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MONEY BOX

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LEWIS: Hello. In today's programme, as concerns grow about the state of Iceland's economy, we ask how safe is our cash in Icelandic banks. Here, the Chancellor promised again yesterday to do "whatever it takes" to protect depositors. So is raising the protection limit on cash savings to £50,000 on Tuesday irrelevant? The US Congress has finally agreed to spend \$700 billion of taxpayers' money buying up bad debt. Here the Bank of England will pump £40 billion more into the market on Tuesday. Is this even the beginning of the end for the world banking crisis? And campaigners are going to court on Monday to try to force the Government to end fuel poverty.

But first, the Icelandic government is seeking a loan from abroad to prop up its ailing economy. Despite its small size, Iceland supports several large banks. Last weekend, the Icelandic government stepped in to rescue the third biggest bank, Glitnir. More than 100,000 UK savers have put their money into its two biggest banks, Kaupthing and Landsbanki. Both banks seem secure, but how safe is our money in them? Concern was raised in the press this week, most notably in today's Daily Telegraph, and confidence hasn't been helped by reports from customers that they've been unable to take money out of their accounts due to a fault with the website. We'll be talking to the Head of Icesave in the UK shortly, but a few minutes ago I spoke to Triggyi Herbertsson, the Economic Adviser to the Icelandic Prime Minister. I asked him first could the Government afford to rescue another big bank?

HERBERTSSON: It's obvious that the banking system in Iceland is very large compared to the economy, but still we think we can maintain the problem, you know, because the balance sheet of the bank is after all very good. That is what is the asset side of the balance sheet and because they have not been involved in sub-prime or buying housing debt from the States or from abroad. So we're pretty confident that the balance sheet is healthy and the banks can operate healthily in the future.

LEWIS: Sure, but just to repeat the question. If one of them did get into difficulties, despite what you say, could you afford to rescue it?

HERBERTSSON: Definitely we would come to the rescue of the bank, definitely.

LEWIS: A lot of people in the UK have savings in those two banks - Landsbanki and Kaupthing. Is their money safe?

HERBERTSSON: Yes. According to my knowledge, you know Iceland is a part of the European directive on deposit insurance, so yes they should be.

LEWIS: I know you're part of the scheme. I'm asking if they did come to you, you would say, "We can pay your 20,000 euro", or would you say, "The economy's in such difficulties, I'm sorry we can't meet this obligation"?

HERBERTSSON: No, we're not in that kind of difficulty.

LEWIS: So you wouldn't?

HERBERTSSON: And it's also you know some of the Icelandic banks are operating out of branches in the UK, so the UK scheme applies to those banks.

LEWIS: It does to Kaupthing but, as I understand it, not to Landsbanki. But there's no danger that you will not have enough money to meet the claims of British savers if they come to the compensation scheme in Iceland for help?

HERBERTSSON: Yeah, like I say, you know we're bound by international law to apply to ... Yeah, we have to apply to international law.

LEWIS: Triggi Herbertsson, the Economic Adviser to the Icelandic Prime Minister, talking to me a few minutes ago. Now Icesave is owned by Landsbanki and has around 300,000 customers in the UK. Live now to talk to the Chief Executive of Icesave in the UK, Mark Sismey-Durrant. Mark, should UK investors in your bank be nervous about the state of the Icelandic economy?

SISMEY-DURRANT: Hello Paul. No. Well, no they shouldn't be nervous about the state of the bank. Certainly the article in the Daily Telegraph today will have attracted attention from people, but Landsbanki is an international bank. The other major Icelandic bank, Kaupthing, is also an international bank with operations abroad and a lot of the focus of attention has been on the size of the banks in relation to the Icelandic economy. But the banks have assets abroad and they raise deposits abroad, so we're a robust, well managed bank.

LEWIS: Sure, but the deposits you raise from your customers abroad, including as I say 300,000 here in the UK, are used for international investments. If everybody asked for their money back, that money would be tied up elsewhere, wouldn't it? So there are always concerns when money is invested in that way that the money won't be there if people want it back.

SISMEY-DURRANT: Well I think the important thing is that you know banks like us raise deposits to fund our activities. The important element of this is how much liquidity you maintain within your business to meet any repayments that are required and we have a strong capital base and we have a high level of deposit funding. 63% of our balance sheet is funded from deposits and we maintain strong liquidity levels to support our normal business operations.

LEWIS: It hasn't helped though, has it, when the very day that these reports are in the press people have been telling us they're having difficulties getting onto the website and moving their money around?

SISMEY-DURRANT: Yes and I must apologise to those of our customers who've had difficulties getting through on the website. We have experienced an intermittent problem, so what I would ask people to do is to persevere because they will get through. We're working on the technical problem at the moment to get it fixed.

LEWIS: So it's a glitch, not a failure?

SISMEY-DURRANT: It's a glitch, not a failure.

LEWIS: And we heard the Economic Advisor to the Prime Minister telling us that you weren't involved with the sub-prime mortgages and the dodgy debts we've talked about on this programme many times over the last year. Is that right? Your money is invested of course abroad, but it is safe, it is in places where you know what it is and you know what the return will be?

SISMEY-DURRANT: Yes, yes, it is.

LEWIS: So just let me ask you finally in a word. UK customers of Icesave can be sure their money is safe and they can get it out when they want?

SISMEY-DURRANT: Yes, they can be.

LEWIS: Mark Sismey-Durrant, thanks very much for talking to us. Well Bob Howard's with me. Bob, just let's clarify about Kaupthing and Landsbanki. What about savers? If one of these banks did get into difficulties - and they've assured us they won't and everyone says they're not going to - but just if they did, what would happen?

LEWIS: Well, Paul, the two banks are different. People with money in the popular Icesave savings accounts or ISA's, which have been offering market leading rates, are protected up to the limit that applies in the UK - £35,000 or £50,000 from Tuesday - but they have to go to the Icelandic Compensation Scheme, which covers the first

20,000 euros (that's about £15,600) and the balance they get from the Financial Services Compensation Scheme here. Now people with money in Kaupthing in the UK are in a different position because it's licensed separately here. It's Kaupthing Singer and Friedlander. So if Kaupthing did go bust - very unlikely - they would go to the compensation scheme here for all their money up to the limit of £35,000 now or £50,000 if that happened from Tuesday.

LEWIS: Thanks very much, Bob. And of course we did hear the Economic Advisor to the Prime Minister saying that that 20,000 euros would be honoured by the Icelandic government should that unlikely event happen.

Well Bob mentioned the £50,000 limit on savings that's going up on Tuesday, and it was part of a joint action on Friday by the Government, the Bank of England and the Financial Services Authority to bring some stability to the financial crisis that's been paralysing the world banking system: the Bank of England will lend more money to the high street banks and on easier terms, starting this coming week; the Government has set up an Economic Development council; and the Financial Services Authority announced that from Tuesday the amount of money in a bank or building society that's protected if the firm did go bust would rise from £35,000 - an amount that was fixed last October - to £50,000. There's been growing pressure to raise the amount after the Irish government passed a law to guarantee *all* savings in six major banks and building societies. Well let's go live now to talk to Chris Pond. He's the Director of Financial Capability at the Financial Services Authority. Chris Pond, why did you pick on £50,000 when there's such pressure in other countries to make it much higher or nothing at all?

POND: Well it was felt that £50,000, Paul, was about the right level. It covers the great majority of deposits, certainly 19 out of 20, and we are consulting to see whether or not that is the right figure in the longer term. But we felt that in order to give people a bit of extra reassurance now, it was thought important from next Tuesday to put the limit up to £50,000 to make sure that almost all deposits were already covered.

LEWIS: And why Tuesday? When the FSA raised the limit last year, it happened immediately.

POND: Well this is just a matter of the logistics and the practicalities of it, Paul. We've got the legislation which is going into Parliament on Monday and, as you've said, this is part of a package of measures which is intended both to increase the stability of the banking system as well as to provide extra protection for consumers while that stability is bedding in.

LEWIS: One of the things that I think causes uncertainty among consumers - and certainly one thing that dominates our correspondence at the moment - is people knowing which bank that £35,000 or now £50,000 applies to. It applies to a registered bank, but that can be a whole list of brands, can't it? One thing people would like is to have that limit apply to a brand, not a bank, so HBOS, the AA, Saga - they're all separate brands but they're all covered by one limit.

POND: Yes, we understand that and that's one of the issues which of course will be the subject of the consultation - to see if there's more that can be done on that. In the meantime, we're trying to make sure that people have a very easy and quick way of checking whether or not the particular deposits they have are a brand of a wider authorised institution or whether or not separately these deposits are covered by the £50,000 from Tuesday and the £35,000 now.

LEWIS: So how will they do that because at the moment it's almost impossible from official sites to find that out?

POND: No, but it is relatively easy. If you call our consumer helpline on 0845 6061234, we'll be very happy to advise people. And also if you go onto the website either of FSCS or indeed the FSA website, you will find which are the registered authorities are on there.

LEWIS: Well, Chris, I have to tell you, I've tried that and from the official websites it's practically impossible.

POND: We'll look into that, Paul, and make sure it's easier.

LEWIS: As the Chancellor said on Friday, "our priority is to do everything we can to stabilise the situation and to protect depositors, and I mean I will do whatever it takes." Doesn't that make this limit irrelevant? The Government really will step in and save everything, won't it?

POND: Well I think this is an important first step and, as I've said, it is part of a *package* of measures. Through this measure, it does cover, as I've said, almost all deposits. And, as you know, the situation in Ireland and elsewhere is being considered by the European Union as to whether or not it is legal to do that. So we need to take appropriate and prudent steps, which is what this constitutes, without necessarily going as far as some of the other authorities have gone.

LEWIS: Chris Pond from the Financial Services Authority, thanks.

Well of course it's the banks and building societies who'll bear the cost of raising that limit to £50,000, so let's talk now to Angela Knight. She's Chief Executive of the British Bankers' Association. Angela Knight, how much will this new limit of £50,000 for UK banks cost you?

KNIGHT: At the moment it's actually quite difficult to give you an exact figure because 96% of individuals are already covered anyway by the existing limit. And what else has been happening is that people have been opening additional accounts. They have if you like been spreading their risk. So the situation is changing as we see it and, as far as we're concerned, where the numbers actually started there was only perhaps maximum 2% more by covering to £50,000. But people, as I say, they have been opening more accounts, they have been spreading their money around to keep below the threshold and, frankly, that's a good thing for them to have done.

LEWIS: Yes, you're thinking that's a sensible thing to do?

KNIGHT: I think that people are spreading risk and that is quite right.

LEWIS: But isn't it only sensible if a bank is likely to go bust, which presumably you tell me is almost impossibly unlikely?

KNIGHT: That's entirely correct and I'd say that again. But, after all, if you're waking up every morning to headlines on the radio and the newspapers ...

LEWIS: You're not going to blame us for this problem?

KNIGHT: Absolutely not. ... and you're seeing that there is a problem in the financial system, it is hardly surprising if people then say okay, I have some things in control in my own hands and so I'm going to open another account as well.

LEWIS: But when the Chancellor says, as he did yesterday again, he will do "whatever it takes" ...

EAGLE: Yes he did.

LEWIS: ... to protect depositors, doesn't that imply that if a bank does go bust - as you say very unlikely, let's hope it doesn't happen, but Bradford & Bingley was taken out of the system last weekend - there will be protection for everybody as they stepped in with Bradford & Bingley?

EAGLE: Well I was just going to say to you Bradford & Bingley is actually a good example of what happens in practice. It's broadly speaking, first of all, the authorities acted as we think they should - get in there early. Second, if you look at the actual deposit protection aspect of it, yes the banking industry has picked up the majority of that - in fact about 80% in that instance - which does show how many people are below the £35,000 limit, and then government picked up the rest. And you know give them their due. Both Gordon Brown and Alistair Darling have rightly said that they will do what it takes, but fortunately we're now seeing that other European countries

have realised that the issue of what is a frozen global financial system affects all countries and they're taking steps too.

LEWIS: But you've written, as I understand it, to the Irish government to complain that it's promising to pick up everything. What's the difference? The government here will do it, but just won't say it. The Irish government - and I understand the Greek and also the Italian governments as well - have just said we're going to protect it all.

EAGLE: Well I haven't heard that from the Italian government and I haven't either written to the Irish government complaining of what they've done. What I've done though is said that this raises competition issues and that is important that one has a level, fair and competitive framework because that's what's going to serve consumers best. Now there is a considerable difference between an explicit guarantee, which small countries have felt that they have had to do, and take all those liabilities onto their public balance sheet, and that will have for them consequences for their taxpayers and for their people. So what I think is much the better way is that governments have a variety of actions available to them, so that action can be taken in advance and that sort of extreme step doesn't have to be taken.

LEWIS: Let me move on from the limit itself and just to ask you briefly, isn't the real problem with the banks at the moment that they've got to start trusting each other again, lending to each other, letting the money move around? When is that going to happen?

KNIGHT: The real problem, as you rightly say, is that we've got a gummed up financial system. Anybody with any sense knows that if you're in an uncertain world, you do look after your own responsibilities and liabilities first, so that is what banks are doing and there's a lot more entities that are in the money market than just the banking industry. Now the Bank of England though made a very important statement yesterday and it is of course working in conjunction with the other central banks, and it's broadened out the collateral that it will take in order to advance long-term money and we think that that is actually a very sound and responsible step to take. It is one that's been taken as well in conjunction with the other major central banks.

LEWIS: Sure, but that is actually stepping in and doing the bank's job for them. What I'm asking you is when are you going to start trusting each other enough to lend each other money?

KNIGHT: Yes, well I've just answered you that question, so I'll answer it a second time around and in a slightly different way. The answer is when the system starts to become unblocked, the answer is we see the consequences of for example the steps that the US have taken in trying to move these very bad debts out of the system and, lastly, when we can see the actions properly being taken by other countries. You want stability. So do we and so do our customers, and that's got to be the first priority.

LEWIS: Angela Knight from the British Bankers' Association, thanks for talking to us and answering my question twice.

We've just had a message from Icesave. It tells us its website is now fixed. No doubt, you'll tell us if that's right.

Now it wasn't only action here in the UK - we talked briefly with Angela Knight about this extra liquidity - but also the United States Congress which finally passed the by now massive bill to buy up \$700 billion of dodgy debt and give another hundred odd billion in tax cuts. Here in the UK, as we've been saying, the Bank of England agreed to lend banks £40 billion on Tuesday on much easier terms - more expensive but less secure terms - and then similar amounts in future weeks. Let's go live now to talk to Michael Hughes. He's an economist and an independent investment consultant. Michael Hughes, one of the papers is saying that central banks are becoming not the lender of last reserve but the lender of *only* reserve now the banks have to go to them for their money. Is that right?

HUGHES: Well obviously it is and I think that we've started to see from the stories you've been covering that this is a global phenomenon and it's not just about the housing market in the States. We're beginning to see the cross border financing deals affect companies and countries in Europe and a lot of these countries and companies have been dependent on building up deposits and financing from across the world,

and that's coming unstuck as well.

LEWIS: And are we going to see this becoming stuck, if it's becoming unstuck, by these actions - by the Bank of England providing this liquidity, it's happening throughout Europe, other parts of the world - and America buying up this dodgy debt for \$700 billion? Is that going to begin to unfreeze the system, as Angela Knight suggested had to happen?

HUGHES: It'll start, but it's possibly not enough. There have actually been forty-two banking crises since 1970, although this arguably is the daddy of them all, but there are some lessons that come from that and separating bad assets from good assets, which is starting to be done, is the first step to rebuilding the system. You then have to recapitalise the good banks and the guys there may have to require equity injections from governments. But finally, for all this to work there has to be a debt relief programme. We saw an element of that in the US proposals, but we haven't yet seen anything like that here. And there is an adverse impact on the real economy which needs to be contained and you need to give debt relief programmes for distressed borrowers, many of whom have been affected by no fault of their own.

LEWIS: So you're talking about not debt relief for banks. You're talking about helping people who've been sold possibly expensive, over extended mortgages by the banks that caused this problem in the first place. They should get *individual* help.

HUGHES: They should get some help and indeed you need it in terms of supporting the economy. I think there is a case for bringing back mortgage tax relief possibly at the basic rate of tax and possibly for a limited period like 5 years, but there are people who are going to find not only is their mortgage rate going up but they may not be able to have the same mortgage they had before.

LEWIS: We talked earlier about whether Iceland could afford to bail out its banks. The Government here is putting tens of billions of pounds every week into the banking system. Is that affecting our economy?

HUGHES: I think it would affect it if they didn't do that because clearly the whole thing would cease up, and even now you're getting difficulties in terms of getting credit supplies and that would be much worse. The question here though is that the Government will have to take the strain and the issue, therefore, is how big can the budget deficit get to and I think it just has to be much higher than it is at the moment.

LEWIS: And we've seen hundreds of billions of dollars committed in the US - tens, if not more, of pounds committed here. We're spending a very great deal of money. Is it going to get better?

HUGHES: Not quickly. I do think these things take years rather than months to come round. But if you go through the three stages I've just mentioned in terms of recapitalising the good banks and introducing a debt relief programme, then I think there will be a light at the end of the tunnel. But that light isn't on yet.

LEWIS: Okay. Michael Hughes, thank you very much indeed for talking to us.

Now on Monday Friends of the Earth and Help the Aged are taking the Government to court. They claim it's failing to deliver on its legal duty to eradicate fuel poverty. The Government's own figures published this week show the number of households in fuel poverty in the UK rose to three and a half million in 2006, an increase of a million on the previous year. And with me is Mervyn Kohler, Special Adviser to Help the Aged. Mervyn Kohler, fuel poverty is spending more than 10% of your disposable income on keeping warm and light and that type of thing?

KOHLER: Needing to spend more than 10% on keeping adequately warm.

LEWIS: That's obviously becoming much more expensive because the price of fuel has gone up, gas has gone up 50%, electricity 30% over the last year or so. How can the Government fulfil this commitment given those outside problems?

KOHLER: There are three strategies to reduce fuel poverty. One is to bear down on

energy prices, which actually drove the strategy forward quite positively in the early years. Second is to ...

LEWIS: When they were falling of course.

KOHLER: When they were falling. Second is to improve people's incomes so that they've actually got more money to spend, and things like pension credit and so on helped in that respect in the early years. And the third is to adequately insulate and draught proof this leaky housing stock that we've got in this country and fix it up with decent heating systems.

LEWIS: Well of course the Prime Minister did promise to do a lot more of that a few weeks ago, didn't he?

KOHLER: Well you say "a lot more". I mean he promised that the companies would spend extra money on doing it. The Government's own flagship programme in this area, it actually cut in the comprehensive spending review last autumn, and it's really because of that that Friends of the Earth and Help the Aged are taking this issue to court.

LEWIS: Now you're taking it to court, as I understand it, because there was an Act of Parliament passed by this government in 2000 saying it would eradicate fuel poverty by 2016 and among vulnerable groups like elderly people by 2010 - a target no-one thinks they're going to meet. What happens if they fail?

KOHLER: And the Government in its own annual reports admits that it's not going to meet that. What we need is a much stronger, more vigorous anti-fuel poverty strategy and we hope that if the judgement goes the right way in the High Court that the Government will feel obliged to actually do that.

LEWIS: So the courts will actually impose on the Government policies which it is saying it either can't do or can't afford at the moment?

KOHLER: The court cannot impose policies because it's a judicial review, but it can say you, the Government, are not dealing competently with the workload that you are supposed to be delivering.

LEWIS: And whether you win or not on Monday, if the Government doesn't take that action, briefly what would be the effect?

KOHLER: I think we will have to have another thought about where to go next, but the immediate effect is going to be that there will be millions of people in poverty this winter struggling to keep themselves adequately warm.

LEWIS: Mervyn Kohler from Help the Aged, thanks.

Well that's it for today. You can find out more from the BBC Action Line - 0800 044 044 - and of course our website, bbc.co.uk/moneybox, where you can download a podcast of the programme and let us know what you think about anything on today's programme. Personal finance stories, Working Lunch BBC2 weekday lunchtimes. I'm back on Monday with Money Box Live taking questions on maternity and paternity benefits and rights, and I'm back with Money Box next weekend. The editor of Money Box is Stephen Chilcott and I'm Paul Lewis.