



The banking crisis: cause and effect

Nationalising the banks

Narrator

When it looked as though contagion could spread throughout the entire financial system, the government stepped in, wholly-nationalizing Northern Rock, part-nationalizing others and taking significant stakes in Royal Bank of Scotland and Lloyds.

Vince Cable

If the Government hadn't intervened at that point, with fresh capital for the banks and guarantees, the banking system would have gone. I mean it was actually that close.

Paul Mason

They had to save the banks. George Bush was absolutely right. As he put it: "We gotta get some money into the system, soon otherwise this sucker goes down."

Narrator

Despite taxpayer's money being used to prop up the banks, the country was nevertheless plunged headlong into recession.

Martin Wolf

"There are very big costs with very large banks, in that they are very powerful and they start looking what's called 'too big to fail', so you have to prop them up.

Global banks are pretty well bound to be very, very large institutions. In some cases the result is that a bank gets incredibly big relative to the domestic economy.

That's of course the most famous example recently is Iceland but it's also been true for the UK."

BBC News archive sync

The eruption in financial markets across the world now threatens Iceland with national bankruptcy. Just over 300,000 people live here - the gross domestic product is ten billion pounds but its financial institutions owe a staggering £50 billion pounds. Its estimated banks here have estimated British deposits worth 8 billion pounds and Iceland, already on its knees, is being asked to give the money back.

Narrator

Ultimately, individual UK investors lost nothing in the Icelandic collapse, though many councils and businesses wrote off millions.

The major impact came when RBS and Lloyds had to be rescued at the same time as the government had to bail out part of Bradford & Bingley.

The cost of supporting the UK banks would run to nearly a trillion pounds, many were angry that the Tripartite System of the Bank of England, The Treasury and the FSA had failed to foresee the impending collapse.

Vince Cable

"The Financial Services Authority made a complete and absolute mess of this crisis.

They didn't see the problems in the banking system, didn't act. Northern Rock, HBOS, RBS, they were sitting in front of them, they were looking at the evidence and they didn't react to it."

Narrator

These failures in the regulatory system and the lack of clear accountability raise the question of where the balance of government regulation should lie.

Larry Elliot

"We've had the crisis and now we have to decide what we want to do about the banking system going forward.

There is going to be tighter regulation; the FSA is going to be crawling all over banks and other financial institutions, and there will be tighter capital requirements.

But I think that the Keynesians, the people who believe that the government has a role to play, have won that argument hands down in the last two years."

Lord Skidelsky

"I think we have to get back to a more activist role for government, a more activist role for regulation and then we can avoid some of these falling into the foxhole as often as we have been doing. That would still leave a very large scope for market forces; I'm not suggesting we go into socialism, or communism or anything like that – there'd be a wide area for decentralised markets - but we've just got to limit the amount of damage they can do because otherwise it's much too expensive very very costly for individuals, normal ordinary people.