

Part 2

VERBATIM NOTES

OF

COMMISSION OF ENQUIRY INTO CIRCUMSTANCES
THAT LED TO THE COLLAPSE OF THE FINANCIAL
INSTITUTIONS
IN THE 1990s

HELD AT

THE JAMAICA PEGASUS HOTEL
81 KNUTSFORD BOULEVARD, KINGSTON 5
ON

WEDNESDAY, 25TH NOVEMBER, 2009

1 control that, I don't know. But it represents
2 and -- let me indicate that I am intrigued by
3 some of the positions being taken but in
4 several of these instances that policy
5 position came as a result of discussions is
6 by both political parties so it wasn't a
7 controversial issue and it was extended and
8 we also negotiated it as part of the Agreement
9 with JRF. So I don't know whether he wasn't
10 aware of it or he just didn't apply.

11 Continued. .

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1 out of the house.

2 CHAIRMAN: All right. DEBTOR, one of our obligations
3 under the Terms of Reference is to review the
4 practices of the JRF and the treatment of
5 delinquent borrowers and, in particular,
6 the management, sale and/or disposal of
7 their assets so that whenever JRF comes to
8 give evidence those are the appropriate
9 people to question. All right. Any further
10 questions

11 DEBTOR?

12

13 A: I just want to know whether there was any
14 exception for people like me and others
15 maybe who were in the same position like me
16 and the kind of suffering that we are going
17 through and what can we do because right now
18 I am really suffering. I am almost living
19 on the street with me and my family and I
20 have been trying as hard as I can to save
21 my two sons from ending up in the group of
22 the unwanted because I don't have anywhere
23 to protect them, I cannot protect them, I
24 don't have anywhere to

25

1 live to keep them together as a family
2 as I used to. Because of that they tend
3 to go astray.

4 CHAIRMAN: Mr. Willis?

5 DEBTOR: Yes, sir.

6 CHAIRMAN: Nobody here can be other than
7 sympathetic towards your desposition and
8 to what question you are putting.
9 Unfortunately, we live in a practical
10 word and I don't really think that the
11 question can be asked of Dr Davies. He
12 is certainly no longer in government --
13 well, I shouldn't say that. He is no
14 longer Minister responsible for these
15 things.

16 Any comments you wish to make

17 Dr. Davies, perhaps you wish to...

18 A: Well, even though I am no longer in
19 government or whatever.

20 CHAIRMAN: Misuse of language, you are in
21 government.

22 A: His situation is something, both his and
23 the lady before me, I would carry out
24 private investigation, because both
25 should not have happened, both are

1 equally strange, so I will carry out my
2 own investigations.

3 CHAIRMAN: We will be grateful because afterall it
4 happened under your watch, so to speak.

5 A: There are some good things which
6 happened too.

7 CHAIRMAN: Yes, DEBTOR?

8 A: I think that is that for now.

9 CHAIRMAN: For the moment. Thank you very much.
10 think this is the hour when we take our
11 luncheon break so we will adjourn until

12 2 o'clock, and resume at 2 o'clock. If
13 there are any persons who wish to present
14 questions to Dr. Davies, will you please
15 put it in writing and hand them to our
16 Secretary. It is now time for adjournment.

17 LUNCHEON ADJOURNMENT TAKEN AT

18

19 12: ON RESUMPTION AT 2:05 P.M

20

21 Good afternoon ladies and gentlemen, the the
22 CHAIRMAN: afternoon session now commences, let's
23 resume. Dr. Davies, you are still on oath.
24 Mr. Secretary, have you got

25

1 any questions from the persons on the
2 floor?

3 MR. SECRETARY: No, Chairman, I have not.

4 CHAIRMAN: I don't know whether counsel wishes to
5 proceed.

6 MR. WONG KEN: Mr. Chairman, by consensus I believe I
7 am to proceed first.

8 CHAIRMAN: Mr. Wong-Ken, could you just announce
9 your...

10 MR. WONG KEN: Yes, Mr. Chairman, I wondered if a mike
11 was necessary or is it sufficient to --

12 CHAIRMAN: Use the other mike.

13 MR. WONG KEN: Good afternoon Commissioners. My name
14 is David Wong Ken and I represent the
15 Association of FINSAC'd Entrepreneurs.

16 CHAIRMAN: Thank you.

17 MR. WONG KEN: I apologise Chairman for not having
18 submitted the questions before. Dr.
19 Davies, how are you?

20 DR. DAVIES: I am fine.

21 Q: Good. When did you become Minister of
22 Finance?

23 A: In December, 1993.

24 Q: And if memory serves me correctly that
25 was shortly after election?

1 A: Well, the election, I believe was in
2 February 1993.

3 Q: Just so that I understand clearly your
4 expertise, what is your Doctorate in?

5 A: In Regional Economics from North Western
6 University.

7 CHAIRMAN: Sorry, I didn't get that answer. I must
8 confess, I am a little, what should I
9 say, a little shady in what that covers.

10 A: It looks at settlement patterns, it
11 looks at what they call location theory
12 as to optimal location of what we call
13 facilities but it was mainly a
14 Mathematical dissertation.

15 CHAIRMAN: Thank you.

16 MR. WONG KEN: When you became Minister of Finance,
17 what did you understand your job to be?

18 A: Well, I was Minister of Finance and
19 Planning and it covered a whole range of
20 the traditional areas of responsibility.

21 CHAIRMAN: Excuse me, Mr. Wong Ken, you can obtain
22 a copy of the transcript that was given
23 yesterday at nil cost, maybe you
24 can advise because we don't want to
25 have repetition, we did ask those

1 questions and he did respond and I don't
2 think you are quarrelling with his
3 qualification. Are you?

4 MR. WONG KEN: No, not at all.

5 CHAIRMAN: You can move on then.

6 MR. WONG KEN: Thank you. Have you at any time Dr.
7 Davies, made any examination, analysis,
8 enquiry into what caused what has become
9 known as the financial sector melt-down
10 in Jamaica in 1996 and the '90s?

11 A: Well, both in terms of my personal
12 exposure, but there have been numerous
13 analyses carried out by both local and
14 external institutions.

15 Q: And what do you understand to have been
16 the cause?

17 A: Well, I don't know whether the Chairman,
18 we dealt with -- do I continue sir?

19 CHAIRMAN: We have to remind ourselves.

20 A: Okay. There are a range of issues; the
21 inadequate legislation to govern the
22 actions or to facilitate the actions of
23 the regulatory agencies; bad management
24 practice in terms of just management,
25 sometimes practices which were

1 questionable as a euphemism but going
2 beyond bad management practices;
3 institutions venturing into areas in
4 which they had no expertise, a variety
5 of issues.

6 Q: Well, let's explore them a little bit.
7 Lack of regulation, and you are talking
8 lack of banking regulations.

9 A: Well it was much more than banking
10 because it was the financial sector.

11 Q: So lack of regulations over the
12 financial sector?

13 A: As adequate, yes.

14 Q: Whose responsibility would it have been
15 to properly regulate the financial
16 sector?

17 A: Well, in terms of responsibility there
18 are institutions but if you are talking
19 about ministerial responsibility it
20 would be the Minister of Finance.

21 Q: So it would have been at least since
22 December of 1993, your responsibility?

23 A: Exactly.

24 Q: When we speak about bad management
25 practices whose practices are you

1 speaking about.

2 A: The practices of the management of the

3 institutions.

4 Q: And by institutions now you mean the

5 financial institution?

6 A: Yes.

7 Q: Now, have you made any assessment as to what

8 percentage of the financial institutions

9 have been badly managed at the time of say

10 the melt down?

11 A: Well, to varying degrees, the Bank of

12 Jamaica, their audits and their inspections

13 revealed from various institutions

14 demonstrating practices so you had virtually

15 every institution from time to time. They

16 have a scoring system they call the 'camel

17 system' which they may assess institutions

18 in terms of -I don't know of any institution

19 which was perfect, some consistently did

20 well and some fell down in certain areas.

21

22 Q: Would it be correct to say or would you agree

23 with me if I suggested to you that by the time

24 of the closing of Century National Bank, that

25 perhaps 20% of the

1 existing financial institutions were
2 badly managed?

3 A: Well, I never thought of the percentages
4 because you can either count up
5 institutions just by number or you look
6 at them in terms of their size of the
7 market, et cetera. I don't know whether
8 your question was with regard to the
9 size of market or overall.

10 Q: What I am understanding from your
11 response is that there were many, many
12 institutions and that there were few
13 that represented the bulk, the heaviest
14 sector, big players then, as it were.

15 A: There were about four which represented
16 the bigger...

17 Q: There were many many more financial
18 institutions than four?

19 A: Oh, yes, there were many more financial
20 institutions but you have financial
21 institutions which were not formerly
22 regulated by the Central Bank, for
23 example.

24 Q: I am intrigued though, Dr. Davies, as to
25 why it was that there were so many

- 1 financial institutions, what caused
2 that?
3 A: Well, several were given licences. Part of
4 the Legislation which was tightend up on my
5 watch was the way in which a licence could
6 be disposed of; at one stage you could
7 literally sell a
8 licence.
9 Q: What would it cost for an individual or
10 group to form a bank, what was the entry fee?
11 I don't recall the capital thing but one
12 A: could establish a building society without
13 reference to the Minister of Finance.
14 And isn't it true that banks, when they are
15 created, are able to lend more than they
16 Q: have on deposits?
17 Well than the...
18 Well, I am not entirely certain of the
19 A: forensic language.
20 Q: No, no, I don't know what, apart from
21 their capital I don't know what
22 A: additional sums entail.
23 Let me rephrase that, I used the word
24
25 Q:

1 deposit, I really meant capital. I am
2 sorry.

3 A: Okay, it's a significant difference.
4 The capital, there is a ratio which is
5 allowed in that regard.

6 Q: So you would agree with me then, that
7 when banks are established money
8 literally gets created because the bank
9 is able to lend money that it really
10 doesn't have?

11 A: Mr. Wong Ken, I am very wary about
12 answering questions using technical
13 language and I am not clear whether you
14 are using technical language or, I
15 don't know how to respond. Let me
16 explain. It's particular. When you say
17 money is created, that has a very
18 precise meaning and I don't know whether
19 that's the meaning you wish to impart.

20 CHAIRMAN: You are saying money is printed, are
21 you?

22 Q: I am not saying money is printed. What
23 I am getting to, is that with the number
24 of banks that you have, the unregulated
25 entry as you put it, of building

1 2 societies, et cetera, what happened in the
3 1992 to '93 era was that we had a serious
4 A: inflation problem, didn't we? I am not
5 clear the linkages you are -Have you jumped
the previous question?

6 Q: No.

7 CHAIRMAN: Sorry, he will answer one question at a
8 time. What is the question, you asked a
9 question?

10 Q: The question is...

11 CHAIRMAN: We need some clarification.

12 Q: Would you agree with me that the with
13 the ease with which banks were created
14 that ease also had the effect of, or had
15 an inflationary effect on the economy?

16 A: You would have to take me a little
17 further, that is not a logical
18 development because a bank can really
19 lend, it has to actually lend real
20 money.

21 Q: Work with me, I am not an Economist.

22 CHAIRMAN: Or a banker.

23 Q: Nor a banker. If a bank is able to lend
24 more than its capital.

25 A: Yes.

1 Q: So a bank puts in capital of \$10, it
2 maybe able to lend legally \$15.
3 A: Or 20.
4 Q: Or 20.
5 A: Yes.
6 Q: Doesn't that fact have an inflationary
7 effect on the economy?
8 A: No, Mr. Wong Ken, because for them to loan
9 15 or 20 they would also have been taking
10 deposits and a bank has to lend in order to
11 make money.
12 Q: Okay.
13 A: But there would be real money placed
14 with that bank by real people.
15 Q: Okay. Would you agree with me that in 1992,
16 Jamaica's inflation rate was 80%? Well, I
17 A: would agree with you and I would go further
18 that in '91, '92, it was over a hundred
19 percent, but that had nothing to do with the
20 banks.
21 Q: When you took office, had you been able to
22 determine what caused that high inflation
23 rate?
24 A: I can tell you exactly what caused it. Tell
25 Q: me.

1 A: It was contingent on the liberalization
2 of the foreign exchange market and the
3 very, very rapid devaluation of the
4 Jamaican dollar and given that impact.

5 Q: Had it not significantly to do as well
6 with government borrowing money to
7 service the deficit, the budget deficit?

8 A: Not that inflation, no.

9 Q: You disagree?

10 A: Yes I disagree. The main cause was
11 devaluations resulting from the
12 liberalization.

13 Q: So the liberalization of the foreign
14 currency markets is what you attribute
15 to high inflation in 1992?

16 A: Yes.

17 Q: What steps did you take in 1993 when you
18 assumed office to correct this
19 inflationary problem?

20 A: I am glad you asked because it
21 represents -- I identified control of
22 inflation as my priority objective on
23 assuming office and I can trot out the
24 numbers if you wish but we targeted
25 that, not only for economic reasons but

1 to stabilize the labour market because
2 following that level of inflation
3 everybody was demanding increases
4 consistent with inflation, so that I
5 think recognized as one area of success
6 in terms of controlling inflation,
7 bringing inflation down and then
8 controlling it.

9 Q: When you made the analysis as Minister
10 of Finance in December of 1993 or
11 thereabout, had you informed yourself as
12 to what were the drivers of
13 deregularizing the foreign currency?

14 A: Deliberating.

15 Q: Deliberating.

16 A: Yes.

17 Q: And then without regulation?

18 A: We are linking foreign currency with the
19 inflation, but you are talking about a
20 separate issue, that of the banking
21 system and the inadequate regulation.

22 Q: I am linking the two because you have a
23 banking sector by your words, that was
24 not well regularized.

25 A: Regulated.

1 Q:

2 Regulated. And now we have a situation of
3 deliberalize or liberalization of foreign
4 currency. I am trying to get an

5

understanding from you because I don't

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know, I am trying to get an understanding

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from you how did those things result in the

8 A:

hyper inflation? You are making the linkage

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you know sir. I indicated to you that the

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main driver was the fact that such a rapid

11

devaluation took place and in a sense

12

because it was all new. The fact that the

13

fixed exchange rate before was really

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fictitious, so part of the change was due to

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the dollar actually finding a more realistic

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level but beyond that, added to that fact

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was just the uncertainty and people were

18

speculating. It would be fair then to say

19 Q:

that when the foreign currency was

20

liberalized, you didn't have the regulatory

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framework in place for the banks?

22

No, I have said that, but where I am not clear

23 A:

you are going is linking the banks to the

24

inflation.

25

- 1 Q: Would you lay the responsibility of
2 regulating the banks on your predecessor
3 Minister of Finance?
- 4 A: Mr. Wong Keng, I...
- 5 Q: You see...
- 6 A: I don't look in the rear view mirror, I look
7 at the problems which I face and then I
8 deal with them.
- 9 Q: It's just that you keep blaming banking
10 sector and I am a little curious as to why,
11 because what I want to put to you is that
12 the financial melt-down in the '90's
13 started from the inflation in 1992 and I am
14 coming to your steps to correct it.
- 15 A: Well, you could so proceed but the US, if
16 you wish to use the word, melt-down, is
17 taking place in the face of interest rates
18 of two and three percent.
- 19 Q: So you disagree?
- 20 A: No, I am just indicating that the simple
21 causation which you seek to establish is not
22 yet established.
- 23 Q: Let's explore it a little more. When you
24 came to the office, you recognized
25

1 as your primary objective getting
2 inflation under control, is that right?

3 A: Yes, and I am on record as saying so. It
4 was to the surprise of many persons but
5 it was my assessment that unless we
6 brought inflation under control
7 virtually everything else was out of
8 wack.

9 Q: What steps did you take to bring
10 inflation under control?

11 A: I would say in the main two. One, was
12 that there was a tighter monetary policy
13 and secondly, we looked at the fiscal in
14 terms of better control over
15 Government's fiscal accounts.

16 Q: I am going to ask to you to indulge me.
17 Explain this monetary and fiscal policy.
18 What is a fiscal policy, what is a
19 monetary policy, as succinctly as you
20 can?

21 A: As succinctly as I said, a country or
22 the government operates in terms of
23 expenditure. Most people say the budget
24 is read or you read the budget, they are
25 just focusing on expenditure, what each

1 sector gets, but there is a flip side to
2 that, its financing the budget, and that
3 financing comes from really two sources,
4 sometimes three, but grants are now neither
5 here nor there so it would really be tax
6 revenue and borrowing and the extent to which
7 the government is borrowing or the extent to
8 which the expenditure exceeds the tax revenue
9 then there is the need to fill the difference
10 by borrowing so we sought to look at the
11 fiscal deficit because that drives the
12 government's demand, certainly for
13 financing. In terms of the monetary policy
14 which effectively is carried out by the
15 Central Bank, they can seek to reduce the
16 money supply; there is somebody here who
17 spoke volumes on that matter and by
18 tightening money supply you make the cost of
19 money more
20 expensive for everybody, including the
21 government.

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Continued...

1 situation where there is the possibility
2 of capital flight.

3 Q: All right. In answer to the question
4 about what you did to reign in inflation
5 you said that you implemented certain
6 monetary policies.

7 A: Well my economic program had a monetary
8 stance consistent with the fiscal
9 stance.

10 Q: And did this monetary stance contemplate
11 what has been commonly called mopping up
12 of liquidity?

13 A: Yes, it does.

14 Q: And how did you go about mopping up
15 liquidity?

16 A: Well, the Central Bank has the power to
17 issue - above and beyond borrowing, the
18 Central Government's borrowing, the
19 Central Bank has the ability to issue
20 notes which then people would purchase.

21 Q: And those notes are called treasury
22 bills?

23 A: No. Treasury Bills are the Government's,
24 are the Ministry of Finance's notes.

25 Q: What are those notes called -- the ones

1 issued?

2 A: The BOJ, I don't know what they call
3 them, I don't know but the BOJ can issue
4 notes above and beyond Treasury Bills or
5 LRS's which are issued for the Ministry
6 of Finance.

7 Q: So the Ministry of Finance, quite apart
8 from...

9 CHAIRMAN: I take it, like the BOJ Repo?

10 A: Yes, and they may have them for
11 different periods. if they feel that
12 they have a short term crisis or
13 challenge then they would issue it for
14 like for 30 days or whatever and if they
15 think the challenge will last longer
16 then they issue it for longer periods.

17 Q: So quite apart from the Bank of Jamaica
18 being able to issue notes at what it
19 determines the interest rate should be,
20 the Government is also able to issue
21 Treasury Bills.

22 A: Well the Government issues -- well, we
23 have turned Treasury Bills into
24 essentially signal rates. In other
25 words, the amount raised from the

1 Treasury Bills really are insignificant.
2 We go for longer term notes but the six
3 months Treasury Bill is the signal rate.
4 So the Government would issue Treasury
5 Bills and LRSs and then the Central Bank
6 has various instruments it will offer.

7 Q: Could this have been 1994?

8 A: I don't understand the question.

9 Q: When you started this monetary policy to
10 mop up liquidity?

11 A: Well, I mean I didn't invent monetary
12 policy.

13 CHAIRMAN: The policy of mopping up?

14 A: I think the Central Bank has overtime
15 issued...

16 Q: When you answered the question earlier
17 you said you recognized as your priority
18 and and that one of the things you did
19 was to institute this monetary policy
20 and one of the policies was the mopping
21 up of liquidity?

22 A: No, no, I didn't say I instituted the
23 monetary -- what I indicated that was
24 part of the element. What we did, we
25 started targeting inflation and in

1 targeting inflation a critical element
2 is the money supply and the control of
3 money supply. So in targeting inflation
4 the Bank of Jamaica would take
5 certain -- we would know what are the
6 needs of the Ministry of Finance and
7 then the Bank of Jamaica would also
8 determine how much of that liquidity it
9 would have to absorb in order to achieve
10 the inflation target.

11 Q: And because you were part of the team
12 and the leader of the team that
13 determined monetary policy you would be
14 aware of the interest rates that were
15 being charged and in fact you would have
16 some influence, wouldn't you; interest
17 rates charged on the notes issued by the
18 Bank of Jamaica?

19 A: No. Well there are two ways of interest
20 rates, Mr. Wong-Ken. You could issue a
21 note and you could say, either the Bank
22 of Jamaica or the Ministry of Finance,
23 you could say I am issuing this note for
24 15 months at this price and if you have
25 called it right then there would be a

1 response, but sometimes you have
2 miscalculated what the market will
3 respond to; that's one way. The other
4 one is to do it as an auction. You
5 could say I have opened a 15-month
6 instrument, make a bid and then you
7 accept the bid so those who have money
8 will say I want 500 million at this
9 price.

10 Q: The question is, would you have known
11 and contributed to determining what that
12 rate is?

13 A: Which one?

14 Q: The rate of interest offered by the Bank
15 of Jamaica on its notes.

16 A: No, I wouldn't be involved in that but I
17 would know about it.

18 Q: But you would know about it?

19 A: Yes, I would know about it.

20 Q: And wouldn't you have had input into the
21 setting of rates offered by the
22 Government, the Treasury Bills?

23 A: This is a technical matter. I would be
24 informed but the Financial Secretary and
25 the team wouldn't come to me and say

1 what do you think the rate should be.
2 They are working consistent with an
3 overall macro program and they are also
4 working on a program which tells you
5 that at the end of the month they need
6 to pay salaries and pay bills.

7 Q: But don't be so modest, Dr. Davies, you
8 are a leader, you would have been
9 involved in these decisions?

10 A: Mr. Wong-Ken I take your compliment but
11 I run a team and if I say so myself that
12 it was a pretty good set of persons and
13 they took decisions.

14 Q: Having taken those decisions though,
15 your team having taken those
16 decisions...

17 A: Yes.

18 Q: If you recognized that the decision was
19 going awry or was causing some adverse
20 consequences, you would step in?

21 A: Yes.

22 Q: And you could call those shots. You
23 could say, "hey let's talk about this
24 and meet again and come to a different
25 situation?"

1 to know that there are times when the
2 Government was actually in surplus and

3 in those instances the Ministry of
4 Finance could contribute to liquidity
5 control by keeping that money in the
6 Bank of Jamaica.

7 Q: So when the Bank of Jamaica issued a
8 note it wouldn't issue the note so as to
9 secure money to pay for its activities?

10 A: No.

11 Q: It issues the note to pull in
12 liquidity?

13 A: Yes.

14 Q: To take in the excess money that is put
15 in the economy?

16 A: Right.

17 Q: And when the Government issues a
18 Treasury Bill it's really borrowing
19 money to meet its expenses?

20 A: Exactly.

21 Q: And in both cases, would you agree with
22 me that in the case of the Government,

23 the Government is competing now with
24 banks when it offers a Treasury Bill;
25 it's trying to extract money that

1 otherwise might have gone into the bank?

2 A: Most times the customer is the bank, the
3 purchaser of the bills are the banks.
4 But although bankers might think of
5 themselves as having money, they have
6 peoples money, depositors money.

7 Q: Well would you agree that when the Bank
8 of Jamaica says to the public, buy this
9 note, what the Bank of Jamaica wants the
10 public to do is to buy that note from
11 them rather than put the money into a
12 bank?

13 A: I don't think you have gotten me the
14 first time, Mr. Wong Ken. I don't know
15 what the average saving rate is,
16 whatever, so banks make money by
17 attracting savings at X. Part of their
18 making money, apart from making loans,
19 is that they attract savings at X, but
20 they buy Government paper or they buy
21 papers to finance other institutions at
22 X plus Y, so the banks or the financial
23 institutions was one of the main
24 entities purchasing the Government
25 paper. So the competition is not in

1 Most customers believe and I think the
2 banks have been quite ingenious in
3 conveying the impression that these
4 rates are imposed by Government. There
5 is a big spread between the cost of
6 money to the banks and what they charged
7 there.

8 Q: And that spread would be also impacted
9 by a bank's uncertainty of being repaid.
10 So for instance if a member of the
11 public went to borrow money it's going
12 to make that assessment.

13 A: Right. And the converse holds too, that
14 the interest rates which a bank offers
15 to depositors is a function of the
16 strength of the bank.

17 Q: Let me just recap a little bit. I just
18 want to make sure that I understand you.
19 When the Bank of Jamaica offers notes
20 and when the Government offers Treasury
21 Bills the effect of that is to drive
22 interest rates up between the bank and
23 its customers?

24 A: Not necessarily.

25 Q: I must have misunderstood.

1 over the duration of the loan?

2 A: No, and they can't be Mr. Wong Ken. A
3 loan agreement would be between a
4 customer and a bank. So it would be
5 almost impossible for the Government to
6 specify what each loan agreement would
7 be.

8 Q: When your team meets, and I imagine the
9 Planning Institute might have been
10 involved?

11 A: Integrally involved.

12 Q: And lack of resource, Government
13 resource of people and money to make
14 these analyses and these things?

15 A: I don't know about money but people,
16 yes.

17 Q: When these analyses are being made, can
18 you recall whether or not there was
19 consideration given to the effect of
20 this on *the* customers, the banks'
21 customers.

22 A: Well there was consideration of the
23 effect on the economy but it's not a
24 either or, because we also analyzed the
25 impact of what you term hyper-inflation

1 on the economy. So the issue was in
2 seeking to address one there are certain
3 consequences. The question was which
4 was the greater danger to the economy?

5 Q: All right, let me just getto gain some
6 context. 1992 during very high
7 inflation, the hyper-inflation 80% or
8 more. You come to office in December of
9 1993, you recognized that your priority
10 is to reduce inflation. One of the
11 things that you do is you start to mop
12 up liquidity and the primary way of
13 doing that would be the Bank of Jamaica
14 notes?

15 A: But I also indicated that the Ministry
16 of Finance also in tighter fiscal
17 management was a factor.

18 Q: And by tighter fiscal management what
19 you mean, just be able to pay your bills
20 on time?

21 A: You seek to collect as much as possible
22 and you are very cautious about
23 spending.

24 Q: But that clearly wasn't the case because
25 the Government during that period

1 continuously issued Treasury Bills?

2 A: The second statement is correct the
3 first one isn't.

4 Q: Which one of the statements wasn't
5 correct?

6 A: The fact that it clearly wasn't the case
7 that there was tighter fiscal
8 management. Tight fiscal management
9 does not necessarily imply a surplus.
10 The U.S. Government borrows. You have
11 several different countries which are
12 wealthy countries, they all borrow.

13 Q: Okay. So then notwithstanding the
14 tighter FISCAL management, the
15 Government was still unable to meet its
16 bills and had to issue Treasury Bills to
17 raise money to do that?

18 A: Yes.

19 Q: And your team and you recognized that
20 this would have had some adverse impact
21 on the customers of the banks?

22 A: I spoke to it more broadly on the
23 economy.

24 Q: Okay, so it would have had some adverse
25 impact on the economy.

1 high inflation.

2 A: Well, high interest rate occurred but it
3 was not the policy. The policy was to
4 bring the inflation down.

5 Q: High interest rate was a consequence of
6 the policy?

7 A: Of the intervention of the Central Bank
8 in terms of mopping up of liquidity.

9 Q: And had you not recognized that this was
10 having an adverse effect on businesses
11 in Jamaica?

12 A: And Mr. Wong Ken I have already answered
13 that question and pointed out that the
14 inflation rate of 80% was having a
15 disastrous impact not just on
16 businesses, on households, on the labour
17 market and that was identified as a
18 critical element.

19 Q: Okay. So then would you agree with me
20 that a collapse of the financial sector
21 was not so much a problem with the banks
22 but it was a problem of the economy?

23 A: I disagree with you because as I have
24 indicated and I think you would be aware
25 that there were other banks operating

1 within the same environment which didn't
2 collapse.

3 Q: How many banks didn't collapse, Dr.

4 Davies?

5 A: I can list you, apart from banks
6 collapsing there are security dealers
7 which didn't collapse. The Jamaica
8 National didn't collapse.

9 CHAIRMAN: No, but 70% collapsed?

10 A: He is asking me which ones didn't
11 collapse and I am just indicating.

12 Q: The Chairman has clarified it; 70% of
13 the financial institutions did collapse
14 did they?

15 A: Well you are making that assertion.

16 Q: I am taking it from the Chairman.

17 A: You are making that assertion. I am not

18 answering that question because I don't
19 have that percentage at hand.

20 Q: Tell me again, Dr. Davies -well let me
21 not go there. But you disagree with my
22 assertion though, that the economy
23 didn't collapse but the financial sector
24 did?

25 A: Well we have been quite loose in terms

1 of the terms. The reality is that there
2 is significant parts of the financial
3 sector which did not collapse and we
4 were able to intervene and bring back to
5 health, I don't know about the word
6 collapse.

7 Q: Dr. Davies isn't it true that the
8 customers were...

9 CHAIRMAN: Sorry, one moment. Let me understand.
10 Mr. Wong Ken is speaking about
11 significant factors?

12 A: Chairman, the fact is that at no stage
13 the financial system ceased operating;
14 trading went on, businesses went on,
15 foreign exchange trading went on,
16 people externally could do business with
17 Jamaica. So I think we have been
18 slightly loose in speaking about a
19 collapse. Collapse means mash up. The
20 fact is that institutions kept going
21 and even in the worse period, entities
22 kept trading, the foreign exchange
23 market kept going and so I must...

24 CHAIRMAN: Partially collapsed.

25 A: Well, I can't...

1 CHAIRMAN: Let me just say, I am not trying to be
2 semantic or anything like that because
3 there was indeed a situation where a
4 great many of the financial institutions
5 failed.

6 A: I agree, sir.

7 CHAIRMAN: Whether you want to use fail,
8 collapse...

9 A: But my problem Chairman, is when you
10 move to speak of the financial system
11 and my definition of the financial
12 system collapsing would be like you went
13 to a situation that you couldn't go to a
14 bank, you couldn't transfer money you
15 couldn't carry out transactions, and
16 that never occurred.

17 Q: Well, would you agree...

18 CHAIRMAN: One moment now. Nor was there a partial
19 collapse. There was, I think I would be
20 correct to say, massive intervention?

21 A: Well, yes, there was massive
22 intervention but part of that
23 intervention was to ensure that
24 operations could continue with some
25 degree of normality.

- 1 CHAIRMAN: Indeed, because there was a collapse of
2 some sort.
- 3 MR. WONG KEN: Dr. Davies even if you do not agree that
4 the financial sector collapsed, would
5 you agree that the economy collapsed?
- 6 A: No.
- 7 Q: Would you agree that there were
8 thousands of businesses that could not
9 service their bank debt?
- 10 A: Yes, I agree with that.
- 11 Q: And would you agree with me that their
12 inability to service their bank debts
13 arose significantly from the high
14 interest rates that resulted from the
15 Government's policy to bring inflation
16 under control?
- 17 A: Well, if you ask me whether some of
18 those who were unable to service their
19 debt the problem was the rate of
20 interest, I will agree but you have
21 coloured your question with some non
22 sequiturs.
- 23 Q: Well, point the colors out to me, Dr.
24 Davies, because I am really struggling
25 to follow this story?

1 maintaining certain things.

2 A: Well, we can look at the numbers, you
3 know sir. The numbers are available
4 from the Bank of Jamaica.

5 CHAIRMAN: We have it here that's why I am saying
6 that.

7 MR. WONG KEN: Dr. Davies, we started by recognizing I
8 think you have agreed with me, that in
9 1992, Jamaica's inflation was around
10 80%?

11 A: Yes.

12 Q: You have indicated that you recognized
13 your priority to be to bring that
14 inflation under control?

15 A: Yes, sir.

16 Q: You have agreed that those policies
17 resulted in high interest rates? You
18 have agreed that thousands of businesses
19 were unable to service their bank debts
20 because of the interest rate? I haven't
21 gone wrong yet, have I?

22 A: Well, let me indicate that clearly the
23 high interest rates would be one of the
24 factors but even in intervened
25 institutions, even in institutions that

1 weren't challenged there were persons
2 who had borrowed who serviced their
3 debts.

4 Q: Why are you so resistant though,
5 Dr. Davies, to the suggestion that what
6 has been called the financial sector
7 meltdown by 1996 really had its genesis
8 in the high inflation of 1992?

9 A: Because there are several other factors
10 Mr. Wong Ken, which have been
11 introduced, have been discussed at
12 length by the Bank of Jamaica
13 representatives, et cetera and would
14 seek to make a little bit more complex
15 your elegant cause and effect
16 relationship.

17 Q: I put it to you though Dr. Davies, that
18 your hesitancy is in putting the blame
19 where it belongs at the feet of the
20 Government of the day and its policies?

21 A: Well you could put it to me, but in
22 carrying out your analysis and your
23 cause and effect, Mr. Wong Ken you may
24 wish to consider the situation of
25 financial crises in other countries

1 which had low interest rates which would
2 seek to suggest that there are other
3 factors including bad management
4 practices. Why is it that in the U.S.
5 when they make this assertion and then
6 they show where bad management practices
7 have impacted on the health of
8 institutions, no one questions that?

9 CHAIRMAN: Sorry, the question is rhetorical.

10 Q: Dr. Davies, are you aware that the in
11 the 1970s the 1980s there were financial
12 collapses in both the UK and the United
13 States?

14 A: Yes, sir, I am aware.

15 Q: And you are aware no doubt that the
16 first approach was high interest rates,
17 you are aware of that?

18 A: Well I am not clear where you are
19 talking about.

20 Q: Well in the UK for instance when they
21 implemented the high interest rates to
22 bring inflation under control, within a
23 year and a half they abandoned the
24 policy and publicly made it known that
25 it was ruining us; you weren't aware of

1 those challenges?

2 A: No, I am not aware of those examples but
3 I am also aware that under Paul Volka
4 the Fed Chairman, they addressed the
5 inflation by increasing interest rates.

6 Q: Nonetheless you continue to resist this
7 notion that it's bad fiscal management
8 arising out of 1992, before your time,
9 that really resulted in the financial
10 sector meltdown.

11 A: Sir, I resist the notion.

12 Q: And you continue to hold the notion that
13 it's really bad management on the part
14 of the institutions?

15 A: Mr. Wong Ken, I have indicated that
16 there is no way I could disagree that
17 high interest rates represent a factor,
18 but i am saying that there are other
19 issues which are salient and should be
20 taken into consideration and these have
21 been documented.

22 Q: We touched on the question of the policy
23 of high interest rates and as you have
24 said the policy of high interest rates
25 were a consequence. We touched on the

1 contemplated duration. How long this
2 thing was contemplated to have lasted?
3 Can you say in terms of years what was
4 it that the government thought would
5 have been an appropriate time for this
6 high interest rate to have endured?
7 A: I can't recall any sort of estimate of
8 that time. But one of the difficulties
9 which we had faced was that in previous
10 periods there had been attempts to have
11 interest rates which were below
12 inflation rates and clearly any wise
13 saver recognizes that there is no point
14 in saving it even as you say the value
15 is reduced.

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1 DR. DAVIES: So part of the policy, overall policy,
2 was to have what they call the real
3 interest rate, meaning that the interest
4 rates are higher than inflation rate.
5 So one of the issues was how soon could
6 that be established and as inflation
7 rates came down interest rate should
8 come down.

9 Q: That situation where interest rates are
10 higher than inflation, is that what is
11 referred to as negative interest rate?

12 A: Where inflation is higher than interest
13 rate.

14 Q: That is negative, that is what you call
15 negative?

16 A: Yes.

17 Q: And in a situation of negative interest
18 rates, bank couldn't make money by
19 lending money, could they?

20 A: Well, it depends on what the cost of
21 their funds is but I am just saying that
22 if you have difficulty in attracting
23 savers who understand that their funds
24 are decreasing in purchasing power just
25 by putting them away, if the inflation

1 rate is higher than the interest rate.
2 Q: And wouldn't this be a reasonable
3 explanation as to why banks went into
4 enterprises that were not part of the
5 core business?
6 A: Mr. Wong Ken, I couldn't hazard a guess
7 as to what informed those decisions.
8 Q: Wouldn't it be reasonable, if you are a
9 bank and can't attract customers...
10 CHAIRMAN: I am sorry, this has to be probed
11 because it was put forward that the
12 banks went into businesses that in quote
13 'wasn't their business', I would assume
14 Minister -- sorry Dr. Davies -- that you
15 were aware that these organizations, not
16 calling them banks, because it was not
17 only banks that were getting into
18 business that is normally not banking
19 business, you were aware of that?
20 A: To be precise, I was aware that groups
21 were getting into business, so in other
22 words, you had these various financial
23 groups and arms of the groups...
24 CHAIRMAN: Some planting papaw and having mangoes?
25 A: And hotels.

1 CHAIRMAN: And hotels. From your point of view it
2 would be a novel posture?

3 A: Well, there was nothing illegal about
4 it, but...

5 CHAIRMAN: That is why I use the word novel?

6 A: But it led to certain -- for example,
7 when one of the groups, a company in the
8 group would acquire real estate and the
9 bank would finance that, now if you
10 don't do something with real estate,
11 this entity isn't able to service the
12 loan and that is how several of the bad
13 loans came into being.

14 CHAIRMAN: I am sorry, these banks, these
15 organizations had gotten into these
16 businesses to make money. That must be
17 a logical thing?

18 A: Well, yes, I will concede, but sometimes
19 its ego, you know, sir.

20 CHAIRMAN: Whether ego or not, the bottom line must
21 be that they want to make money and what
22 I am asking really is whether or not, as
23 Minister, you are aware that they were
24 getting into real estate, did the
25 authority ever carry out a survey to see

1 what the effect of that could be since
2 you are concerned with the welfare, I am
3 very concerned with your concern.

4 A: Well, one of the points I would like to
5 make, sir, is that even -- that is why
6 the legislation was tightened, but even
7 if you are concerned, these were not
8 financial institutions per se licensed
9 by the regulatory bodies and so the
10 holding company is just a company
11 although you may have holding companies
12 chaired....

13 CHAIRMAN: We accept that these were bodies that no
14 statute governed.

15 A: No financial statute, it's governed
16 under the Companies Act or whatever.

17 CHAIRMAN: At least they had no effect to control
18 over, under any statute, despite the
19 effort, you were aware of that?

20 A: Yes.

21 CHAIRMAN: Then now, as Minister, you see this
22 phenomena, I call it phenomena, what do
23 you do, do you carry out a survey, what
24 do you do?

25 A: Well, the Central Bank had kept the

1 matter under review and pointed out the
2 need for tightening the legislation
3 which would bring about the powers that
4 they now have. For example...

5 CHAIRMAN: Well, I am sorry, they took remedial
6 action after the horse had bolted and
7 you see, I asked my question, if I may
8 say so, if the Ministry is aware of this
9 curious, because it's being highlighted,
10 phenomena, it maybe be hindsight, that
11 these businesses, having gone into these
12 businesses and failed, everybody gets
13 very wise but before there was failure,
14 when the papaw getting bigger or the
15 mango riping or whatever, it struck, I
16 wonder, it would have struck the
17 Ministry of Finance that, what curiosity
18 these businesses are carrying on, in
19 terms of financial stability into the
20 country, a good thing, is it to be
21 encouraged, it isn't to be whatever.

22 A: Well, sir, two points, one is yes, it
23 was noted and it was -- the work in
24 terms of preparing or revising or
25 improving the financial legislation

1 didn't just begin with the crisis, it had
2 started before, but the Central Bank pointed
3 out that they had no authority to go beyond
4 or go above the level of the actual
5 institution which they supervise. They now
6 have that authority.

7 You see I get the impression that what
8 CHAIRMAN: happened nobody thought anything about

9
10

it.

11 A: That's an incorrect impression, sir.
12 CHAIRMAN: Very well, when it came to grief, I will

13 revise it if you convince me. When
14 people came to grief, you say, ah, I
15 will look into it but nobody foresaw
16 what the result would be.

17 A: Well, some of the developments couldn't
18 have been foreseen, but Mr. Chairman, I
19 don't know if -- you deal with the law
20 at the back end but getting legislation
21 passed in a democratic situation, for
22 example, many of the changes which we
23 have implemented, to use your term,
24 after the horse bolted, took an
25 extremely long time because there were

1 objections to the stringency of some of
2 these measures, so it's not that there was
3 nothing being done, but they had to be done
4 in a particular way and democracy may be a
5 noble objective but it can be time
6 consuming.

7 CHAIRMAN: Mr. Wong Ken, I am just wondering if we
8 could take a ten minute break at this time
9 to refresh ourselves.

10 MR. WONG KEN: As it pleases you, Mr. Chairman.

11 ON RESUMPTION:

12 CHAIRMAN: We resume ladies and gentlemen,
13 Dr. Davies, you are still on your oath.
14 Mr. Wong Ken you were on your feet.

15 Q: Thank you Mr. Chairman. Dr. Davies when
16 we broke we were speaking about the
17 banks' foray into area that did not
18 constitute their core business?

19 A: Yes, but I indicated to the Chairman
20 that it was not by the banks per se but
21 by other entities within their groups.

22 Q: And as Minister of Finance, had this
23 become concerning to you?

24 A: Yes, it was of concern to me.

25 Q: Earlier in your responses to me you had

1 indicated that where policy was going
2 awry, you as the Minister could step in
3 and change course as it were?

4 A: Well, in so far....

5 CHAIRMAN: I am sorry, just one moment, please, we
6 wish to have silence. If you have to
7 carry on seminars, debates, please
8 retire, we can't hear what is being said
9 as there is this rumbling.

10 Q: You were saying Dr. Davies?

11 A: I was indicating that insofar as these
12 investments were being carried out by
13 entities which were not financial
14 institutions and thereby regulated by
15 the Central Bank, there is nothing
16 within the legal powers to stop that, in
17 that the entity can borrow from whatever
18 financial institution and make these
19 investments, but it became our concern
20 when the loans were being obtained from
21 the financial institution within the
22 group.

23 Q: From the parent?

24 A: Right, but that could not just be
25 rectified by ministerial fiat because

1 being able to attract savers and we had
2 spoken about the Government competing
3 with customers of the banks insofar as
4 money was concerned?

5 A: When you say 'we', you mean you?

6 You and I.

7 A: I didn't speak about the Government
8 competing, you made reference to that.

9 Q: Perhaps I put a phrase to it, but we have
10 spoken about the fact that the Bank of
11 Jamaica was offering notes to the
12 public?

13 A: Yes.

14 Q: And wouldn't you agree that that was
15 competing with private enterprises,
16 businesses for money from the banks?

17 A: Yes, but I indicated that the banks
18 themselves were the clients too.

19 Q: Yes, the banks were the clients, so
20 rather than lend to the customers, the
21 bank is buying the notes from the Bank
22 of Jamaica, wouldn't you agree?

23 A: Well, the reality is that a bank will
24 only -- whilst a bank has up to now one
25 hundred percent certainty, or a client,

1 that they will be repaid by the
2 Government of Jamaica, it's not just a
3 matter of whether a client suggest an
4 interest in a loan, the bank has to
5 assess whether that loan is one they
6 would wish to make.

7 Q: I take it back, it wasn't a competition
8 at all, because the bank was guaranteed
9 one hundred percent repayment from the
10 Government whereas it wasn't from the
11 private sector?

12 A: Right.

13 Q: But in truth, the activities of the Bank
14 of Jamaica in issuing that note had an
15 effect on the available cash or had an
16 effect on the cash that was available
17 from the Bank to the private sector, do
18 you agree?

19 A: Yes, that holds internationally Mr. Wong
20 Ken, if the American Treasury issues
21 bonds....

22 Q: I am not fighting you on that.

23 A: Okay then we agree on that.

24 Q: Wouldn't you agree that the Government
25 issuing treasury bills would have the

1 same effect of taking up available cash,
2 cash that might have otherwise been
3 available to businesses?

4 A: I would agree but as I indicated there
5 is no guarantee that this cash would go
6 to the businesses.

7 Q: So when I suggest to you that the
8 Government is competing with the private
9 sector, I am not really being
10 disingenuous, am I?

11 A: You are not being disingenuous, there is
12 another way to look at it, there is
13 available amount of credit in the system
14 and part of the construction of the
15 macro economic programme is to determine
16 how much of that credit will be left for
17 the private sector which then determines
18 how the government will -- the size of
19 the Government's budget and how it will
20 fund its needs.

21 Q: So when a bank...

22 CHAIRMAN: Sorry, you are operating in a time of
23 scarce capital so to speak?

24 A: Yes.

25 CHAIRMAN: Government wants money?

1 split between the credit to be utilized
2 by the public sector, and that to be
3 utilized by the private sector, but
4 Mr. Wong Ken as you would be aware, it's
5 not every time that there is a request
6 made that the Bank would feel obliged to
7 lend, if there are no viable products it
8 will not be responsible for them to so
9 lend.

10 Q: Would you agree then, Dr. Davies, that a
11 bank being guaranteed a 40% return on
12 its money either by purchase of a Bank
13 of Jamaica note or a treasury bill is
14 guaranteed return is something very
15 difficult for a private sector entity to
16 compete against?

17 A: In terms of...

18 Q: In terms of borrowing that same money?

19 A: Well, there are certain activities which
20 supported this.

21 Q: You answered somebody's question
22 earlier, they had pitched it at one
23 hundred percent, whether any business
24 could survive at one hundred percent?

25 A: I said no.

1 Q: I am asking you, are you aware that if a
2 bank bought a treasury bill at 40%, its
3 on-lending to a customer, would more
4 than likely be in the range of 60%?

5 A: It what?

6 Q: It's on-lending to a customer for the
7 same money would be higher than that
8 40%?

9 A: Well, the fact is that whilst the
10 interest rate to the Government or paid
11 by the Government is a factor, its not
12 an ironclad relationship. One of the
13 problems is to reduce the spread.

14 Q: Well, what is your opinion, do you think
15 that a private sector business can
16 survive paying a bank...

17 CHAIRMAN: Sorry, we are getting a little Irish

18 here or something. I mean, the questions
19 being asked and the answers being given,
20 it really doesn't matter what the
21 Minister says because this is pure
22 mathematics, business and logics,
23 whatever the Minister says, so you are
24 dealing with at the macro level, not
25 system.

1 Q: But chair to the extent...

2 CHAIRMAN: I understand what you are asking.

3 Q: To the extent that the enquiry is aimed
4 at determining the causes...

5 CHAIRMAN: I am not preventing you, what I am
6 trying to make clear is that it seems to
7 me that you are asking the question at
8 one level but the Minister is
9 responding -- sorry, Dr. Davies is
10 responding at the micro-level, so that
11 we are a little -- because obviously it
12 must follow as night to day, that the
13 bank must charge within that range, that
14 spread, that is just logical, it seems
15 to me that is commonsense in other
16 words.

17 Q: Chair, that seems to be commonsense that
18 just didn't happen, it seems that there
19 is a need to...

20 CHAIRMAN: The Minister doesn't seem to think so,
21 maybe you better go on.

22 Q: Let me repeat the question here
23 Dr. Davies. The question is, in your
24 opinion, do you think a business, a
25 legitimate business, can survive with a

1 bank debt that carries an interest rate
2 of 40%?

3 A: Mr. Wong Ken, certainly that's not an
4 interest rate which one would recommend
5 for any perpetuity but there are
6 businesses which carried it and there
7 are persons who took a deliberate
8 decision to utilize as much of their own
9 resources as possible.

10 Q: I come back to the question which still
11 haven't answered and the question is,
12 how long did you envisage that this high
13 interest rate policy would prevail?

14 A: And I have answered Mr. Wong Ken, it may
15 not be the answer you wish but I
16 indicated that we --- our primary aim
17 during that period was to bring
18 inflation under control and as soon as
19 that was brought under control, then
20 logically the interest rate should come
21 down, the question is what time lapse
22 there was between.

23 Q: So you didn't, nor did your consultants
24 and advisers see that high interest
25 rates prevailing for long periods of

1 time and by long periods of time I am
2 thinking in excess of three years, you
3 didn't see that as being fatal to the
4 productive sector?

5 A: Well, I tend not to use words like fatal
6 to the productive sector, because there
7 were entities which faced challenges but
8 there were entities which, as I said,
9 adjusted, utilized more of their own
10 resources to finance operation.

11 Q: Dr. Davies, did you...

12 CHAIRMAN: I am sorry, but can we go to life, if
13 there is a plague, some people survive,
14 in a plague, if there is a plague some
15 people will survive.

16 Q: Sorry I can't hear. I actually have a
17 hearing problem Chair?

18 CHAIRMAN: I didn't know you were challenged; I am
19 saying even in a plague, you know,
20 epidemic then, some people survive.

21 MR. HYLTON: Mr. Chairman, the thing though, the
22 question posed, was it fatal to the
23 sector, that was the question that was
24 asked, not whether most people survive
25 or didn't survive, was it fatal to the

1 sector.

2 Q: The reference to the sector was
3 intentional Chair?

4 CHAIRMAN: I know, I am not clear about the
5 objection.

6 Q: Dr. Davies, had you received the advice
7 of consultants, be it local or
8 otherwise, that the prolonged period of
9 high interest would have been fatal to
10 the productive sector of the country?

11 A: Well, since you ask the question in that
12 way, no.

13 Q: Would you answer the question in the
14 spirit that the question was asked,
15 perhaps I don't know the correct
16 question because I was not in the
17 Ministry of Finance nor was I in
18 Government, but had you received advice
19 that ran contrary to the high interest
20 rate policy?

21 A: Well, Mr. Wong Ken...
22 CHAIRMAN: Well he did get advice, the evidence is
23 that he did, he said so.

24 A: But, Chairman, I objected to the
25 question because I have a difficulty

1 with questions being asked with fatal to the
2 sector, etcetera, I have a
3 difficulty with answering questions like
4 that, but apart ..

5 CHAIRMAN: Sorry, Dr. Davies, since you are in the
6 witness box, you can emphatically reject
7 it.

8 A: Well, that is what I am doing, sir.

9 CHAIRMAN: Good.

10 Q: A follow-up question, did it include any
11 reference to fatality, it had to do with
12 advice that was contrary to the high
13 interest rate policy that was being
14 pursued.

15 A: Mr. Wong Ken, as I indicated at the
16 beginning, that you are faced with a
17 host of problems, and we determined that
18 the prolonged period of high inflation
19 which could perhaps lead to hyper
20 inflation, as has been demonstrated in
21 several South American countries, can
22 not only lead to economic ruin but
23 social ruin particularly among the poor
24 and that is why we targeted inflation
25 controls and in that regard the policy

1 was targeted at the reduction of the
2 rate of inflation.

3 Q: Dr. Davies, in your earlier answers, I
4 think yesterday it was, you indicated
5 that you held various technical
6 positions, between February 1989 and
7 March 1993, I was Director General of
8 the Planning Institute of Jamaica. You
9 would have taken part in the decisions
10 that led to the hyper inflation of 1992,
11 isn't that true?

12 A: Well, I was certainly aware of the
13 involvement decision to liberalize the
14 foreign exchange system and that
15 decision Mr. Wong Ken was taken because
16 everybody but the Government of Jamaica
17 recognised that the foreign exchange,
18 the fixed exchange rate and the rigid
19 exchange system was not working, so the
20 decision to liberalize was taken because
21 the people had already liberalized the
22 system.

23 Q: The people?

24 A: The system had been -- everybody was --
25 in fact one of the revelations was that

1 the Central Bank had been buying foreign
2 exchange on the black market, on the
3 beaches of the North Coast and that
4 indicated that the system which the
5 Central Bank itself was supposed to
6 preserving, was being compromised by the
7 entity itself.

8 Q: Dr. Davies, I suggest to you that the
9 hyper inflation was really as a result
10 of the Government of Jamaica financing
11 its activities by treasury bills?

12 A: Mr. Wong Ken, the answer is no to that.

13 CHAIRMAN: Right.

14 A: No.

15 HER LADYSHIP: He said no. The answer was no to your
16 question.

17 Q: I heard. Dr. Davies, and correct me if I
18 am wrong, I am going from memory here,
19 the first financial institution that ran
20 into trouble was Blaise Trust, was it
21 not?

22 A: You mean during that period.

23 Q: Yes, and I think that was in 1995?

24 A: I don't recall -- well, Century had
25 always been having challenges but Blaise

1 was the one which was the first in this
2 period which was intervened.

3 Q: And you indicated earlier that as
4 Minister of Finance you started to
5 become concerned about the activities of
6 these banks as their groups involved
7 themselves in non-core business
8 activities?

9 A: Yes.

10 Q: When Blaise got itself in trouble and
11 you took the decision, and I am assuming
12 you did, correct me again if I am wrong,
13 you as the Minister of Finance, took the
14 decision to intervene and to take over
15 that bank, did you?

16 A: Well, I was advised and I recommended it
17 to Cabinet, but it was not a lone ranger
18 situation.

19 Q: And when you advised Cabinet at that
20 time, were you aware of any other
21 problems in the financial sector?

22 A: Yes, there are always problems in the
23 financial sector, you know Mr. Wong Ken,
24 even now although I am not the Minister,
25 I am aware of problems and people seek

1 my help to seek to resolve problems, so
2 there are always challenges in the
3 financial sector and the way I saw my
4 job as Minister was as much as possible
5 to seek to resolve them without a big
6 commotion.

7 Q: You had done a visit to somewhere in
8 England, I can't remember where it was,
9 it was well reported and on that visit
10 you indicated that Century National Bank
11 was the perfect bank, to put words in
12 your mouth because it was how you would
13 establish a bank, you recall those
14 comments?

15 A: I don't think it was England, I recall a
16 speech I made praising Mr. Crawford.

17 Q: And at the time you were praising
18 Mr. Crawford, were you aware of any
19 problem with the Century National Bank?

20 A: I was aware that he has had liquidity
21 problems prior to that, that is the
22 extent of what I was aware.

23 Q: And if you were aware at the time of his
24 liquidity problems or the bank's
25 liquidity problems, what was the purpose

1 of your making that speech in praising
2 Mr. Crawford and his bank?

3 A; Well, I made that speech because -- well
4 virtually all banks have liquidity
5 problems from time to time and I made
6 that speech because he indicated certain
7 initiatives in terms of assisting
8 different entities, schools, etcetera, I
9 made that speech in recognizing his
10 social responsibility and some of the
11 things he did were quite commendable.

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13 Continued. .

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1 3:55 P.M.

2 MR. WONG KEN: And were you not in fact attempting to
3 encourage people to bank with Mr.
4 Crawford, at that time?

5 A: That was not contained in the speech.

6 Q: But had you not recognized that people
7 would have been encouraged by your
8 comments and in fact would put money
9 into Mr. Crawford's bank as a
10 consequence of your assurances?

11 A: I have never had that assumption of the
12 impact of my words.

13 Q: You agree that it was not a year later?
14 CHAIRMAN: Well, I don't know if that was a year

15 later. You say he was making a speech,
16 Ministers don't make speeches without
17 some purpose, I would suggest.

18 A: Well, I don't know about that, sir.

19 (LAUGHTER)

20 CHAIRMAN: Well, we are happy for the revelation.

21 A: I have heard many recently which I am
22 seeking a purpose for.

23 (Laughter)

24 CHAIRMAN: I don't know to what extent you can

25 respond that if you make a speech, as I

1 understand, relating to the Workers
2 Bank, that that might not encourage
3 persons who are, let me say, making up
4 their minds whether they should or not,
5 that you might well tilt the scale.

6 A: Well, I don't I think that's the
7 question posed by Mr. Wong Ken.

8 CHAIRMAN: I am...

9 A: I wish you could extend to me some of
10 that support.

11 CHAIRMAN: Regrettably, you have to answer the
12 question.

13 A: I know, sir.

14 CHAIRMAN: We want to get at what he wants. The
15 question is already put. Yes, I suspect
16 that's what Mr. Wong Ken would like to
17 know.

18 A: If I thought that I would have
19 influenced people to...

20 CHAIRMAN: You know, as Minister -- I mean let's
21 face it, the reason why I called you and
22 not Mr. So round the corner, is because
23 you are the Minister. These are
24 inconvertible facts. The fact of the
25 matter, this is impatient of debate.

1 When you go to make a speech people
2 listen to you carefully. I mean you are
3 not the Minister of Fisheries.

4 (LAUGHTER)

5 You are the Minister of Finance.

6 A: I wouldn't want you to give the
7 importance of that.

8 CHAIRMAN: What I mean is they didn't invite the
9 Minister of Fisheries talking about a
10 bank or about finance. They logically
11 invite the person who is responsible and
12 whose words mean something. And so the
13 question really is, being in that
14 position you would be conscious, would
15 you not, that your words might well
16 influence people who are cheating of a
17 desire, so to speak. For instance, they
18 might be aware, like you, of the
19 liquidity problem, but to say, the
20 Minister say so and so himself, I mean
21 he wouldn't say so unless he had some
22 confidence there so I am relying on him.

23 A: I answer you Mr. Chairman two ways, one,
24 I take the validity of your point made,
25 could have influenced, but the second

1 part is that at no stage, either as
2 Minister and even now, do I ever
3 discussed -- well when people ask me
4 what you think of such an institution, I
5 have never ever discussed that
6 institution as a matter of -- for the
7 same reason which you indicated.
8 CHAIRMAN: Thank you very much. Yes, does that
9 assist you, Mister...
10 MR. WONG KEN: Yes, Chairman, thank you very much. Dr.
11 Davies, isn't it true that it was less
12 than twelve months after praising Mr.
13 Crawford and his bank that the
14 Government took over Century National
15 Bank?
16 A: Well, you have...
17 Q: Dr. Davies, this is a seismic event in
18 Jamaica's history, don't you recall it?
19 A: I don't recall the issue of when I made
20 a speech and date. If you give me the
21 date but...
22 CHAIRMAN: You remember the words or the sense of
23 the speech?
24 A: No, he is speaking about the time span,
25 Mr. Chairman.

1 MR. WONG KEN: What event caused you to come to the
2 conclusion that the Government of
3 Jamaica had to intervene and take over
4 Century National Bank?

5 A: Not one event, several occurrences, one
6 is when it was recognised that the bank
7 faced, what seemed now to be chronic
8 liquidity problems.
9 Secondly was when the bank had been
10 called in first by the Bank of Jamaica
11 and subsequently by me to indicate steps
12 which needed to be taken to which Mr
13 Crawford agreed.
14 Thirdly, when these commitments
15 were not carried out.
16 Fourthly when Mr. Crawford
17 indicated that he was on the
18 verge of having significant
19 additional capital injection and
20 these didn't materialise. I
21 don't which number I am at.

22 Q: It doesn't matter. Go ahead.

23 A: Whatever the next number is, when Mr.
24 Bligh, who was then a Director and
25 co-investor in the bank indicated to me

1 and to the officials at the Bank of
2 Jamaica, that many of the decisions
3 which Mr. Crawford had conveyed to us as
4 having been taken by the Board had not
5 been taken by the Board and he was
6 hearing about them when I summoned the
7 whole Board. So there is no one event,
8 and I think the Bank of Jamaica has
9 chronicled all the steps which we took
10 in terms of dealing with Mr. Crawford.
11 But the critical issue is that the sum
12 total is that having gone through all
13 these different interactions I did not
14 find that he was worthy to be trusted
15 and the things that he had committed to
16 do had been done.

17 Q: At the time of the Government's
18 intervention and take-over of Century
19 National Bank, had you formed an opinion
20 as to the condition of the rest of the
21 financial sector and its viability?

22 A: Not in total but it caused us to --
23 because of what we discovered about the
24 relationship between Century and several
25 other institutions including Blaise, we

1 realised that there was a -- it's not
2 coordinated, but there is similarity in
3 the institutions in terms of their modus
4 operandi and the extent to which the
5 problems which we saw in one, there were
6 certain bad debtors which appeared in
7 the set of institutions.

8 Q: Wasn't the overriding similarity the bad
9 debt portfolio of almost all the
10 institutions?

11 A: It was one critical one, but there were
12 others in terms of -- and perhaps the
13 overriding similarity was the way in
14 which the resources were managed.

15 Q: But the bad debt portfolio was very
16 significant?

17 A: Yes, it was very significant.

18 Q: So we have come to a point where you
19 have agreed with me that hyper inflation
20 was rampant in 1992, that you
21 aggressively undertook the reigning-in
22 of inflation which had the consequence
23 of high interest rates? You said that
24 there were attempts made to reduce
25 interest rates but for whatever reason

1 it could not be done.

2 A: No, I don't recall saying that. I
3 didn't say that.

4 Q: In answer to one of the
5 questions
6 relating to the time...

7 A: You asked me if I had a precise time,
8 and I told you that this is not
9 something which you could say this will
10 happen in this particular period but if
11 you are to have real interest rates they
12 can only come down as inflation came
13 down.

14 Q: Okay. We have come to an understanding
15 that the Government was
16 competing with the private
17 sector for available bank money,
18 and you have agreed with me that
19 the high interest rate would
20 have an adverse effect on the
21 private sector's ability to
22 service its bad debts and now we
23 have come to the conclusion that
24 one of the significant
25 similarities in all of the
financial institutions was its

1 bad debt portfolio?

2 A: Yes.

3 Q: Do you still resist the suggestion that
4 the genesis of this melt-down was really
5 in 1992?

6 A: Yes, Mr. Wong Ken, I resisted then and
7 I resist now.

8 Q: Do you still resist the suggestion that
9 this wasn't a banking sector problem as
10 so much a problem with the viability of
11 the economy itself?

12 A: Well, you are making reference for the
13 first time what I resisted.

14 Q: Okay. When you realised the similarity,
15 the problems of a similar nature in the
16 financial sector, had you as Minister
17 of Finance, come to a decision on how to
18 deal with it? Had you in fact by the
19 time you took over Century recognised
20 that you would have had to form an
21 entity such as a FINSAC?

22 A: Mr. Wong Ken I had an extensive -- that
23 question was the opening question sent
24 to me by the Commissioners -- we had an
25 extensive discussion. To summarise, when

1 we realised that they had an extensive
2 problem we engaged over a period
3 discussions with the multi-laterals
4 given that they would have had
5 experiences similar, and those went for
6 a period, and we determined -- we got
7 advice from them, some of the points of
8 advice we accepted, others we didn't,
9 but we determined -- and then I
10 consulted with some overseas Jamaican
11 Economists, most notably Dr. Gladstone
12 Bonnick, and from that emerged the
13 decision for a generic intervention
14 using an institution such as FINSAC.

15 Q: And when you formed that conclusion, had
16 you also formed a conclusion as to the
17 cost of the intervention to the Jamaican
18 taxpayer?

19 A: There are various estimates all of which
20 turned out to be underestimates because --
21 apart from the extent of the visible bad
22 loan portfolio, what we discovered within
23 the groups was that there had been
24 attempts, successful attempts to conceive
25 the extent of the

1 debt such that all the estimates were
2 low including those from the external
3 institutions.

4 Q: Do you recall what your initial estimate
5 was that you announced in Parliament?

6 A: I don't recall the announcement, I
7 don't recall the announcement, but we
8 thought it was something in the region
9 of 20% of GDP.

10 Q: 20% of GDP. Would I be correct to
11 suggest to you that you had estimated
12 the cost to be 20 billion Jamaican
13 dollars?

14 A: I don't recall exactly. If I knew I was
15 going to be quizzed on my speech I
16 would have checked -- is that something
17 you are certain of?

18 Q: I am not at all certain of.

19 CHAIRMAN: Have you got the speech?

20 Q: No, sir. Do you as Minister of Finance
21 recognised that there were weaknesses in
22 the Ministry in respect to the lack of
23 banking regulation that persisted
24 through '92, perhaps to '98, was it?

25 A: Well yes, and as I indicated to the

1 Chairman, there was and there is ongoing
2 work in terms of revisions to the
3 Financial Legislation. There is still
4 work to be done.

5 Do you accept that a large part of the
6 result which is the financial sector
7 melt-down, I put it more liberal, the
8 economy, but the financial sector melt-
9 down, that a large part of that was due
10 to the lack of regulation?

11 A: It was a significant contributor but
12 even in the best regulated systems if
13 there are persons out to...

14 CHAIRMAN: Eg.?

15 A: To...

16 CHAIRMAN: Eg.?

17 A: Of what?

18 CHAIRMAN: Best regulated.

19 A: Britain is a very good example; if you
20 were...

21 CHAIRMAN: I thought you were going to say the
22 US.

23 A: No, because I would suggest that our
24 regulatory system is stronger than the
25 US.

1 CHAIRMAN: They have none.
2 A: Eh?

3 CHAIRMAN: They have none.
4 A: Their problem is regulatory arbitrage
5 because in certain instances State laws
6 dominate over the Federal laws and so
7 you can get around....

8 CHAIRMAN: It shifts.
9 A: Yes. So even the best of regulatory
10 systems....
11 CHAIRMAN: Mr. Wong-Ken, I suspect you have more
12 questions, a great many questions to
13 ask.
14 MR. WONG KEN: I suspect Chair, that I would need
15 another hour.

16 CHAIRMAN: Yes. But then..
17 MR. WONG KEN: The interesting thing is that I thought
18 I only would only have needed an hour to
19 start but the answers have been so
20 interesting and the answers have led me
21 in so many different ways. And I
22 apologise to my learned colleagues
23 because I did tell them that I would be
24 about an hour. I really do apologise.

25 CHAIRMAN: That prompts me therefore to make my

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announcement. I will take a rest and we will
all benefit from it. Very well, we will
adjourn and resume tomorrow morning at 9:30.
Mr. Wong Ken and Dr. Davies, tomorrow morning
at 9:30.

(ADJOURNMENT TAKEN AT 4:20 P.M.)