccaneer", "the squire", "the baron", "Dunner" , "Sean, the tower", "Bernard the builder", "posh Paddy "Robo Paddy" etc.[47] [48]

One such social incident reported in the *Sunday independent*[49] serves to illustrate, providing an account on the wedding of property developer Sean Dunne to Gayle Killilea on the Jackie O, the yacht that Grace Kelly and Aristotle were married:

… It was redolent of nothing as much as the Great Gatsby… The nuptials which cost €1.5m were the best kept secret in Ireland… The guests were a fascinating sample of Irish society; bankers and footballers, designers and theatre directors, not to mention, given the groom's background, political dealmakers…He presented his wife to be with a diamond necklace which cost €300000 and earnings to match…After a champagne reception in the Splendido, the guests returned to the Cristina for dinner where Italian Michelin star chef Alphonso prepared a ten- course dinner, each one accompanied by vintage wines.

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[43] Time for a new look at the old enemy, *Irish Times* ,29 June 2010. This point was further developed in his book Ship of Fools: How Stupidity and Corruption Sunk the Celtic Tiger published in .

[44] In fact as O' Toole (2010) and McDonald and Sheridan (2008) report many of the property developers did not come from the traditional professional middle classes but rather owed their ancestry to rural backgrounds predominantly small farmers many of whose ancestors were dispossessed of their land or had suffered as a result of the Great Famine in the mid nineteenth century, *Irish Independent*, 26th November, 2004.

[45] No Room for doubt in developers' world view, *Irish Times*, 2 December, 2008.

[46] For today's property developer, the world is their stage- and they're in the centre, *Irish Independent*, 26 Nov 2004; Up, up and away Irish Independent, 31 December , 2005; Kellys heros join in €60m Tulfarris plan, *Irish Independent*, 16 February 2006; How scrum, sea and sand soothe the property pain, *Sunday Independent*, 31 May, 2009; A glittering showcase of Ireland's property and development industries

[47] E.g. Irish developers: it's a small, small world *Sunday Independent*, 15 February, 2009; With hotel chains, bars, apartments and now a ski resort under his belt, it seems no mountain is too high for developer Paddy Kelly to climb, *Irish Independent*, 16 February 2006.

[48] Squire Dunne's precarious €510m, *Sunday Independent*, 17 June, 2007

[49] Gayle Force wedding shows A-listers how to do it in style, *Sunday Independent*, 18 July 2004

Even the Irish Prime Minister was meant to attend but at the last minute, due to the publicity surrounding the event, did not attend but rang in during the wedding speeches:
Dunner, you and I go back a long way. I wish I could be there. I'm sorry I couldn't come but I would have been more trouble to you than I'd be worth.

Such was the collective euphoria and madness that credit became easily available and many ordinary people got involved in purchasing multiple properties both in Ireland and abroad as the following extract reported in McDonald and Sheridan (2010) about a circuit court repossession case in February 2009 illustrates:
.. a Dublin father of three on an Air Corps pilot's (Irish airforce) salary of around €53000 a year had managed to build up a twelve- house property portfolio, with loans of €8 million from nine separate financial institutions

Thus we argue that property and property ownership are hotwired into the Irish psyche and the potential for property to emerge as a phantastic object was lying dormant in the Irish psyche awaiting a catalyst to unlock it. As illustrated in the previous section this included the favourable interest rate reductions initiated by the ECB post the dot.com crash of early 2000 and was reinforced by existing property incentives, additional property incentives introduced in December 2001, the pattern of price increases from 1994 and other economic factors which we will refer to below in the next subsection on groupthink.[50]

We turn to this in next section where we present evidence on groupthink and how it permeated Irish society in particular post mid- 2003. We will present evidence that no section in society was exempt from its exposure as property emerged as a phantastic object meaning that there was no effective countervailing force to control the rise in property prices and the property bubble that resulted.

Groupthink

In this section we explore the consequences of the emergence of real estate and residential real estate in particular as a phantastic object. Groupthink, supported by basic assumption group thinking will be explored by reference to all the actors in Irish society. Of particular interest in the first instance is the commentary of the economics profession, to include the Central Bank, independent think tanks notably the ESRI[51], independent economists, those employed in stockbroking houses, banks, academics, and those employed as specialists in the main real estate agencies. In this context we present economic data clearly suggestive that there were clear warning signs that the banking system and the broader macroeconomy and

[50] Interestingly from a sociological perspective it has been argued (Maher and O Brien, eds 2014, page 21) that the contemporaneous revelations and scandals in the Catholic church lead to a paradigm shift in Irish society from symbolic capital to real capital "*as encapsulated in disposable income, income, cars and property portfolios"* as no civic morality replaced the role of the Church. Property may have filled the vacuum. This view was also promulgated by Inglis, 2008, p189-190; "*They (the Irish people) had moved from being quiet , poor Catholic Church mice embodying a discourse and practice of piety and humility to becoming busy, productive self- indulgent rats searching for the next stimulation".*

[51] The ESRI was founded in 1960 as an independent research institute and its mission is to produce research that contributes to understanding economic and social change and to inform public policymaking and civil society in Ireland. Its research is disseminated through publications, seminars and media contributions.

the financial sustainability of the Irish State were hitched to the property bandwagon in particular post 2002 and that the economics profession failed to adequately warn about this and the knock- on consequences for the banking sector and ultimately the sustainability of the economy.

Economic backdrop

In contrast to the pre- early 2003 period no international institutional research post that period argued that the Irish residential real estate market was rationally priced (e.g. Economist 2005; OECD 2005; OECD 2006; IMF 2006). In fact it is clear that post- early 2003 a fundamental change took place in the dynamics of the residential property market. Real estate and related activities grew geometrically constituting significant proportions of the total lending of the Irish Banking system. A number of graphs will clearly illustrate these shifts.

Figure 3 about here

Figure 4 about here

Figure 5 about here

Figure 6 about here

Figure 3 illustrates the growth trajectory of real estate and related activity vs GDP[52]. From 2004 onwards total real estate lending activity exceeds GDP and by 2007 is almost 66% greater than GDP from being 50% of GDP in 2000 and 75% of GDP in 2003. Figure 4 illustrates that by 2007 real estate lending activity constitutes in excess of 60% of the total loan portfolio of bank's balance sheets an increase of 50% from that reported in 2003. Figure 5 clears illustrates the growth in private sector Irish debt between 2000 and 2007. GDP is included for comparison purposes. Again, from the graph the steepness of the trajectory of the indices (with the notable exception of nominal GDP!) rapidly accelerated from 2003. Total bank lending increased by almost 340% over the period from 2000 whereas GDP increased by 183%. In contrast though those indices attributable to real estate and related activity increased more significantly with real estate lending going up by 816% over the period, construction by 716% and personal mortgage lending by 419%. Thus of the increase in total bank lending over the period 2000 to 2007, 73% of this increase is attributable to property- related transactions. As the ECB started its programme of successive interest rate increases in December 2005 the Irish banks responded by attempting to "lean against the wind" by reducing the margins on their property related loans relative to those prevailing in the 2002-2004 pereiod. (Figure 6). Interestingly, much of the increase in bank lending was not financed via domestic deposits but rather by borrowing on international wholesale markets. Lane (2011) showed that while in 2003 20% of Irish banks net liabilities were owed to international lenders this rose to almost 80% in 2008.[53] In addition credit conditions after 2003 were relaxed significantly by the banks. Over the period 2004-2007 new mortgage originations greater than 30 years duration increased from 10% of total mortgages in 2004 to 35% in 2007, peaking at 39% in 2008 whilst 100% loan-to-value mortgages increased from

[52] Comparisons to GDP are more relevant than comparisons to GNP in an Irish context due to the open nature of the economy.

[53] To put this in context Honohan (2009) reported that the net foreign borrowing of the Irish banks at the start of 2004 stood at 10% of GDP and was stable at that level for the previous decade. By 2006 it was 40% of GDP and in 2008 was 60%.

5% of total new mortgages in 2004 to 15% in 2006, decreasing slightly in 2007 (as prices started to go down) to 12% of new mortgages.[54]

Given the rapid growth in banking lending and its progressive concentration in real estate related activities, in particular post 2003 this lack of lending portfolio diversification together with an explosive growth in lending activity itself largely driven by real estate lending activities made the banking sector considerably exposed to a negative shock to real estate prices.

As a consequence of the growth rates in real estate lending activity the proportion of government revenue directly attributable to real estate and related activity increased rapidly over the period too.

Figure 7 about here

Figure 7 illustrates that the property related tax constituted 8% of the total tax take in 2002 rising by 50% to 12% in 2003 and rising a further 50% to peak at 18% in 2005 and 2006 before dropping to 13% in 2007 as real estate prices began to fall.[55] Other data support the thesis that housing and construction in general came to become significant proportions of the macroeconomy versus the proportions expected in a normal developed economy. Kelly (2007) reports that in an economy at a similar stage of development to Ireland construction would constitute approximately 5% of GDP whereas the comparative percentage for the Irish economy by 2007 was 20%.

Thus it is clear from the data that when the property bubble burst in the second quarter of 2007 its consequences would have ramifications across the entire banking sector and given the rapid growth in property related lending and associated tax receipts there would be implications from a government revenue perspective.

Figure 8 about here

Figure 8 tracks the share price performance of the index of Irish financial shares over the period 2000-2007. Interestingly over the period from 2000 to the peak of the property market in April 2007 financial shares went up 163% whereas the index of all other shares went up only 54% over the same period! In normal circumstances over such a long period it would be expected that banks share price performance would mirror the performance of the underlying economy.

Central Bank, ESRI and Department of Finance

Central Bank

The primary publications produced by the Central Bank are its *Quarterly Bulletins*. In addition the Central Bank has published an annual *Financial Stability Report* providing an

[54] Department of Environment Annual Housing Statistics, various years

[55] This property- related tax intake enabled governments to reduce the income tax burden. By 2007 the average income tax rate for a single earning married couple with two children receiving the average wage as 6.7%, compared with an EU average of 23.7% and OECD of 21.1%.

update on developments in the economic and financial environment with particular focus on the key risks. The Quarterly Bulletins of 2003, 2004, 2005 only refer to property in terms of credit growth being driven by property based lending. It was only in Spring 2006 it was first noted a potential slowdown in property related lending posed a "*risk to the stability of the public finances"* (Spring 2006, p. 4) but that there was still evidence of "*robust*" capital and rental returns. In Summer 2006 this was reiterated but noted that the high property based lending "*increased the economy's high dependence on the health of the broad property sector to an extent that constitutes a significant risk*" (p.6). This was the first mention of a significant risk. However, at the same time the Report noted (p.47) that " *the underlying demand for residential property remained strong and, as a result house price increases are expected to remain quite high*" The remaining reports in 2006 only referred to property lending growth being "robust" and significantly dominating other lending activities. From April 2007 property prices started to decline and the Bank commented in its Summer 2007 Bulletin that the "…*Bank is forecasting a further moderation in building and construction*" (p 17). In Winter 2007 it noted that "*prices this year have moved to a more sustainable position*" (p. 4) attributing the decline to "impact of interest rate increases in 2006 and 2007"… "*high level of house prices on affordability and demand*" and "*uncertainty in the market due to possible changes in stamp duty and mortgage interest relief*" (p. 42) with the Spring 2008 Report noting that the downward movements in property prices were a "*necessary adjustment in the market*" . It was only in Summer 2008 over a year after prices started to secularly decline that it was noted that "*much of the increase in house prices during 2006 and early 2007 did not appear to be supported by fundamentals*" (p. 39). The Winter 2008 Bulletin (p. 41) noted that *" the decline in house prices has gone a long way to reduce the overvaluation evident from around 2006 and the fall in the output of housing units this year represents a necessary adjustment to a more sustained level of output and would be consistent with more stability in the market*". The commentary in these reports in effect argued that there was nothing really to worry about and did not mention at all the potential banking sector and economywide spillovers.

The commentary in the various *Financial Stability Reports* (FSR), which were intended to exclusively focus on risks, followed a similar pattern. The 2004 FSR identifies residential property exposure as "…*the risk that poses the greatest threat to the banking system. Nevertheless the shock absorption capacity of the banking system is currently adequate..* "[56] (p12) and in the FSR 2005 reports that the risk has abated as " *a moderation in house price growth in the meantime suggests that while the risk of a sudden fall in prices cannot be dismissed this risk may have receded somewhat"* (p.7). In 2006 it was reported that in the event of a price decline " *a soft landing is the most likely outcome*" (p. 6) and this view was reiterated in 2007 where "*The underlying fundamentals of the residential property market continue to appear strong. The 'central' scenario is therefore, for a soft, rather than a hard landing*" (p.12), and interestingly noting on p. 29 that "*house prices appear to have become more responsive to fundamental factors*". It is noteworthy that in the 2006 Financial Stability Report (p. 34) a number of fundamental models are evaluated to assess overvaluation with all of these models, save one, indicating that property prices are overvalued by 14% to 72%. However, the Report comments that those models indicating an overvaluation "treat housing purely as an investment product". In the case of the one "exception" model, using a "broader approach" itself subject of a dedicated technical paper in part 3 of the FSR, it is argued that " *these variables (income levels and interest rates) can broadly explain developments in*

[56] The strength of the banking system is reiterated in the 2005 and 2006 Financial Stability Reports.

house prices over the period 1980 to 2005" (p 35). However, a close look at chart 2 of that paper clearly shows that actual prices lie above fundamentals for the entire post-2000 period! Similarly in the 2007 FSR (p. 30) OECD and IMF models are criticised as these studies tend to be "*univariate and do not account for fundamentals*" and "*the distribution of house price declines (in their models) indicates that the majority occurred in the different economic period prior to the 1990s*." This is in effect the argument that this time it's different!

In this context it is interesting to note that the Central Bank had at its disposal tools to require the banks to make changes to their lending activities, such as imposition of sectoral limits on lending but did not act. As Honohan (2009) pointed out the only meaningful intervention was to slightly tighten capital requirements surrounding 100% mortgages by increasing capital from 4% to 4.8%. In addition he reports that the stress tests performed on the banks loan losses were based on very low thresholds for price declines.

At no time through any of these reports question the solvency of the banking system arising from its real estate exposure. The following commentary by Patrick Neary, former chief executive of the Financial Regulator, who was responsible for monitoring the banking system illustrate:

"Ireland's banks are solvent and will be able to offset potential losses on property loans with their better performing loans" (*Irish Times*, 14 October 2008). This statement was made shortly after the Bank blanket guarantee in September 2008.

On *Prime Time* on 3 October 2010, just one month prior to the Bailout, Neary said that bad lending practices had little or nothing to do with the banking crisis and that even after the property crash, Irish banks had plenty of capital.[57]

ESRI

A similar narrative to those reports published by the Central Bank occurs in the *Quarterly Economic Commentary* and technical articles published by the ESRI over the period 2003 to 2014. A search on variations of the terms "Property bubble" or "property crash" on the ESRI website generated only four articles over the period. Of these articles two were written in the period 2003 to 2008. [58] One was written in in 2003 (Roche, 2003) and we referred to this above where the article criticised the OECD and IMF measures of overvaluation. The other article (Kelly, 2007) was published as an addendum to the Summer 2007 *Quarterly Economic Commentary* which argued that house prices could fall by in excess of 50%. However, the press release accompanying the release of the *Commentary* (3 July, 2007) stated that "*Members of the media should note that Professor Morgan Kelly is not a staff member of the ESRI. Whilst this article has been accepted for publication by the ESRI, the views expressed are not the views of the ESRI."* [59] In fact the ESRI in that *Commentary* expressed the view

[57] Regulator could calm storm by publishing banking data, *Irish Independent* 4, October, 2008

[58] The other two articles were published in 2010 and 2014: Managing Housing Bubbles in Regional Economies Under EMU: Ireland and Spain, *ESRI Research Bulletin* 2010/2/1 Conefrey, T & Fitzgerald J ; Bubble, Bubble Toil, and Trouble? An Assessment of the Current State of the Irish Housing Market, Special article in *Quarterly Economic Commentary*, Summer 2014.

[59] Much media commentary at the time criticised the ESRI for publishing Kelly's article. E.g." *There is, of course, nervousness about a property collapse and there is always a danger that it will become self- fulfilling, Confidence has been battered and it is unfortunate that when sentiment is weak the ESRI should opt for melodrama over cool- headedness*" Sunday Independent 8 July, 2007; "… *the economists and fellow*

that property prices were overvalued by 3% implying a soft landing for the Irish housing market! In fact, the view that there would be no adverse impact on the economy continued right through 2008 and is reflective in the ESRI *Medium Term Review: 2008-2015* (14 May 2008):

While our understanding of the key factors driving the economy has evolved over recent years, our view is its likely medium term growth rate has not. The forecast for the growth rate in GNP over the period 2007-2015 is identical to what it was when we published the last Review in December 2005, an average of around 3¾ % a year. (Fitzgerald et al, 2008, p. vii).

Department of Finance

One other group with economic expertise were the Department of Finance, one of whose jobs is to advise the Minister of Finance on budgetary matters. The Wright Report[60] stated that potential warnings had been given about the potential dangers in the public finances but that "*these are not part of the official record*" It was reported in the Irish Times by one journalist who spoke to members of the government one of who questioned this conclusion of the Wright Report: "*What warning? Given by who, when?*"[61]

Interestingly there are even cases of the Department of Finance pointing out that other economists had not suggested that there were problems and even that forecasting itself was a hazardous activity! "*It said that "bank and stockbroker economists repeatedly concluded that residential investment in Ireland was sustainable and prices were justified by fundamentals*" and, in addition, that ""*forecasting was a hazardous activity*"[62]

In summary therefore, none of the commentary from the Central Bank, ESRI and Department of Finance in the euphoria period warned sufficiently about the dangers of an overheating property market. Where they did mention risks they were usually sugercoated by reference to sound fundamentals. When the property market started to decline the commentary was that the fundamentals were sound and that at worst there would be a "soft landing". None of the commentary pointed out the potential severe consequences for the banking sector and the wider economy, though the Central Bank did routinely report on the growing proportion of bank lending being driven by real estate related activity.

Other Economists and the Period surrounding the After Shock Programme

As the residential property market peaked and commenced its first quarterly period of price declines starting in early April 2007, the Irish State television station, RTÉ, broadcasted a programme *Future Shock: Property Crash* which questioned the Irish property market's vulnerability to a shock. Interestingly, it was in this programme and a follow- on current affairs programme programme that took place the following evening that there was the first specific mention in a public forum about the possibility of a *hard landing* in the property market and its implications. [63]

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travellers in the media who want to talk Ireland out of its boom because it does not suit a mythical semi-socialist future where we would all be equally poor together", and that "*Do Professor Kelly and his doom-laden cohorts ever stop to think that they themselves are perpetuating a self-fulfilling expectation that prices will fall*? Sunday Independent, 8 July, 2007.

[60] The Wright Report was commissioned by the Minister for Finance in September 2010 to investigate and report on the Department of Finance over the period 2000-2010. It reported in December 2010.

[61] Wright Report is wrong- department of finance failed to warn cabinet of bubble, *Irish Times*, 3 March, 2011.

[62] Department staunchly defends its economic advice, Irish Times, 24 June, 2010.

[63] *Prime Time*, 17 April , 2007

The period surrounding the lead up to the peak of the market and these two programmes are potentially good vantage points to examine the commentary of members of the economics profession, including those employed in banking institutions, stockbrokers, real estate agencies and independent economists.[64] On these programmes a number of bank economists spoke about the "*strong fundamental factors in the Irish economy*" , "soft landing", a deceleration of house price increases "*improving affordability*", "*dramatic transformation of the Irish economy*" in recent years, the price declines being "*a once- off step adjustment*" "*Irish economy utterly transformed in recent years*", "*fundamentals of Ireland are pretty unique*", "*strong natural demand* " for property and the market was not going to go down but would remain "*stagnant*." and even one quoted former British premier Margaret Thatcher "*No prouder word in our history than freeholder*" [65] There was even one comment on 2006 having the "*highest employment in the history of the (Irish) State"* until it was pointed out by John Fitzgerald from the ESRI that 25% of that employment was property and related activities being in excess of twice the comparative proportions in economies in a similar stage of development![66]

It was during these programmes that the only two independent academic economists that would consistently speak out about a property bubble appeared: Morgan Kelly and Alan Ahearne. [67] However, it is noteworthy that Kelly's first pronouncement on the possibility of a property crash was in December, 2006 just three months before the property market peaked in March 2007 and Ahearne's, which were to appear as a regular series of weekly columns started on 1st July, 2007 three months after the secular price declines had commenced! [68]
These two economists attracted considerable negative commentary in the media at the time, either treated as wrong or criticised for their smugness! This negativity continued from April 2007 right up to and beyond the bank blanket guarantee of 2008 and up to the bailout of the Irish economy in November, 2010.
"*Morgan, it seems likes to have us all fasting. You see, Morgan sees toxins everywhere. Toxic builders, toxic debts, toxic banks. Sometimes he favours the Japanese cure- I mean model (property to drop by 70 per cent, as brutal as eating raw fish), sometimes the Swedish (property down by 50% and potted herrings for breakfast), But one way or another its short rations with Morgan"* [69]

"*Kelly is the thinking man's economic clairvoyant. Morgan likes his disasters in big round numbers. He opened 2008 with a concession that his October 2007 prediction of a 50% fall in house prices was wildly optimistic. His 2009 New Year's message of hope was that we were looking at an 80 per cent drop from peak to trough. It is clear that Morgan understands*

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[64] Even the ESRI joined in condemning the programme David Duffy said" We are not on course for a property crash, unless we choose to manufacture one with irresponsible comment on the state of the market". *Irish Times*, 11 May, 2007
[65] Participants included Pat McArdle (chief economist Ulster Bank), Rossa White (chief economist Davy stockbrokers), Jim Power (Friends First)
[66] This was likened by one contributor to "*building castles in the air*"
[67] Both of these economists argued in these programmes in April 2007, based on their own studies of prior property crashes, that the size of the initial property boom was a strong predictor of the size and duration of the subsequent bust with Kelly predicting declines of in excess of 60%.
[68] How the housing corner stones of our economy could go into a rapid freefall, Irish Times, 28 December, 2006; Time to get out of rental property, *Sunday Independent*, 1 July 2007
[69] Let's get rid of the dismal divas, *Sunday Independent*, 5 October 2008.

that there isn't much media value in the headline 'academic stills thinks the same' so he is willing to go for broke with new levels of misery in order to stay on our radar.[70]

"*The UCG (Ahearne) economist is usually introduced as an expert in the housing market, one who spent seven years briefing Alan Greenspan in the US Federal Reserve before returning home to brief us on our bubble. And yes, that is the same Alan Greenspan who recently admitted that he made a massive mistake in his handling of the US housing bubble…. You may wonder why a supposed economic heavyweight moved from the Federal Reserve to UCG- maybe he likes the sea air."*[71]

Even when the economic situation started to improve and the S&P called the "bottom" of the property market a pole by the Sunday Independent asked whether they thought it was right with 53% saying no and 47% yes and also asking should the Government come up with some initiative that would get movement back into the property market with 76% for and 24% against:

"*Yet as we clutch Morgan Kelly to our bosom, a strange irony is occurring- for rather like the dry alcoholic who joins the local temperance movement, such is the level of our post-colonial desire to appease and atone for our past optimism a new herd mentality has arisen. Like the famous Bourbons, who forgot and learned nothing, we now believe with the same manic, illogical, passionate, thoughtless intensity that characterised the bubble era, that it will never be worth our while to buy a house again*.[72]

In a similar manner economists employed by banks, stockbroking houses, and estate agents tended to be either positive on the property market during the euphoria phase or be silent in the media and simultaneously defensive and in denial as the property market slowed in 2006 and went into declines from early 2007.

Bank economists

In 2006 as the rate of acceleration in house prices started to decline all the bank economists started to talk about a "*soft landing"* usually with accompanying commentary about the sound economic fundamentals underpinning the economy.

David Begg, chief economist in AIB said the *"so called soft landing" for the market, in which house price growth would calm to about 2-3 per cent per annum, won't happen until at least 2008". … "The market is going to remain red hot for the moment*"[73] and in October, 2006 reported that *"looking ahead, more moderate growth in house prices of 3 to 5 per cent is possible over the next few years*".[74]At around the same time Dan McLoughlin, chief economist at Bank of Ireland was predicting a 13 per cent increase in prices despite the "*record levels of supply and the prospect of higher interest rates*"[75] Even interest rate increases themselves were downplayed and talking in February 2007, Begg stated that even a rise in ECB interest rates to 4 percent is in terms of real rates " *probably close to a neutral*

[70] The economists- these are the guys who predicted the bust. Thanks, but must they be so pleased with themselves, *Irish Independent*, 1 February 2009.

[71] The economists- these are the guys who predicted the bust. Thanks, but must they be so pleased with themselves, *Irish Independent*, 1 February 2009.

[72] A property revival threatens our attention seeking dismal scientists: Is it time to abandon the new herd mentality and learn to love the housing game again? Sunday Independent, 8 May 2011.

[73] Prices hot first-time buyers' bid for homes says AIB, *Irish Times*, 12 April, 2006.

[74] AIB says house- price inflation to ease as growth ebbs. *Irish Times*, 24 October 2006

[75] Government reassurance belies tricky house market. *Irish Times, 14 April, 2006*

stance and broadly consistent with an economy growing close to potential" [76] In 2006 Pat McArdle, chief economist in Ulster Bank, was referring to " *still buoyant construction*" [77] and "*it looks like the construction industry is on target to deliver another record level of house completions this year"* [78] A similar pattern prevailed across other bank economists , such as Austin Hughes, chief economist at IIB Bank. On 25 January 2006 Hughes argued that the "*Ryanair effect*" would have a positive impact on house prices noting that *"a Ryanair effect on property prices has been noted in certain parts of France and Italy, following the introduction of low cost flights*". Additionally, he argues that - When prices started to go down that "*Rising demand was supported by a buildup in housing wealth*[79] He even argued that when interest rates went up the cost of borrowing would still be low because of inflation, notably house price inflation.[80] Even at the peak of the bubble Hughes was arguing against that taking action to cool house price growth and that "*the acceleration in house prices reflected strong demand and improved borrowing power rather than speculation by investors*"[81]. He argued that though household debt was up housing was also up: "*Commentators often failed to look at the "other side of the balance sheet" or the €500bn worth of housing assets on which most consumer debt is secured*[82]

When prices started to decline these same economists went into denial. In April, 2007 Begg stated after the *After Shock* programme that in terms of the slowdown in property construction "*We are looking for a slowdown in the pace of economic growth from its very robust pace in 2006 and not a slump in activity*" [83] Even in November 2007 when the Construction Industry Federation (CIF) reported based on a survey of its members that new house construction would drop significantly Begg said this would in effect slump economic growth to "*zero*" and said he was "*dubious*" about the CIF's housing forecast. [84] McArdle, in May 2007 said, the decline in building activity in the month of April was directly attributable to the *Future Shock* programme and noted that "*I wouldn't be surprised if the index improved next month because there is no reason for commercial activity to go down*"[85] [86] In an article in December 2007 McArdle argued reducing stamp duty would " *take away some of the nerves*" in the property market[87]

Even in 2008 the economists were upbeat with McArdle indicating that in terms of house prices he expected " *a levelling off in the second half of this year*[88] When prices started to decline Hughes argued that stamp duty and mortgage interest relief need to be reformed to kickstart the housing market "*… increasing mortgage interest relief for all borrowers and reforming the stamp duty system could help kickstart the housing market and have long term benefits for the stability of the economy."* On 14 February 2008 Hughes argued that the

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[76] ECB chief signals imminent rate rise, *Irish Times*, 9 Feb 2007
[77] Construction still buoyant, *Irish Times,* 9 Oct 2006.
[78] Construction activity up in July, 14 August 2006
[79] Ryanair effect adds to confidence in housing market, *Irish Times*, 25 January, 2006.
[80] Outlook gloomy for homeowners as rises continue, *Irish Times*, 4 August 2006.
[81] IIB warns against plans to cool house prices, *Irish Times*, 5" September 2006
[82] Debt fear as interest rates rise, *Irish Times,* 27 June 2006.
[83] Bank warns of slowdown in economic growth, *Irish Times,* 27 April, 2007.
[84] Housing slump could lead to zero growth, *Irish Times*, 17 November, 2007
[85] Growth in building industry falls, *Irish Times*, 14 May 2007
[86] State action urged over housing market, *Irish Times,* 11 September, 2007
[87] Cowan urged to reduce top rate of stamp duty, *Irish Times,* 4 December, 2007.
[88] Weakest economic growth since 1986 expected, *Irish Times*, 2 May 2008.

house price declines were attributable to the world economy, interest rates between December 2005 and June 2007, and a delay in reducing stamp duty [89]

Real estate agent economists

CBRE, labelling the makers of the *After Shock* programme as "*doom merchants*" and pointing out that whilst demand is "*easing*" houses are still selling, noting that a "*house price crash is not imminent- just because it happened elsewhere does not mean it will happen here* (Marie Hunt of CBRE)[90] Prior to this in Nov 2006 Hunt was arguing " *Irish investors have a natural affinity with property*"[91] and that interest rate increases would be affordable due to the banks "*stress tests*" [92] and when prices went down that other sections of the property market would replace the void by reduced residential housing activity[93]. A similar thematic came from other real estate agents e.g. Lisney who argued that sound fundamentals meant construction would continue on an upward trajectory[94] reforming stamp duty would stop the declines in house prices and even if not there are possibilities for switching housebuilding towards refurbishment or extensions[95], urged swapping to infrastructure development to fill the housing market void[96] or that the slack could be taken up by commercial activity[97]

It was reported in the *Irish Independent* in August 2007 that the Irish Auctioneers and Valuers' Institute (IAVI) made a formal complaint to the Broadcasting Complaints Commission (BCC) that the *After Shock* programme had not been impartial and had a detrimental impact on the property market but the Commission had rejected the claim on the basis that "*there was a public interest in examining a worst case scenario and that the programme never stated that a price crash was inevitable"*[98]

Brawn (2009), a former Head of Research at Savills HOK took a contrarian view to the zeitgeist among the other estate agent economists

"*They blame rising rates; in fact rates went from ridiculously low to just very low and are still (2009) well below trend rates. They also blamed poor sentiment caused by confusion over stamp duty. If this was so, why did first-time buyers stop buying new homes completely, without having to pay any stamp duty at all*" (p. 201). Brawn goes on to argue "*The twin causes of the Irish property correction were oversupply and excessive valuations".* He follows on to say "*The latter destroyed affordability, as prices simply went up too much too quickly".* (p 200).

Stockbroker economists

Similar optimism during the boom and denial was expressed by economists employed in the leading stockbroking houses. At the time of the Future Shock programme Rossa White, of Davy stockbrokers said that he believed house prices would continue to fall for about three

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89 Maturing market to get back to normality, *Irish Times*, 14 February, 2008
90 Dismal science merchants only happy when we're poor, *Sunday Independent*, 8 July 2007.
91 Stamp duty uncertainty tops concerns at surveyors' conference, Irish Times, 8 Nov 2006
92 Outlook gloomy for homeowners as rises continue, *Irish Times*, 4 August, 2006
93 Report says investor activity to increase in second half of the year, *Irish Times*, 9 January 2008
94 We're mossing the facts among all the figures, *Irish Times*, 5 April, 2007
95 The year that builders became available- at last, *Irish Times*, 6 December 2007
96 Now is the time to ramp up spending on infrastructure, *Irish Times*, 24 August 2007
97 Report says investor activity to increase in second half of the year, *Irish Times*, 9 January 2008
98 RTE programme on property crash likelihood 'was not biased' *Irish Independent*, 11 August 2007

months and then "*prices will still end the year higher than they started it*" whilst NCB chief economist Eunan King argued as comparisons were made by commentators between the Irish and Spanish markets "*where Spain's market is over-reliant on fickle holiday makers, Ireland is backed by steady and strong growth in population*[99]

In May 2008 NCB was dismissing the "*bearish arguments*" that the Irish economy was in trouble saying that "*the housing slowdown in 2007 did not weaken the overall economy substantially" and predicted growth rates of 5% and 6% in 2008 and 2009*". [100] There was similar commentary in terms of tone from the other stockbroking houses over the same period, arguing against IMF reports, talking about soft landings in the property market, turning the downtown into a virtue in terms of better affordability and buying opportunities at these more affordable prices, arguing that downturn in residential would be compensated by other sectors such as refurbishment or substitution into commercial activity etc [101] Interestingly in an article published in April 2009 Eunan King is quoted from a report by NCB in mid- 2008 arguing "*The gloom about the Irish economy by the downturn in the housing market is misplaced… the conditions for a spiral down and a recession in the economy are not present. House building was not the engine of the boom and should not be the cause of a bust*"

Construction sector

Looking at the construction sector the press releases from the major quoted companies identify almost no risks until after 2008. McInerney, a major residential builder suggested in 2005 that "*strong market demand for Irish housing shows no sign of diminishing. It is expected that this demand will continue, boosted by employment, demographics and inward migration* (McInerney Holdings plc, 2007). Treasury Holdings reported from its 2007 annual conference that "*the sun is not ready to set on Ireland's rapidly growing property empire* (2007). While there was some recognition of slowing growth in late 2007 and 2008 these risks were discounted based on "*a strong indigenous economy*" , "*ongoing strength in the non-residential construction market* (Kingspan plc, 2008) and "*a resilient income producing portfolio and its well- timed long- term development pipeline*" (Treasury Holdings, 2008).

Banks

In a similar fashion banks reports commented on strong market fundamentals leading up to the property price decline and were in denial as prices continued to spiral downwards. The following extracts from a selection of annual reports illustrate:

[99] Falling house prices, a return to reality, *Irish Times*, 28 April 2007.

[100] The game is up for stockbroker economists, *Irish Times*, 7 April 2009

[101] Department staunchly defends its economic advice, *Irish Times*, 24 June, 2010; What's on the horizon, *Irish Times*, 27 July, 2007; Davy disputes IMF claims, *Irish Times*, 27 September, 2004; Davy raises economic forecast, *Irish Times*, 7 April, 2006; In housebuilding terms, that was the peak that was, *Irish Times*, 29 December 2006; Government boost to construction, *Irish Times*, 15 May 2006; Davy predicts growth will slow to 2.1%, *Irish Times*, 4 January, 2008;

"*The set of circumstances that could result in a sudden sharp correction to the market are not in place and it is unlikely that they would come into place for the forecastable future* (Friends First, annual report 2006)

"While short-term economic prospects for AIB's main markets are somewhat mixed, the medium outlook is more positive. Irish GDP is forecast to slow to 2.5% this year, reflecting the slowdown in the housing sector and a weaker global economy. However, economic fundamentals remain solid and growth is expected to pick up again in 2009 and beyond" (AIB annual report, 2007)

"Economic fundamentals remain firm- demographics, job creation, income growth and the government's fiscal position all remain positive while the interest rate environment is now more supportive. These fundamentals support ongoing demand for housing" (Anglo Irish Annual report, 2007)

"*The banks performance in 2008 demonstrates the resilience and strength of our business model. "The bank has no exposure to US or other sub- prime sectors and does not sponsor any off-balance sheet activities*" (Anglo Irish Bank, Interim Report, September 2008)

The commentary in the Anglo Irish Reports and senior management commentary is particularly instructive as this was the bank that had originally lead the way in terms of its exposure to property developers (e.g. Lawrence, Pazzaglia and Sonpar, 2011) and was the first Bank to be nationalised in January 2009. As noted by Ross (2009, page 59) "*Anglo was brazen about its worship of the new deity of property. The annual reports, while coy about using the 'property' word, were shameless. Flashy pictures of some of the projects the bank supported took garish pride of place in the reports, which began to look more like auctioneers' brochures than bankers tomes.*" He also noted that concurrently with these comments Anglo's share price was down by 50% in 2007 at the same time as they were reporting recorded profits and that the results were "*defying gravity*".

The strategy pursued by Anglo Irish Bank in relation to concentration on real estate related activity lead other banks to follow suit, in particular in the period post 2003, as the following quote from one AIB director illustrates!
"*Of course we saw what Anglo was doing. It was all everyone else was talking about. The mood was, if that little s***-box of a bank can do that, then why can't we*[102]

As the property market began to unravel senior executives at Anglo Irish Bank continued to deny there was a problem blaming international markets, bad luck and even criticising the Regulator's "principles- based" approach to regulation. The following quotes from the autobiography of the CEO of Anglo Irish Bank, Sean Fitzpatrick, illustrate:
"A*mong the more insidious aspects of the current regulatory environment is its apparent presumption of guilt on the part of entrepreneurs and business people generally…. "The whole structure seems to be geared towards something akin to an annual proof of innocence statement. This is corporate 'McCarthyism' and we shouldn't tolerate it"* [103]

[102] Night that brought us to our knees: The true impact of the decisions made to save the banks is only now becoming evident, *Sunday Independent*, 11 April, 2010.
[103] Regulation is 'strangling the wealth and creative flair of business' says banker, *Irish Independent*, 22 June 2007.

"*We were all in this together*.*"… "I never thought he* (Neary- the Financial Regulator) *was over endowed with grey matter"…*"*It was not about the money- it was about the thrill of the deal*"…"*We (bankers) were admired for making money and doing it well. People on the board loved the culture within the bank, they would get presentations and go* 'Jesus Christ'"[104]

"*It would be very easy for me to say sorry* (for the banking crisis). *The cause of our problems was global so I can't say sorry with any degree of sincerity or decency, but I do say "thank you* (for the Bank guarantee)*". (Saturday 4 October 2008,* Marian Finucane Show, RTÉ)

Willie Mc Ateer, former executive director of Anglo Irish Bank at the Oireachtas (Government) Finance Committee, 2 July 2008 made the following comments:

"We are often wrong but we have a strong belief that we have significant and sufficient capital to meet even worse scenarios than we envisage. If bad debts and the economy get worse, we believe we are sufficiently capitalised… I reject the suggestion that banks have been foolhardy in recklessly lending and driving up values. We are in competition right across the board and I cannot think of a bank that has been reckless. Every loan goes through a central credit committee and is properly underwritten. "

In a similar fashion the senior management of the other banks also were in denial. Eugene Sheehy, the CEO of AIB blamed liquidity
"*…markets worldwide are experiencing severe tightening in the availability and duration of unsecured liquidity and term funding. If these conditions continues, AIBs access to traditional sources of liquidity will be further constrained*"[105]

He declared in mid- October 2008, at an investment conference he declared" *We'd rather die than raise equity*"[106] which was barely three weeks after the Lehmans collapse and the bank guarantee. He also saw himself as "*an experienced banker who wants to work through this cycle*[107] The head of AIB Irish market Donal Forde declared in November 2007 "*There's a nervousness about buying property at the moment. But we're still getting plenty of inquiries*".[108] It was noteworthy that in July 2007 AIB increased its dividends by 10% whilst at the same time reporting that 60% of its loans were to property developers.

Politicians

There were two general elections during the euphoria period being the 2002 and 2007 general elections. Key word searches of newspaper articles on property and property related matters during these elections revealed no instances of politicians questioning the buoyancy of the property market other than to raise questions on housing affordability, and putting forward tax measures such as stamp duty reform and mortgage interest relief to address these concerns.

[104] 'Victim' Fitzpatrick's book is just self-indulgent claptrap, *Irish Independent,* 10 January 2011.
[105] Plunging profits hit AIB chief I pocket as pay slumps 45 per cent, *Irish independent*, 20 March, 2009.
[106] Irish Independent 29 Nov 2008
[107] Sheehy to keep job as bank writes off 2,9bn., *Irish Independent*, 3 March, 2009
[108] Record year for AIB on home front, says Forde, *Irish Independent*, 8 November 2007.

The Irish Prime Minister (Bertie Ahern) said in 2006: *The boom times are getting even more boomer (Irish Times, 14 July 2006)*

Bertie Ahern was highly critical of RTE for broadcasting its *Future Shock: Property Crash* programme saying that it was irresponsible and inaccurate and that he "*disagreed with almost everything in it*"[109] In an interview on 29 April, 2007 he said that even back in 2006 when there was talk of a "soft landing" he expressed his displeasure at those who predicted a downturn in the market noting that those who avoid buying property on the basis of "*their glass half empty*" gloom would now face higher prices[110] In an interview in July 2007 he commented that people should not allow themselves be convinced by "*merchants of doom*" that the Irish economy was in trouble and that the good times were over, appealing to peoples "*practical patriotism*". He further noted: *"Sitting on the sidelines, cribbing and moaning is a lost opportunity. I don't know how people who engage in that don't commit suicide because frankly the only thing that motivates me is being able to actively change something." (reported on RTE News, 4 July 2007)*

Politicians also came out to robustly defend the property market post April 2007 and offer the "solution" of stamp duty reform and further mortgage interest relief.[111] In fact the whole issue of stamp duty reform (reduction) became a major general election issue in Summer 2007 with each party promising to reduce stamp duty to bolster the housing market.[112]

The Minister for Finance in a Seanad Eireann speech on 14th May, 2008 said:
"However, what we do know is that the underlying demand for housing remains strong, driven by a relatively young population and continued inward migration. While we may experience a year or two of sub-50,000 completions, it is reasonable to expect over the medium term that annual completions will return to sustainable levels which will remain high by international standards, reflecting the strong underlying demand for housing in Ireland"

He went on to say: *However, one aspect of the change in the housing market, which is being overlooked by commentators, is that the moderation in house price levels, when combined with measures on stamp duty and mortgage interest relief, taken by the Government at budget time, means that better value is being obtained for those wishing to buy their own home, particularly amongst the first-time buyer group."*

The day after the introduction of the Bank Guarantee in September 2008, (which was precipitated by the Lehman Brothers collapse) the Minister for Finance stated in the Irish parliament "*There is understandable concern that the Exchequer is potentially significantly exposed by this measure. I want to reassure the Irish people that this is not the case. The risk of any potential financial exposure is significantly mitigated by a very substantial buffer made up of the equity and other risk capital."* and said that the guarantee had been introduced because of "*unprecedented disruption in international financial markets"*

[109] Ahern expects immigrant influx to decline, *Irish Times*, 24 April 2007
[110] Government reassurance belies tricky house market. *Irish Times, 14 April, 2006*
[111] House tax u- turn is defended, *Irish Independent*, 4 May, 2007
[112] Labour and FG promise radical changes to stamp duty, *Irish Times*, 20 April 2007; Growth projection may not be realistic, *Irish Tim*es, 20 April 2007.

Two weeks before the guarantee Lenihan said "*I want it to be known that the Government is confident about the strength and resilience of the Irish financial system*[113]

Discussion

The ramifications associated with the bursting of the Irish residential property bubble are still unfolding and, we argue, will continue to unfold and be unresolved unless the role of emotions in general and unconscious phantasy in particular are explicitly recognised.

Notwithstanding the three official reports into the crisis, Irish society continues to struggle with understanding what happened and how it happened. A government inquiry (Oireachtas Banking Inquiry) was formed and has called in excess of 130 witnesses from a wide variety of sections of society, including the authors of the three "official" reports, as well as central bankers, economists, bankers, newspaper editors, property developers, real estate agents, government lobbyists, IMF, European Commission and the President of the ECB, Jean Claude Trichet[114]. With the exception of the testimony of witnesses in relation to the events surrounding the nights the government was panicked into (1) the blanket guarantee (September 2008) and (2) the bailout of November, 2010, the media has lamented the lack of any "new" evidence assigning blame for the crisis that unfolded. The testimony around the date of these two events largely revolved around the exposure of the taxpayer to the banking sector. In other words, the question seeking to be resolved was the question of burden sharing and whether the Irish taxpayer should be held accountable for the entire losses of the domestic banking system or whether some banks, notably Anglo Irish Bank,[115] should have been allowed to fail, with unsecured and secured bondholders participating in the losses.
Both of these events, and the latter event in particular, can be classified as the time that reality started to dawn about the significant and unmanageable banking and macroeconomic consequences of the property bubble. The *manic defence* was no longer possible and all participants could no longer bargain with reality and *basic assumption* group thinking was no longer sustainable. It is noteworthy that the gap of time between the start of the decline in the property market (April 2007) and the bailout (November, 2010) was almost 3½ years and that this period was, with a couple of notable "naysayers", characterised by basic assumption group behaviour.

[113] Night that brought us to our knees: The true impact of the decisions made to save the banks is only now becoming evident, *Sunday Independent*, 11 April, 2010.

[114] The latter, Jean Claude Trichet, appeared in a highly contrived format.

[115] Anglo Irish Bank was the Bank with the greatest exposure in absolute terms to losses from developer loans and, in addition, was not a clearing bank and hence central to the payments system. In such circumstances some commentators argued that Anglo should be allowed to fail with the consequent "burning" of the unsecured and secured bondholders of that bank. It was clear from evidence given at the Banking Inquiry by representatives of the IMF, senior Government ministers and the nuanced answers of the President of the ECB that the ECB and European Commission were against this strategy in fear of the potential impact on the markets not only from the Irish but also from a European perspective and that the Bailout of November 2010 was conditional on not "bailing in" bondholders.

The fact that no *new* information emerged as to the causes of the banking crisis is not unsurprising and is consistent with the repressed anxieties no longer able to be rendered unconscious. As Tuckett and Taffler (2008) note: *"It is striking that the information available to economic agents to judge or price the riskiness of investments does not really change during the course of bubbles. Rather, what seems to change is the attitude of mind towards available information"*. In other words the lens through which the information is viewed starts to alter. The work group starts to replace the influence of the basic assumption group, perhaps with a substantial lag punctuated by the assignment of blame and anger focusing on others such that as Taffler (2014, p.19) notes *"Anger and blame of others rather than feelings of personal guilt erupt allowing investors to remain operating in a divided stare of mind and avoid the painful realisation of how they have been caught up themselves in the very fulfilling and exciting fantasy."*

It is very clear from the economic data that post- 2002 the banking system became progressively more detached from the real economy and the engine of growth in the banking system was banks' property portfolios with such lending increasing geometrically. In addition, investors in general were drawn in as growth in Irish bank share prices continuously outperformed other shares and the growth in the economy as a whole as measured by GDP. Even when interest rates started to go up banks took action to relax credit terms by term extensions. As property prices went up banks also systematically increased their loan- to- value ratios, in effect making credit more freely available. Government became increasingly reliant on property related taxes to finance their expenditures. At the same time a succession of international institutions and financial media, the IMF, OECD and the Economist argued that Irish residential real estate prices were detached from fundamentals and were significantly overvalued. Concurrently all the leading actors (regulators, economists, media etc.) either ignored, dismissed, sugercoated, or downplayed any such "negative" information. Such behaviour is characteristic of the divided state of mind and basic assumption group behaviour whereby ignoring or rationalising away any feelings that cause mental pain and spoil the positive or pleasurable ones, in an attempt to be left with only the pleasurable.[116]

In the basic assumption group such strategies may include *splitting*, mentally separating the good and bad feelings with the latter being suppressed and rendered unconscious, *idealisation* (the unrealistic exaggeration of attributes or qualities), *projectio*n (unconsciously attributing unwanted feelings and attaching blame to others), and critically *denial* (the repudiation or disavowal of aspects of external reality the individual does not want to know about to diminish or avoid painful effects associated with that reality) (Auchincloss and Samberg, 2012). In this way emotional conflict or ambivalence is sidestepped and avoided.

We saw that property was idealized in the media. Emotional language such as "*living the dream"* etc were pervasive in property descriptions. In such circumstances even the property developers themselves attracted sobriquets such as "*Paddy the gent*" and there was a fascination in the media with their social lives. More and more Irish people got sucked into the property market with many owning multiple properties. When opportunities seemed to run out in Ireland attention turned to the acquisition of overseas properties (portrayed using similar colourful descriptions) with the proportion of media articles extolling the purchase of overseas properties increasing dramatically post 2002, a period coinciding with the relaxation

[116] This is in contrast to the integrated state of mind, which is characteristic of the work group, whereby both good and bad feelings are acknowledged and tolerated, ambivalence is felt and recognised and uncertainty accepted.

of credit standards and enormous increases in the sizes of banks' property portfolios. In fact those articles extolling the purchase of foreign properties continued long after Irish property prices started to go down in April 2007 and continues up to the present day to be higher than the pre- 2002 period. Overseas property acquisition was even seen by property developers as a "*revenge for empire"* and as a means of establishing an Irish empire!

Such idealization and the splitting off of all negativity associated with property acquisition was clearly manifest, in particular in the period post 2002. Property was seen as a one way bet with many newspaper articles documenting property price growth outperforming other asset classes such as shares and traditional deposits. The continued upward trajectory in property prices since January 1994 would have provided comfort and reinforced this view of the "one way bet". Such was the excitement associated with property purchases that developers introduced phase 1, 2 and 3 within weeks of one another as a rationale to increase prices as properties were snapped up. Bankers fuelled this excitement by relaxing credit terms.

At the same time *projection* was evident. Those who dared to speak out about the overheated property market were vilified and regarded as "talking down the market" and making downward price spirals a self-fulfilling fantasy as in the case of the media commentary in relation to Kelly and Ahearne. All parties jumped on the vilification bandwagon with even the Prime minister decrying those "cribbing and moaning" and that they should consider committing suicide with their "glass half empty" attitudes.

In fact the *After Shock* Programme itself and its tone became the personification of negativity with one journalist commenting: *It wasn't the facts, which all sounded pretty damn serious, an unappetising platter of tart , little bite-sized indicators, including rising interest rates, relocation of multinationals to cheaper economies, a sliding US dollar and a slowdown in construction (apparently 280000 of the workforce are involved in the building industry, proportionately twice the UK figure). No, my scepticism had more to do with the soundtrack. Wide shots of semi- detached commuter belt, M50- ville housing estates, anonymous units after anonymous unit, their optimistic gables glinting in the sunlight, were underscored by Jaws- like music, a portent, the programme seemed to suggest of imminent ghettoization".* [117]

In addition, as the property market started to deteriorate with spillover effects into the banking system and ultimately into the macroeconomy there was a shifting pattern in the attribution of blame. As shown in the media section initially blame first fell on the politicians for not doing more to facilitate bank lending and reducing stamp duty to make property purchasing more attractive. Blame then fell on the financial regulator (Patrick Neary) for "regulatory" failures with him described not as the financial regulator but the "*financial facilitator*". "*His prime function was to send out a non- stop signal to the financial services cowboys all over the world that the wild west was open for business, and that no questions would ever be asked*"[118].

Another journalist commented:

[117] Hollywood hangers on, Irish Times, 21 April, 2007
[118] No shame dooms us to repeat mistakes, Irish Independent, 11 june 2010.

"*There has always been a touch of Basil Faulty about the hapless financial regulator Patrick Neary. He resembles actor John Cleese. He is tall, sports a moustache, seems like a decent man, a bit baffled, but is out of his depth and accident prone*[119]
The period post the banking guarantee in September 2008 triggered the attachment of blame to bankers [120]. [121] [122]

In turn property developers blamed banks for lending them money and politicians
"*Bank of Ireland begged us for business. And I said at the time to them: 'when things go wrong you won't be able to manage it". But they still pushed and pushed. The man I dealt with said: 'all I'm interested in is your home (as security) and your personal guarantee"*
'*This is a very small country'* he continues. ."*half a dozen people could run the bloody place. But we've a talking shop in Dail Eireann (Irish Parliament) full of people who've mostly never made a shilling in their lives. And now they've used the banks and the developers as a scapegoat for their own bad decisions*.[123]

One banker even blamed those who borrowed money from them
"*Most of us believe the banking crisis was the regulators fault. We've had a property developer write a book telling us it was the bankers fault and especially those at Anglo Irish. So it's only logical that we now get a bankers book blaming the rest of us"* [124]

There was even a view that The ECB was to blame for its interest rate policy:
"*The absence of any quantitative easing when necessary has been at the behest of a German Government that has a pathological aversion to inflation*" [125]

This oscillating pattern of blame has not yet resolved itself and inhibits the transition from the PS to the D state of mind. In such circumstances learning may be inhibited by virtue of the search for scapegoats rather than coming to terms with the collective guilt associated with the wish fulfilling phantasy that property prices could only go up forever.

Denial was clearly manifest as the property bubble started to unravel post April 2007 and its consequences spilled into the banking sector and the wider economy, triggering the bank guarantee in September 2008 and the bailout in November 2010. All economic actors (central bank regulators) participated in the denial. The CBFSAI in its Quarterly Bulletins and Financial Stability report did comment on the rapid acceleration in bank lending and its concentration in property related activities but they argued that strong fundamental factors supported bank lending activity. In addition, in the 2007 FS Report there was criticism of the property valuation models employed by the IMF and OECD and that they did not adequately allow for fundamentals and argued in the 2007 FSR that the "distribution of house price declines (in their models) indicates that the majority occurred in the different economic period prior to the 1990s). Thus they were in effect arguing that "this time it's different". As

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[119] Neary was john cleese to fawlty towers of irish regulation, Suinday Independent, 11 January, 2009.
[120] Its high time that we sacked some of those stupid bankers, Irish Indepebedent 2 October, 2008; Last chance for Lenihan to tame the bankers, Sunday Independent 28 December 2008.
[121] Demise of AIB chiefs must lead the new approach: nationalisation may be the only route to ensure taxpayers get value for money Sunday Independent, 3 May 2009; Fingleton's great work consisted of turning a mutual sociery, formed to help people buy a home into a cavernous gsame of financial ping pong, Irish Independent, 28 March 2009.
[122] Usual suspects survive fiasco, *Sunday Independent*, 5 October 2008.
[123] Developer says Bank of Ireland 'begged for business', *Sunday Independent,* 3 May 2009
[124] 'Victim' Fitzpatrick's book is just self-indulgent claptrap, *Irish Independent*, 10 January 2011
[125] Trichet should resign over this mess we're in, *Irish Independent*, 27 November 2010

prices continued to decline the Reports in 2007 and 2008 whilst acknowledging property price declines argued that the fundamentals were strong and that there would be a "soft landing" with with even the comment that such declines were welcome to improve " housing affordability". Stress tests employed by the banks on banks property portfolios assumed only minimal price declines (Honohan, 2010). The price declines in 2007 were attributed by the Central Bank to ECB interest rate increases and uncertainty over mortgage interest relief, not to detachment from fundamentals. It was only in the Quarterly Bulletin of Summer 2008 that it was acknowledged that prices in 2006 and early 2007 "did not appear to be supported by fundamentals" but that there would still be a soft landing. At no stage did the reports acknowledge the potential for a spillover to the banking sector or the wider economy as the quotes from Patrick Neary, the Financial Regulator illustrate. This is despite the fact that all the Quarterly Bulletins from 2003 and each of the FS Reports in 2004-2006 acknowledge that property related lending accounted for the enormous increases in bank lending activity.

The Honohan Report specifically refers to the fact that all the information was available to the CB but they failed to use it effectively: The CB Financial Stability Reports (FSR) was criticised whereby: "sanguine conclusions were reached based on a "selective reading of the evidence" (p.9) and the commentary in the 2007 FSR regarding a "*Soft Landing*" was regarded as a "*Triumph of hope over experience*" (p10)' Honohan talks about "*deference and diffidence"* on the part of the Central Bank (p.12), a fear of *"rocking the boat"* (p.16). with *"... an unwillingness on the part of the CBFSAI to take on board sufficiently the real risk of a looming problem… Rocking the boat and swimming against the tide of public opinion would have required a particularly strong sense of the independent role of the central bank in being prepared to "spoil the party and withstand strong adverse public reaction"*. (p.16)

On a similar basis other economists (with the notable exceptions of Kelly and Ahearne) made arguments consistent with the soft landing arguing that the fundamentals of the property market and the economy were sound. The ESRI though publishing Kelly's article In Summer 2007 that there would be a hard landing property crash stressed that such views were not the view of the ESRI and that they anticipated a soft landing. Some argued that when the rate house price growth started to decelerate in 2006 due to rising ECB interest rates that it did not matter as cost of borrowing would remain low because of inflation, notably house price inflation. In addition, there were concurrent arguments made that the increase in household debt did not matter as it was underpinned by housing assets. Post April 2007 when prices started to go downward they argued that prices should be bolstered by reducing stamp duty and increasing mortgage interest relief. In addition, they argued that the property sector was very robust and that the downturn in residential could easily be compensated by other sectors such as house refurbishment/ renovations or substitution into commercial activity. There were even arguments that property was not central to economic growth in any case as it "*was not the engine of the boom and should not be the cause of a bust.*" In fact there were even arguments made that the declining prices improved affordability and that these temporarily low prices should be availed of before they started to go up again:

The smart, ballsy guys are buying up property right now. [...] Tell you what, I think I know what I'd be doing if I had money, and if I wasn't already massively over-exposed to the property market by virtue of owning a reasonable home. I'd be buying property. [...] So why would I be buying property right now if I could? Well, for starters, property is good value these days. It's certainly cheaper than it was six months ago[126]

[126] Sunday Independent, 29 July, 2007

On a similar basis banks and politicians were expressing similar sentiments right through the bank deposit guarantee in September 2008 and, in the case of the politicians, up to and including the government bailout in November 2010. The justification for the bank guarantee was attributed by the Minister for Finance to “unprecedented disruption in international financial markets” arising from the Lehman Brothers collapse and that “any financial exposure is significantly mitigated by a very substantial buffer made up of the equity and other risk capital . He had earlier argued in May 2008 that the fundamentals of the housing market were sound quoting “*a relatively young population and continued inward migration”* despite the decline in house prices which had started a long time before the Lehman Brothers collapse and was not arrested by the relaxations in stamp duty and additional mortgage interest relief introduced in late 2007. The Prime Minister had expressed his anger at those who were “talking down the economy” with their “glass half empty” philosophy.

Concurrently the banks were commenting on the underlying strength of the economy blaming their funding crisis on international liquidity issues and that their institutions were fundamentally sound and that there were not going to be loss provisions requiring the raising of additional capital. Eugene Sheehy’s, the CEO of AIB’s comment in October 2008 that “*we’d rather die than raise equity*” speaks volumes. At the same time as these remarks were been made AIBs share price continued as international investors worried about the exposure of the Irish banking system to property related loans.

The introduction of the bank guarantee in September 2008 did nothing to alleviate the anxieties of the international investment community towards the Irish banking system and its exposure to property. Shares prices continued to decline and the ability of the banks to access international capital markets continued to dry up eventually precipitating a cascade of bank nationalisations commencing in January 2009 when Anglo Irish Bank was nationalised.

In aggregate our results indicate that the Irish residential real estate bubble was highly emotionally charged. All economic agents in society (bankers, the media, regulators, economists, estate agents, investors and homeowners) either actively participated in the property roller coaster or, importantly in the case of the Central Bank, from a regulatory perspective did not attempt to sufficiently warn that property prices were becoming increasingly detached from fundamentals, in particular in the period post 2002. Classic *basic assumption* group think set in and international agencies who warned against a residential real estate bubble were either ignored or the validity of their modelling approaches questioned. Those limited number of domestic commentators, (notably the two independent economists, Kelly and Ahearne, though arriving late, only after the property market had virtually peaked), who put their heads above the parapet were vilified and indeed in some cases their very patriotism itself was questioned. There was in addition, clear evidence post-2002 that the exposure of the banking system to real estate lending activity increased in terms of: (1) the magnitude of bank lending as a proportion of total lending activity, (2) loan – to-value- ratios advanced, (3) relaxation of credit terms and on interest rate margins, and, (4) the proportion of such loan expansion that was financed by international deposits. Also the size of bank lending activity devoted to real estate exceeded GDP by 2004 and was 47% higher than GDP by 2007! That this went largely unchallenged by the economics profession in particular is worrying as though economists have differences over certain aspects of bubbles they are agreed that there should be concerns where spillover effects and macroeconomic imbalances may occur.

We argue that traditional economic theories find it difficult to explain asset pricing bubbles in any convincing way and are predicated on efficient markets where prices reflect available information. Though some economic models arising out of the Global Financial Crisis do incorporate limited behavioural aspects of asset pricing, they tend to do so in highly stylised ways, and, importantly, the role of emotions and group and social processes are largely ignored. Given the highly emotional aroused state of all the actors in all spheres associated with the Irish residential property market and the consequent dramatic spillover effects there is a need to understand the underlying emotional process as there are considerable public policy implications.

Specifically, the role of emotions and emotional processes should be incorporated into the curricula of economics degree programmes. The Central Bank in Ireland has introduced a *fitness and probity* regime to ensure that future bankers have the technical skills, competence and experience to ensure that similar crises do not happen in the future. These technical skills need to be supplemented by education in the emotional processes associated with individual and group decision making as indeed does the curriculum of financial advisers in general. From a governance perspective it is important that the boards of banks and regulatory authorities have sufficient balance not just in terms of technical banking skills but also to have training in group dynamics and the role of emotions in decision making. It is interesting to note that the official reports into the crisis have commented on improving technical skills in banking, credit and related matters but have been silent on the role that emotions played in creating and exacerbating the bubble, propped up by classic basic assumption group behaviour. In other words there is a need to have tools in the armoury to fight against the mantra that “this time it’s different”.

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Table 1

Significant News Items and Events in the Irish Property Bubble and Consequent National Economic Collapse

Year	Month	Event/ News item
1994	January	Start of the period of quarter on quarter property price increases coinciding with the commencement of the period characterised as the "Celtic Tiger"
1999	January	Launch of euro as an accounting currency
2001	May	ECB starts on trajectory of continuous benchmark rate reductions lasting before levelling off at 3% in June 2003
	December	Irish government budget introducing favourable property tax incentives including reductions in stamp duty and also increased ceiling of interest rate deductibility for investors against rental income. Successive budgets in 2003, 2007, and 2008 increased the deductibility of interest for owner occupiers.
2002	January	Euronotes and coins go into circulation
2003	May	Economist Newspaper warns that Irish property may be overvalued by 42%
	August	IMF warns that house prices may be overvalued by 20%
2004	Various months	Large increase in competitive rivalry on high loan- to-value mortgages, mortgage term length and interest rates offered (including tracker mortgages)
2005	June	Economist Newspaper warns that Irish property is overvalued
	November	OECD reports that Irish property prices may be 15% overvalued
	December	ECB starts on an upward trajectory of benchmark interest rate increases with at least 25bp incremental increases
2006	March	OECD argues the property market may be overheated and argues for phasing out of property tax incentives
	March	Davy Stockbrokers report that in certain sections of the Dublin property market prices were 100 times rents
	April	ESRI says in its Spring Quarterly Economic Commentary says that a property bubble probably exists but that a "soft landing is the most likely outcome"
	April	Central Bank and Financial Services Authority of Ireland in its Financial Stability Report said that the housing boom "may be unsustainable" but that a "soft landing

		is the most likely outcome"
	August	IMF warns that house prices are becoming overvalued and that a sharp correction cannot be ruled out
2007	April	"Future Shock Property Crash" Programme by the national broadcaster RTE is broadcast suggesting that the property market is very vulnerable to a shock. This is followed within a day by a dedicated edition of the current affairs programme "*Primetime*" to the Future Shock programme. Both of these programmes generate significant public commentary.
	July	ESRI Quarterly Economic Commentary states that their analysis is that house prices may fall by 3% but in an opinion article (not officially endorsed by the ESRI and only appended to the Commentary) academic economist Morgan Kelly states that up to 60% could be wiped off the value of housing.
	October	Central Bank Financial Stability Report argues that the property market would have a "soft landing"
2008	June	Central Bank Governor in his statement on the Banks Annual Report and Accounts that a soft landing was the likely scenario for the Property market
	September	Lehman Brothers collapses
	September	Irish Government gives blanket guarantee on the deposits of Irish banking institutions due to an international haemorrhage of international deposits
	October	IMF World Economic Outlook in reviewing the period 1997-2008 says that the Irish residential property market is overvalued by 33% and is the most overvalued vs. 17 other major economies.
2009	January	Anglo Irish Bank is nationalised starting a succession of nationalisations (Irish Nationwide (August 2010), AIB (December 2010), Irish Life and Permanent (July 2011), EBS Building Society (July 2011)*
2010	February	Irish Minister for Finance commissions 3 reports into the collapse of the Irish banking system (Honohan, Regling & Watson and Nyberg)
	May	Honohan Report is published
	July	Regling & Watson report is published
	October	Irish government bond yields spike at 7%
	November 2010	Formal request by Irish government for IMF, ECB and European Commission (Troika) aid
2011	March	Nyberg report is published
2013	March	Property prices start to rise again
	December	Ireland leaves the Troika aid programme
2015	April	Financial Times reports that there are signs that another property bubble may emerge
	June	OECD warns that Irish residential real estate prices are "reminiscent of the bubble"

*= The only domestic financial institution not to be eventually nationalised was Bank of Ireland , which thanks to its capital raising activity kept the proportion of state ownership to 36%

Table 2

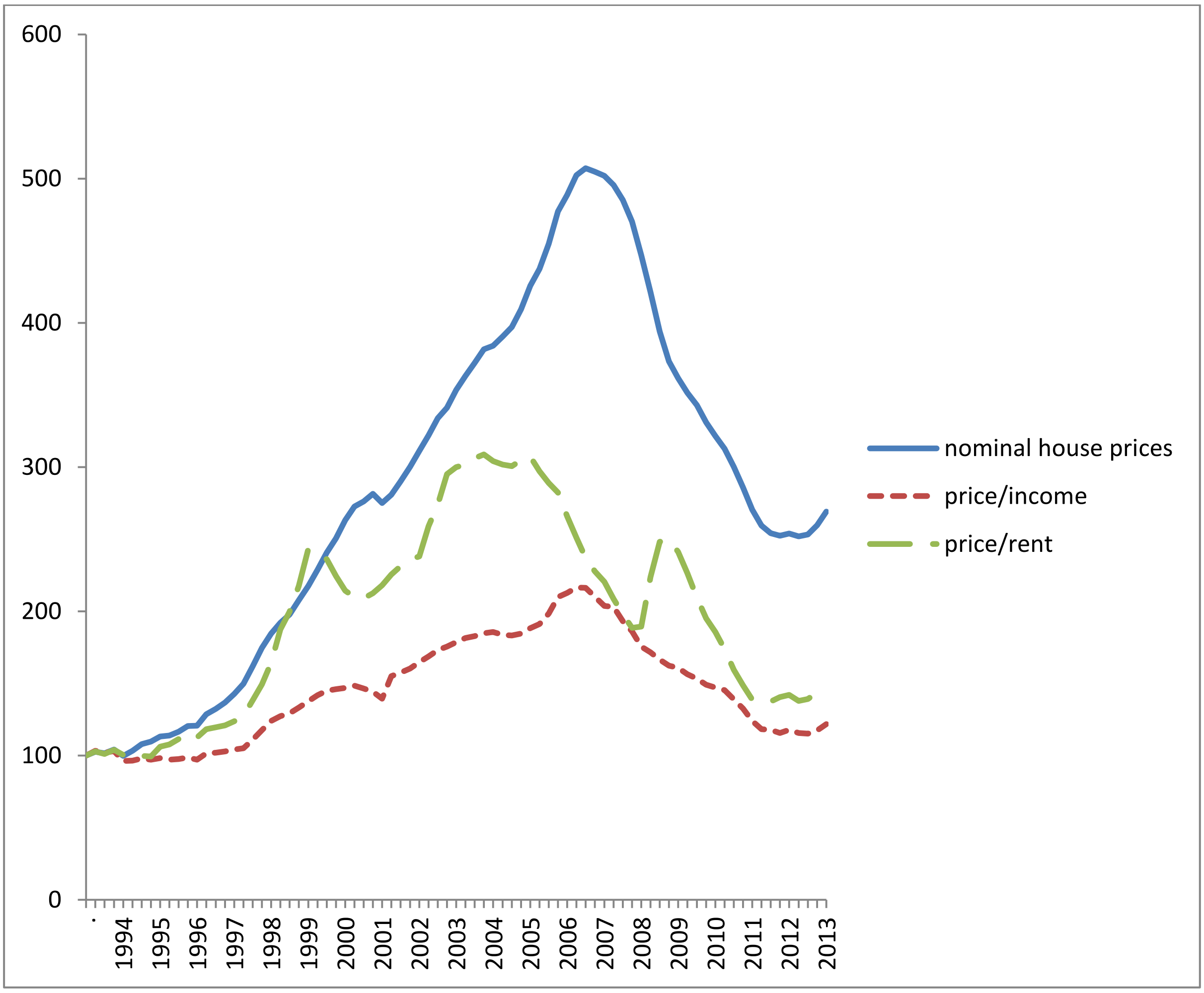
Thematic Analysis of Real –estate Related Newspaper Articles

		News category	article tone	boom	euphoria	denial	blame	boom	
				%of total	% of total	% of total	% of total	% of total	
Panel A: News Events									
		view of property m	positive tone	15.9%	20.2%	17.9%	28.4%	32.3%	
			negative tone	4.9%	4.8%	13.2%	6.9%	1.0%	
			total	20.8%	25.0%	31.1%	35.3%	33.3%	
		banks	positive tone	0.0%	0.0%	0.4%	0.0%	2.0%	
			negative tone	0.7%	1.1%	7.0%	6.9%	0.0%	
			total	0.7%	1.1%	7.3%	6.9%	2.0%	
		Politicians	positive tone	0.7%	0.0%	3.3%	10.8%	5.1%	
			negative tone	1.4%	0.0%	8.4%	2.9%	3.0%	
			total	2.1%	0.0%	11.7%	13.7%	8.1%	
		Sales	positive tone	15.2%	11.9%	2.6%	1.0%	1.0%	
			negative tone	1.1%	0.0%	0.4%	0.0%	0.0%	
			total	16.3%	11.9%	2.9%	1.0%	1.0%	
		Renovations	positive tone	13.1%	9.9%	8.4%	9.8%	14.1%	
			negative tone	0.4%	0.6%	0.4%	0.0%	0.0%	
			total	13.4%	10.5%	8.8%	9.8%	14.1%	
		Affordability	positive tone	2.5%	5.7%	5.5%	3.9%	3.0%	
			negative tone	6.0%	4.3%	0.7%	3.9%	7.1%	
			total	8.5%	9.9%	6.2%	7.8%	10.1%	
		Foreign	positive tone	4.6%	20.5%	12.8%	5.9%	5.1%	
			negative tone	0.7%	1.1%	2.2%	1.0%	1.0%	
			total	5.3%	21.6%	15.0%	6.9%	6.1%	
		Developers	positive tone	1.1%	3.1%	4.8%	0.0%	1.0%	
			negative tone	1.1%	0.6%	5.9%	11.8%	5.1%	
			total	2.1%	3.7%	10.6%	11.8%	6.1%	
		Expert opinions	positive tone	3.9%	0.9%	0.0%	1.0%	11.1%	
			negative tone	0.0%	0.3%	0.7%	1.0%	0.0%	
			total	3.9%	1.1%	0.7%	2.0%	11.1%	
Panel B: Summary Statistics									
			Total#	283	352	277	102	109	1123
			average no. of articles per qtr	20.2	22.0	19.8	12.8	13.6	18.7
			#pos	210	281	165	63	85	804
			#neg	73	71	112	39	24	319
			%pos	74.2%	79.8%	59.6%	61.8%	78.0%	71.6%

Source: Irish Times Newspaper (From Factiva)

Figure 1

Graph of Residential Real Estate Prices, Rents and Income 2000-2013



Source: OECD

Figure 2(a) Sample Auctions

• March 05, Sold €730,000	April 06: Sold € 1800000

Initial Price:	730,000
Upgrades:	90,000
Total:	820,000
Profit:	119%

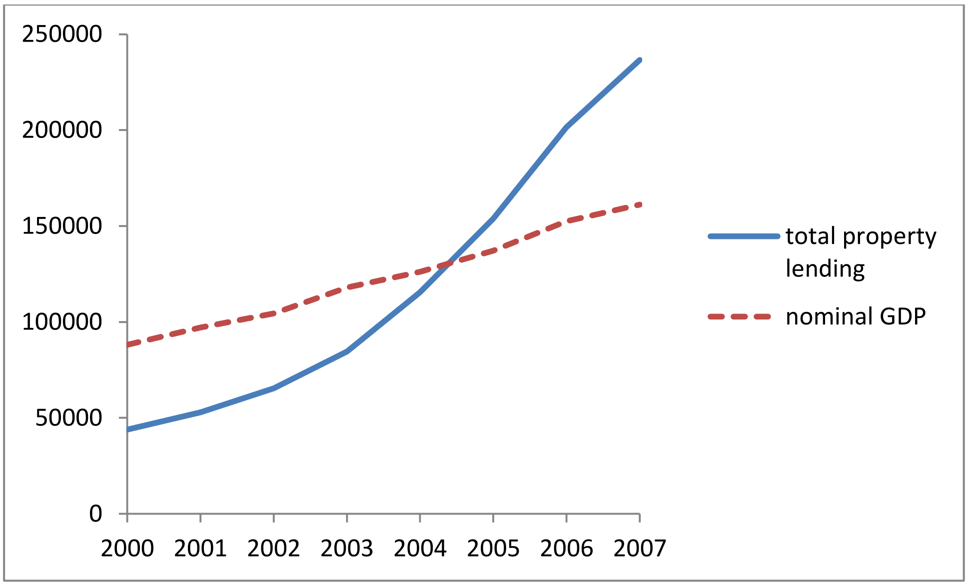
Figure 2 (b) Sample Auctions

September 2005 €3,850,000	October 2006: € 6000000

Initial Price	3850000
Upgrades:	150000
Total:	4000000
Profit:	50%

Figure 3

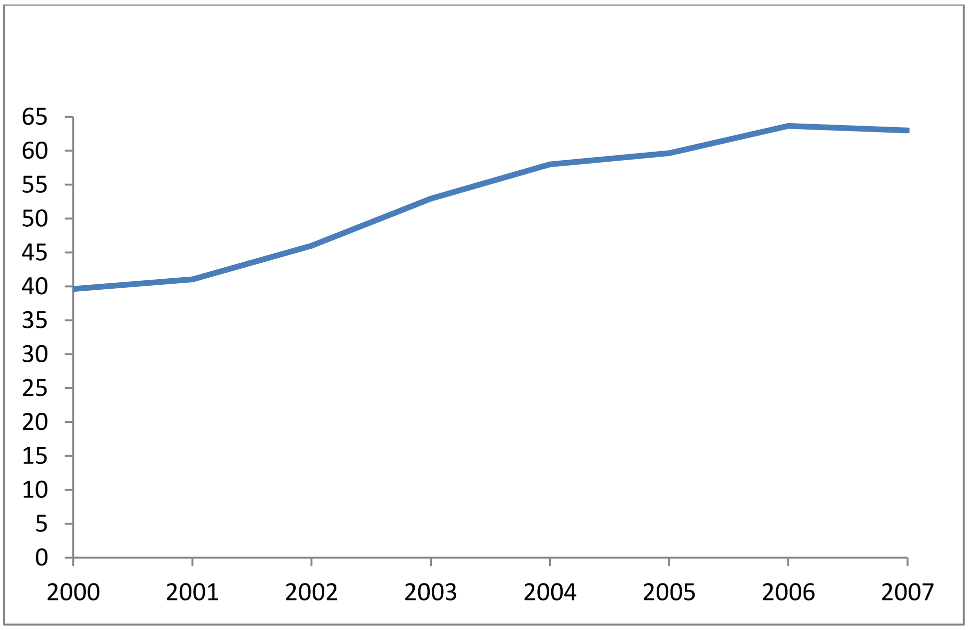
Property Lending and GDP



Source: Irish Central Statistics Office, Annual Statistical Summary

Figure 4

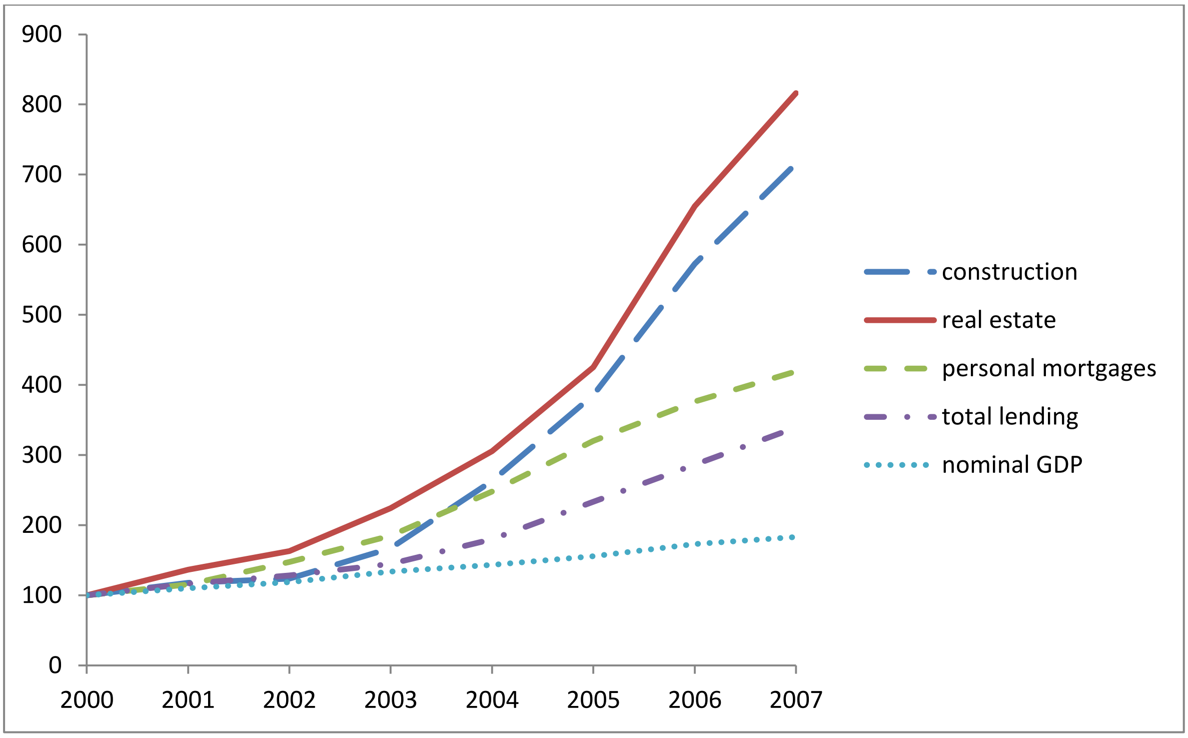
Proportion of Total Bank Lending attributable to Property-related Lending



Source: Irish Central Statistics Office, Annual Statistical Summary

Figure 5

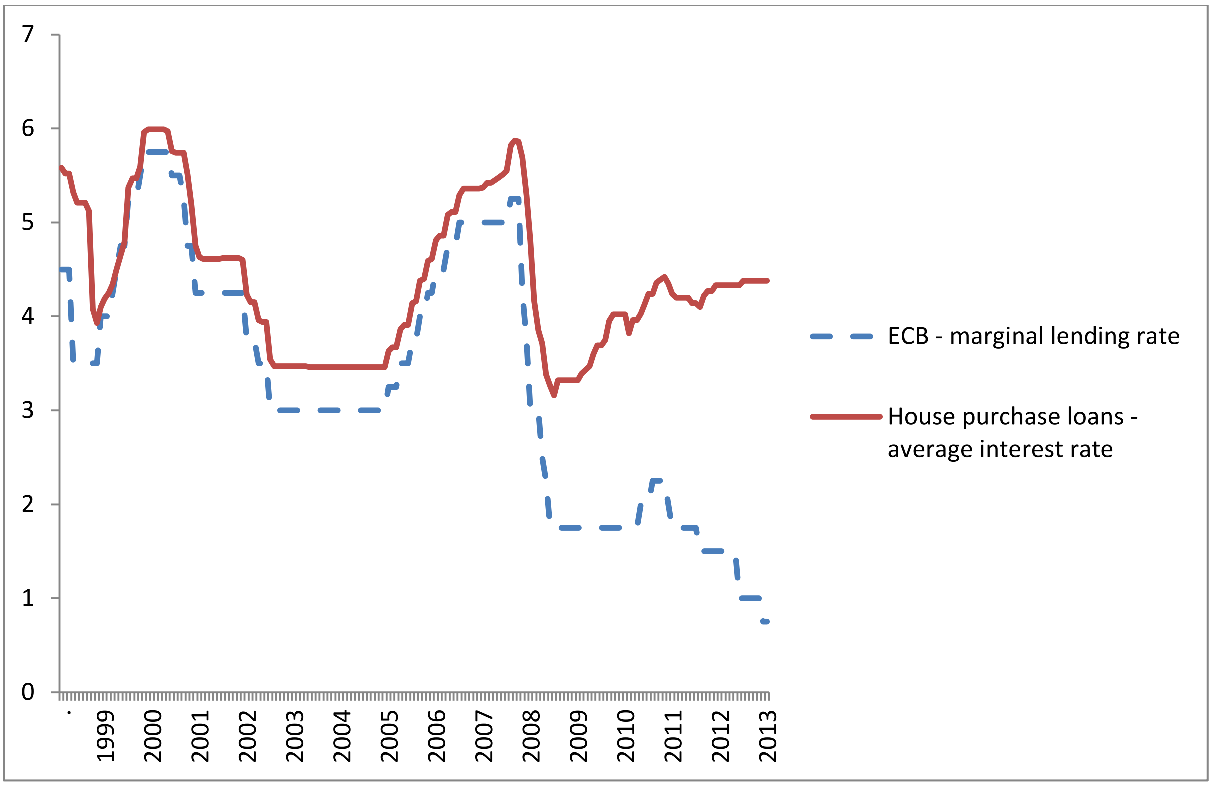
Sectoral Decomposition of Increase in of Bank Lending 2000-2007 (2000=100)



Source: Irish Central Statistics Office, Annual Statistical Summary

Figure 6

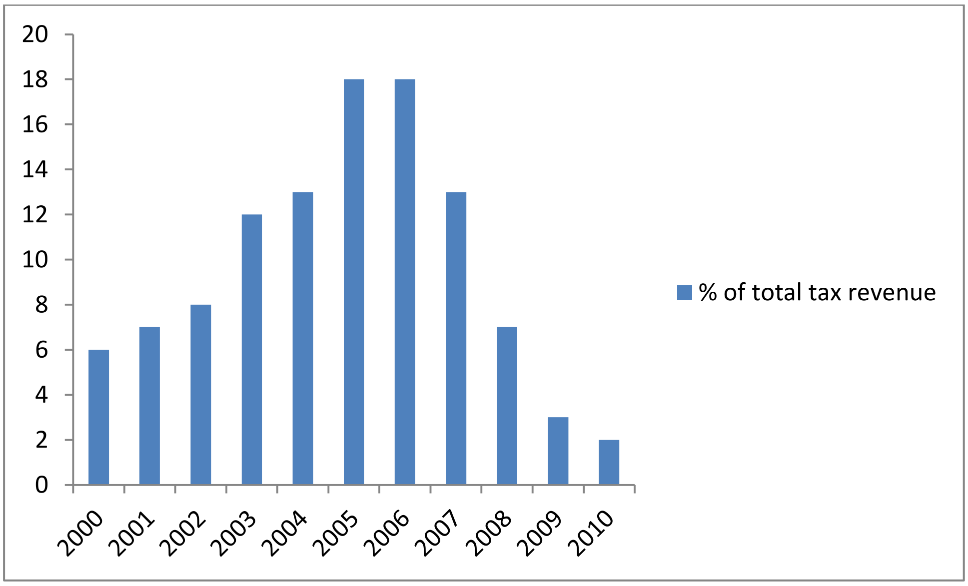
ECB Interest Rates and Interest Rates on House Purchase Loans 2000-2013



Source: Department of the Environment and Local Government

Figure 7

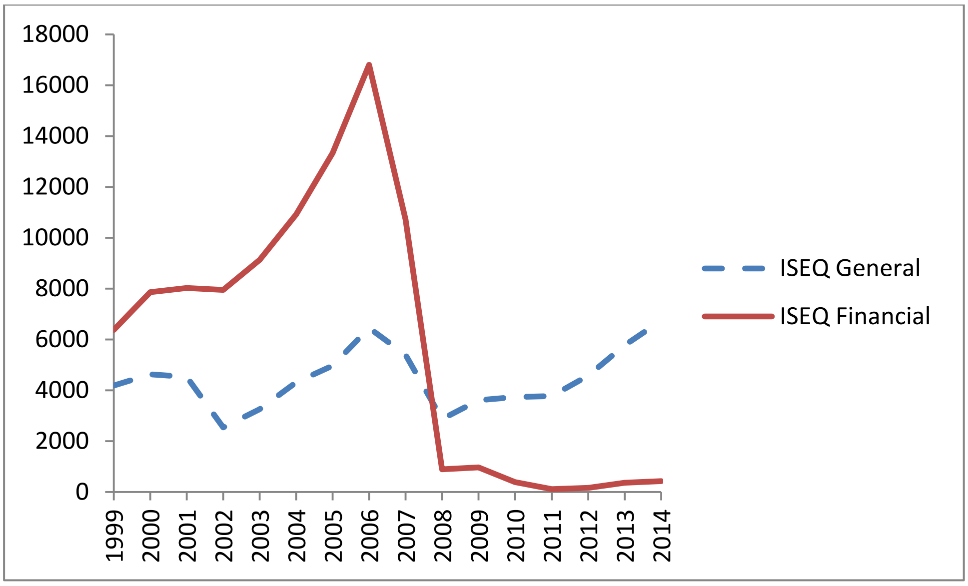
Property – related Tax Revenues as a Proportion of Total Government Income 2000-2010



Source: European Commission and Goodbody Stockbrokers

Figure 8

Performance of Irish Share Indices 2000-2014



Source: Irish Stock Exchange