

FRANÇOISE NICOLAS; ELIANE MOSSE

Economist, Senior researcher at the Centre Asie of IFRI; Economist, advisor at IFRI for the Franco-Austrian Center for European convergence

Credit crisis, financial crisis, economic crisis: what to do?

Interventions and questions/answers addressed the following issues:

- Specific aspects of the crisis
- Sources of the crisis
- Contagion to the real economy
- Governments' responses

1 ° The current crisis is the worst since the crash of 1929. Its various manifestations (bankruptcies of banks and financial companies, collapse of stock prices, global "Credit Crunch", explosion of the real estate bubble in some countries...), the duration of these events, their rising intensity and their gradual expansion throughout the whole world are much deeper than in the financial and real estate crises of the 1980s and 1990s, which hit the United States, Latin America, Asia and, to a lesser extent, Europe. This is probably because a general lack of confidence compounds the objective factors which triggered the crisis.

2 ° The reasons of the crisis are numerous: deregulation and increasing sophistication of financial instruments, especially derivatives, with the use of leverage effect, multiplication of operators working without any regulations and screening of the nature and the results of the operations being undertaken, abundance of liquidity promoting risky investments. The United States played a key role in triggering the crisis, with abundant funds distributed to borrowers to purchase their homes, without taking account of their ability to repay, with interest rates very low or even zero at first, but growing strongly afterwards (the "subprimes"). More generally, the country lived beyond its means during the years of strong growth, with negative saving ratios. In this regard, it is possible to say that the strong U.S. performance in terms of growth in recent years was "artificial."

3 ° Even if the speakers agreed on the intensity of the financial crisis and on its likely duration (perhaps until the end of 2009), most of them reckon that it will not have the same effects on the real economy as the 1929 crash: there will be a recession, particularly due to the lack of credit available for businesses and households and to the difficult return of confidence, with inevitable impacts on employment, but not a depression with widespread deflation accompanied by a massive decline in prices, foreign trade, etc... as was the case during the big depression. This (cautious) optimism is particularly linked to the feeling that emerging economies can play a role in supporting global growth: they continue to grow at a steady rate and may in part offset the decline of activity in developed countries, but only in part: in this regard, the case of Asia has been singled out. The "decoupling" mentioned by some is not yet a reality because of the low economic weight of Asia (excluding Japan) in world GDP and its high dependence toward western markets.

4 ° If the scenario of a depression is not likely to materialize it is also thanks to the systematic dialogue of political and monetary authorities, whereas after the crash of 1929 policies were exclusively directed towards what seemed useful to each of the countries. Today, after a few mistakes and inconsistencies (financial companies assisted or "nationalised" or left to their fate...) the U.S., with the adoption of the Paulson plan, has taken steps which should, after a few weeks of implementation, have effects and restore confidence, but everything depends of course on the policies of the new administration. In Europe as well, after uncoordinated actions, where countries seemed to play their own games (words pronounced on 7th of October), co-ordination has emerged and should be fruitful.

The current crisis is no doubt very serious, although we cannot anticipate its full effects, however we can be sure that it may hit the poorest countries (reduction of foreign aid, market restrictions) and the poor in developed countries: a US-participant in the audience reported the sharp rise and the plight of homeless people in his country. One can also fear that in a climate of increasing poverty and unemployment, political radicalisation might occur, and jeopardize the way democracies operate.