

GLOBAL FINANCIAL AND ECONOMIC CRISIS: HIGH VULNERABILITY STATES

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Are crises rare?

Eichengreen & Bordo:

- 139 financial bubbles 1973-97
 - out of which 44 in developed countries
- Only 44 between 1944 and 1973

However:

- This is the first global crisis (Mexican, Far East, Russian all local crises)
- Massive in size

Current bailout at \$4.6165 trillion larger than

- Marshall Plan: Cost: \$12.7 billion, Inflation Adjusted Cost: \$115.3 billion
- Louisiana Purchase: Cost: \$15 million, Inflation Adjusted Cost: \$217 billion
- Race to the Moon: Cost: \$36.4 billion, Inflation Adjusted Cost: \$237 billion
- S&L Crisis: Cost: \$153 billion, Inflation Adjusted Cost: \$256 billion
- Korean War: Cost: \$54 billion, Inflation Adjusted Cost: \$454 billion
- The New Deal: Cost: \$32 billion (Est), Inflation Adjusted Cost: \$500 billion (Est)
- Invasion of Iraq: Cost: \$551b, Inflation Adjusted Cost: \$597 billion
- Vietnam War: Cost: \$111 billion, Inflation Adjusted Cost: \$698 billion
- NASA: Cost: \$416.7 billion, Inflation Adjusted Cost: \$851.2 billion

THE FINANCIAL CRISIS SO FAR...

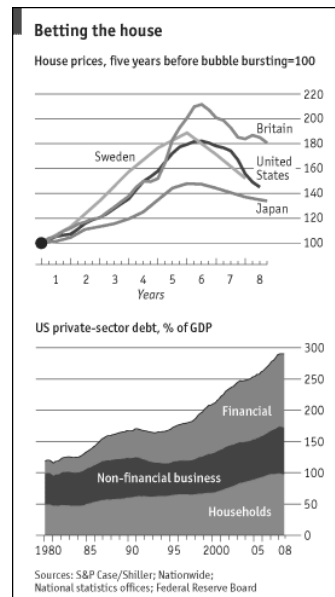
A series of interlocking bubbles:

Asian capital surplus flowing to US and UK, Eire, Spain

- Property bubble
 - Mortgage bubble (+subprime lending)
 - Securitization bubble
 - Household borrowing
 - National debt
- +
- Shadow banking system
 - Crony finance (Madoff, etc.)
- +
- Dollar bubble?

Property prices

Rally of property prices (bubble) leads to increased borrowing of households in US, UK, Eire, Spain, etc.



US household borrowing

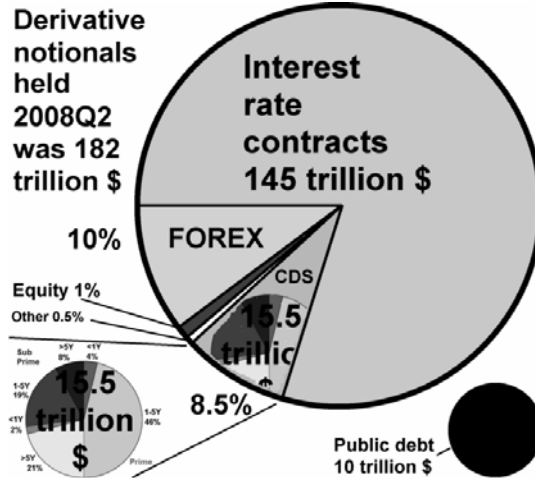
- 1990: 77% of yearly disposable income,
2007: 127% of yearly disposable income

or

- 1980: 100% of GDP
2007: 173% of GDP

Securitisation

Credit Default Swaps (CDSs) created leverage for further mortgage lending



Collapse of financial markets

- Glass-Steagall Act (1933), repealed by Gramm-Leach-Bliley Act (1999)
- Investment and commercial banks merge (already a shadow banking system)
- Growth of securitisation
- Goldman Sachs, Merrill Lynch, Morgan Stanley, Lehman Brothers, Bear Stearns.

BUT

US financial system:

10% of total corporate profits in 1980

40% of corporate profits in 2007

14% of GDP in 2007

FROM THE FINANCIAL MARKETS TO THE REAL ECONOMY

Global decline

- IMF forecast: Global economic growth down to 0.5% in 2009 from 2.5% in 2008
- USA, UK, Eurozone, Japan all in decline
- Global trade decrease first time in 20 years

Four main groups of vulnerability:

1. Property bubble: UK, US, Eire, Spain, Latvia
2. Financial sector vulnerability: UK, US, Eire, Iceland
3. High debt countries: Hungary, Greece, Italy
4. Low credibility economic policies: Latvia, Ukraine, Hungary
5. Loss of export markets: Far East, Eastern Europe , Germany

Financial sector vulnerability

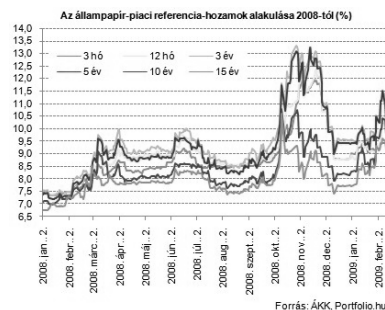
- Global financial centres
- Iceland: small country, foreign landing of banks 10x GDP

High debt vulnerability

2008.q3	Banks	Other sectors	Total private	Government	Total
Belarus	5.6	14.5	20.1	3.9	24.0
Poland	10.9	13.6	24.5	15.1	39.5
Czech Republic	12.8	14.8	27.5	8.7	36.2
Russian Federation	12.5	17.1	29.5	2.1	31.6
Slovakia	18.9	12.3	31.2	11.5	42.7
Ukraine	25.1	26.4	51.5	8.4	59.9
Hungary	38.1	16.7	54.8	32.6	87.4
Lithuania	37.2	17.9	55.2	9.9	65.0
Croatia	19.6	40.9	60.5	17.0	77.4
Bulgaria	27.1	36.0	63.1	8.3	71.4
Slovenia	49.3	24.7	73.9	10.0	84.0
Estonia	64.3	27.6	91.9	2.9	94.7
Latvia	84.9	27.2	112.1	6.2	118.3

Low credibility economic policy:

- Hungary: Gyurcsány, Bajnai, Orbán
- Latvia
- Ukraine: Timoshenko
- IMF bailouts



Loss of export markets:

- Germany: world's largest exporter, feels loss of US and global demand
- Eastern Europe: very export oriented economies, main market Western Europe
- Far Eastern economies: Taiwan, even China slowing down

***Thank you for your
attention!***

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