

# Ten Years after the Global Financial Crisis: what have we learned and what did we forget?

**#LSEfinance**

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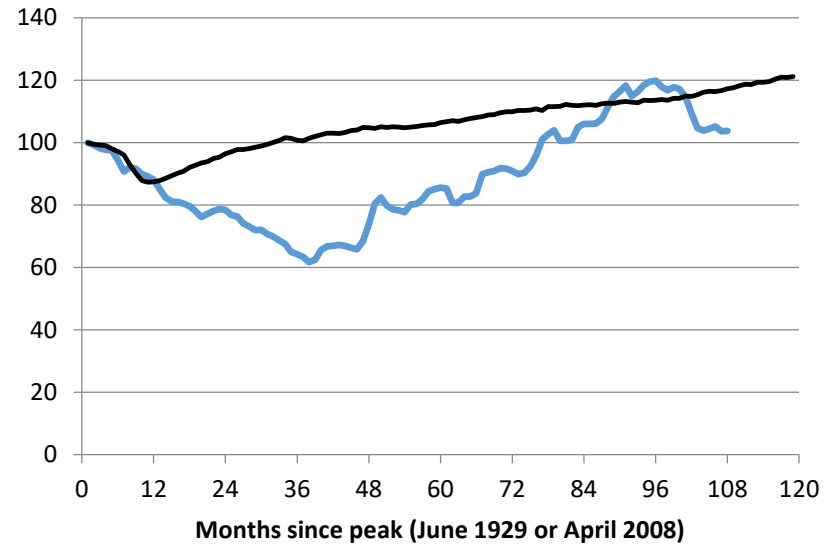
# Ten Years after the Global Financial Crisis: what have we learned and what did we forget?

Professor Catherine R. Schenk  
University of Oxford

# What did we learn?

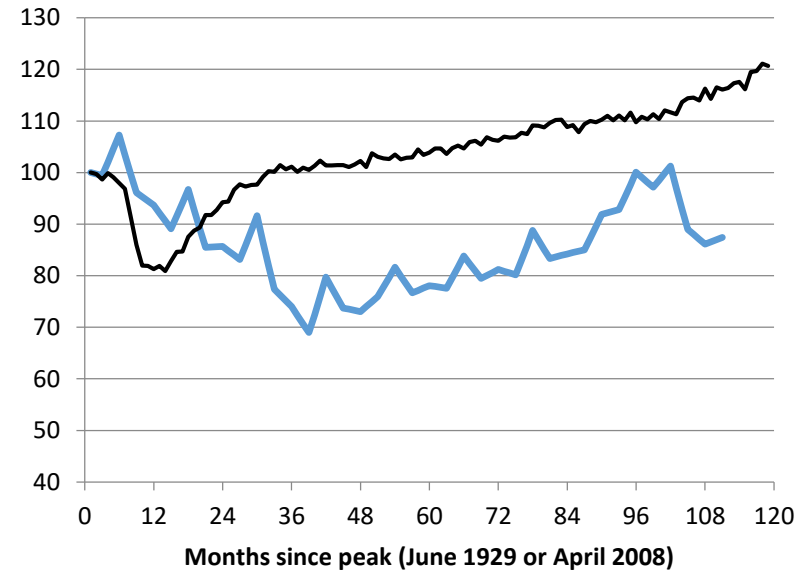
- Many recent reviews of events 10 years ago
  - Hindsight – why were governments so complacent, regulators so blind, bankers so greedy, home-buyers so irresponsible?
- ➔ Reinvigorated focus on (macro)-prudential supervision: but pro-cyclical policies  
Reinvigorated focus on micro-prudential supervision: less tractable
- Key uses of the past based on 1930s (Bernanke, Kindleberger, Eichengreen et al)
  - 1930s Sovereign Debt/War Debt, Asset Market shock, Financial Crisis, Agricultural Slump
  - Lack of US leadership
  - European Financial Crisis: Ten years after = World War II
- Fiscal expansion (short-lived and risky)
- Monetary expansion (QE – now 10 years old)
- Regulation: Basel III and Dodd Frank
- International Cooperation

### World Industrial Production



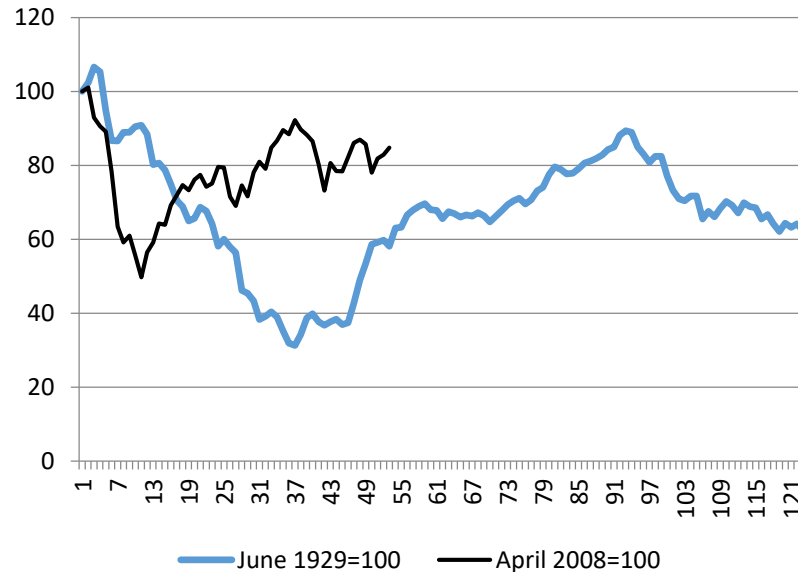
— June 1929=100 — April 2008 = 100

### World Trade



— June 1929 = 100 — April 2008 = 100

Source: Eichengreen and O'Rourke  
VoxEU (2010)  
'A Tale of Two Depressions'  
[O'Rourke: updated June 2018]



### Equity Markets

# Neglected Uses of the Past

- ‘Currency wars’ of 1930s: competitive devaluation (**currency manipulation**)
- Governance of the Global Economy: 1930s crisis inspired the **Bretton Woods System** and the International Monetary Fund/World Bank
  - Capital controls, pegged exchange rates, global source of liquidity for ST deviations from equilibrium
  - Global Financial Safety Net: 1970s vs 2010s
- 1930s trade shock/turn to **protectionism** not fulfilled (yet)
  - The ‘Great Reversal’ of globalization (Rajan and Zingales 2000-2004)

# Currency Wars today?

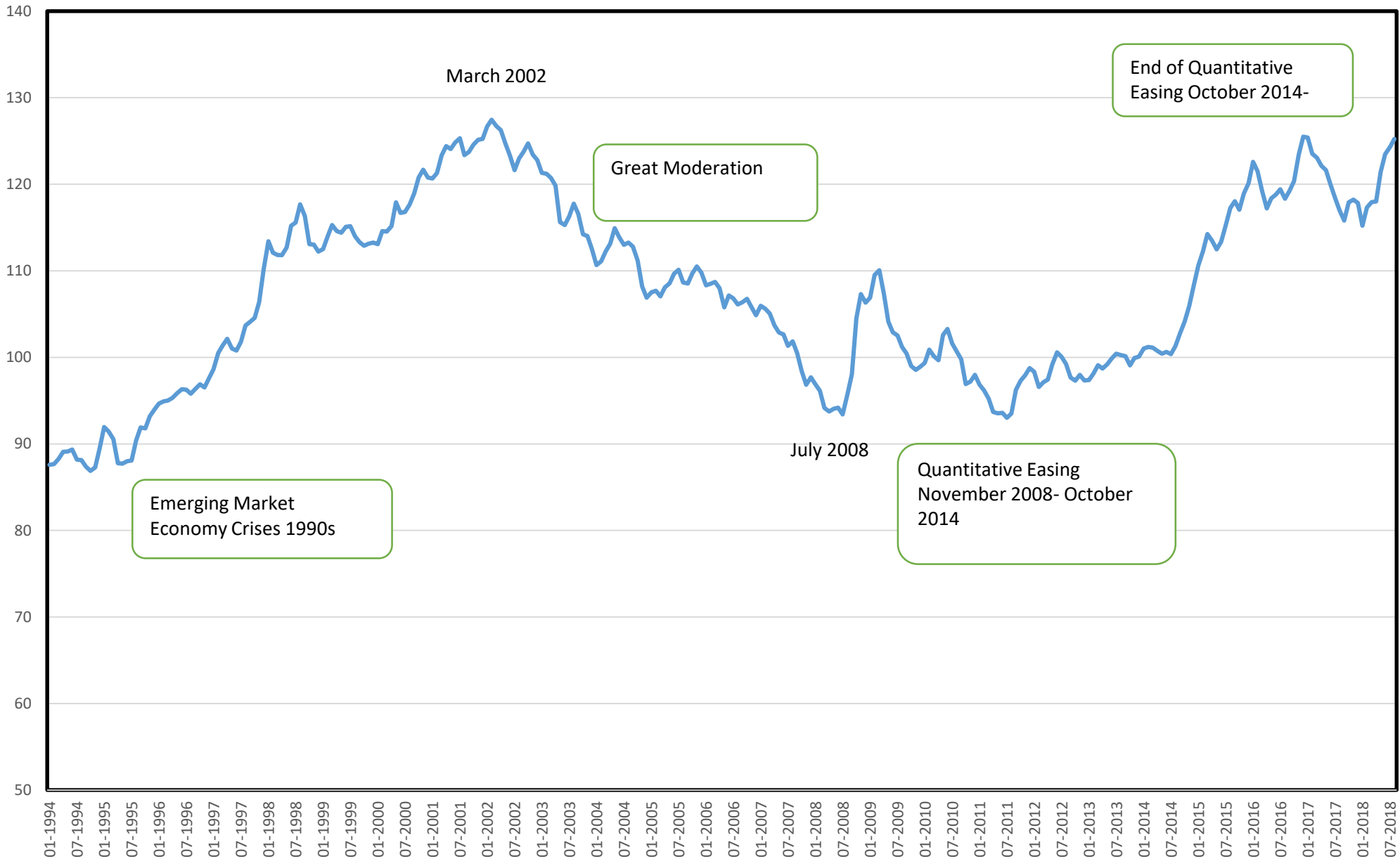
1930s: part of economic nationalism, leads to retaliatory trade barriers, dangers of floating exchange rates and short term capital flows

- 2010s not the same as 1930s, **BUT**
- Spillover effects from Unconventional Monetary Policy
- Impact on Emerging Market Economies:
  - Capital inflow in 2009-12
  - Taper tantrum 2013
  - Capital outflow 2014-
- Impact exacerbated by Dollar indebtedness
- EMEs v USA; USA v China
- Retreat from Floating Exchange rates
- IMF Institutional View on Capital Flow Management (2012)

## Jay Powell – May 2018

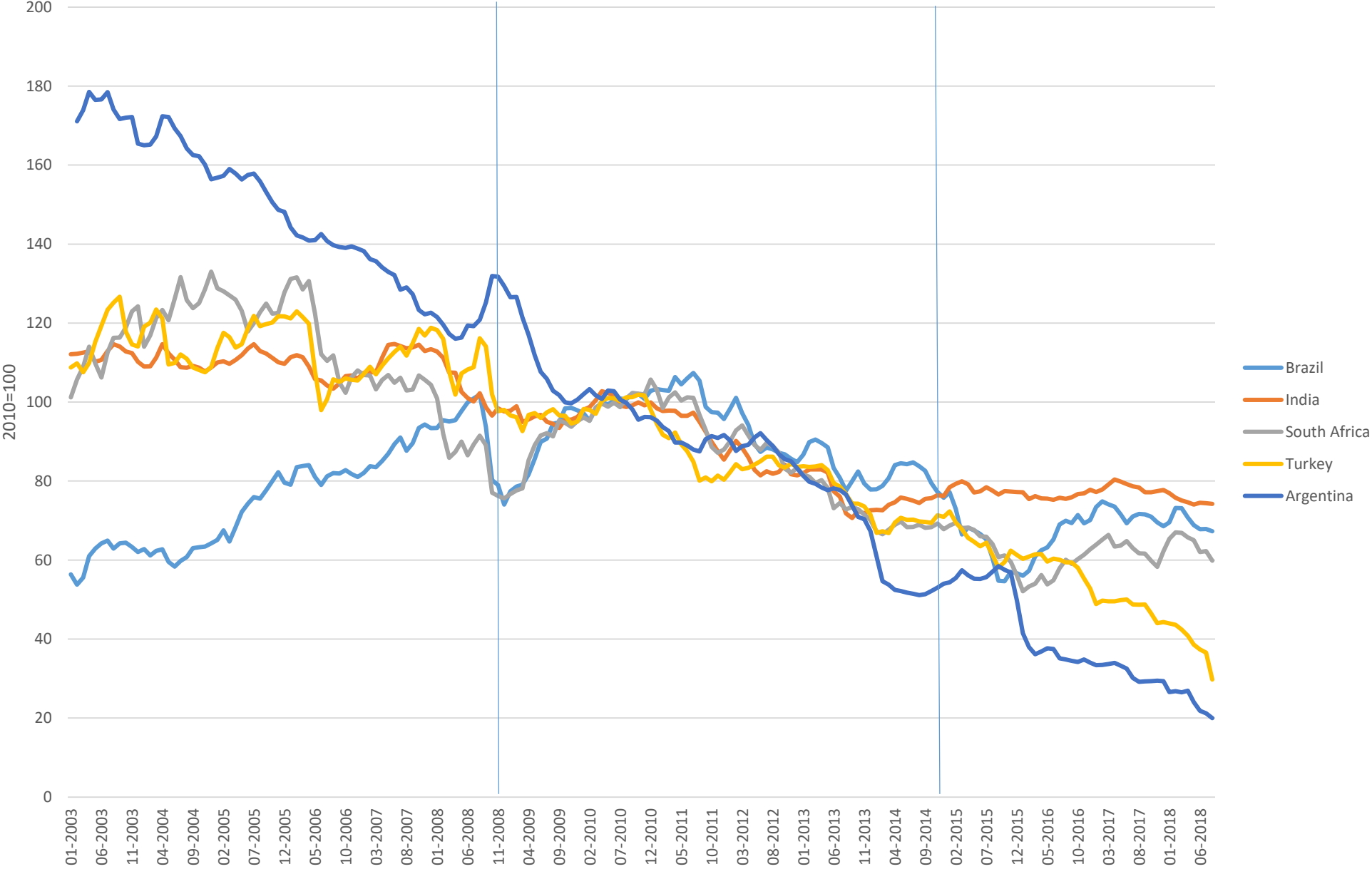
- ‘Monetary stimulus by the Fed and other advanced-economy central banks played a relatively limited role in the surge of capital flows to EMEs in recent years. There is good reason to think that the normalization of monetary policies in advanced economies should continue to prove manageable for EMEs’ (Powell 2018).

US Dollar Broad Effective Exchange Rate Index (2010 = 100)





Emerging Market Nominal Effective Exchange Rate Index 2003- August 2018

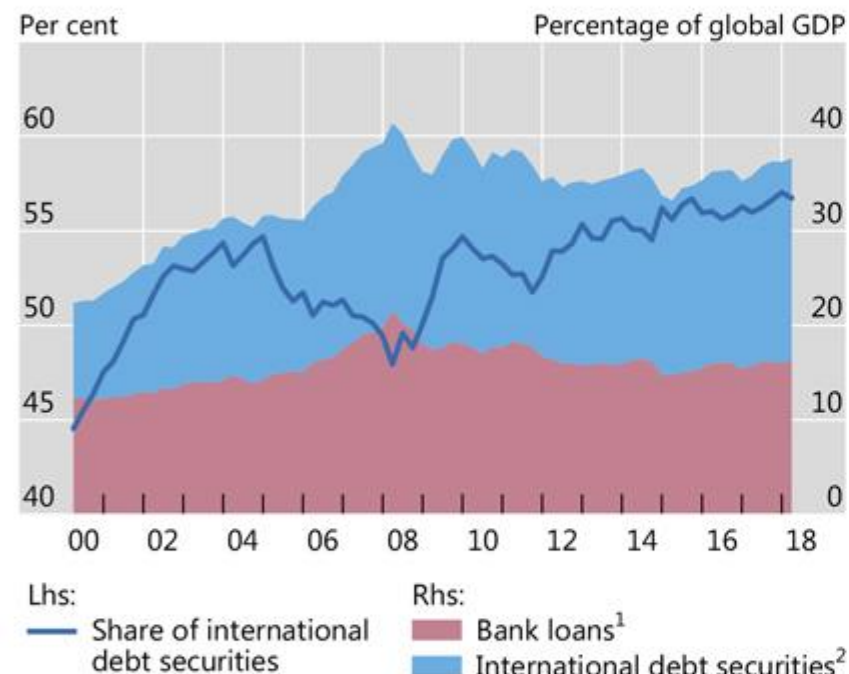


# The share of debt securities and the US dollar in international credit has risen

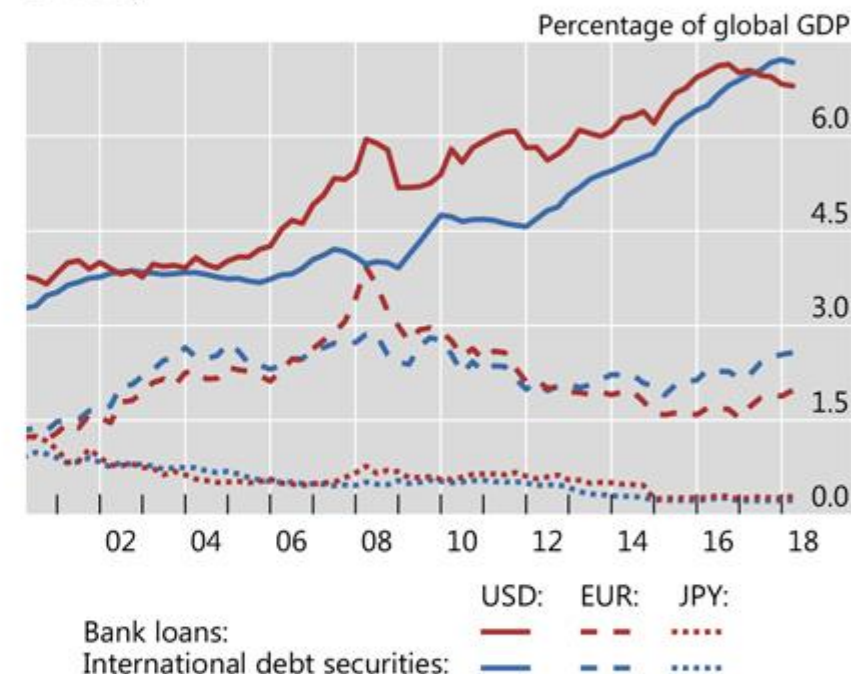
International credit to the non-bank sector, amounts outstanding

Graph 1

International credit to non-banks by instrument



International credit to non-residents by instruments and currency



Further information on the BIS global liquidity indicators is available at [www.bis.org/statistics/about\\_gli\\_stats.htm](http://www.bis.org/statistics/about_gli_stats.htm).

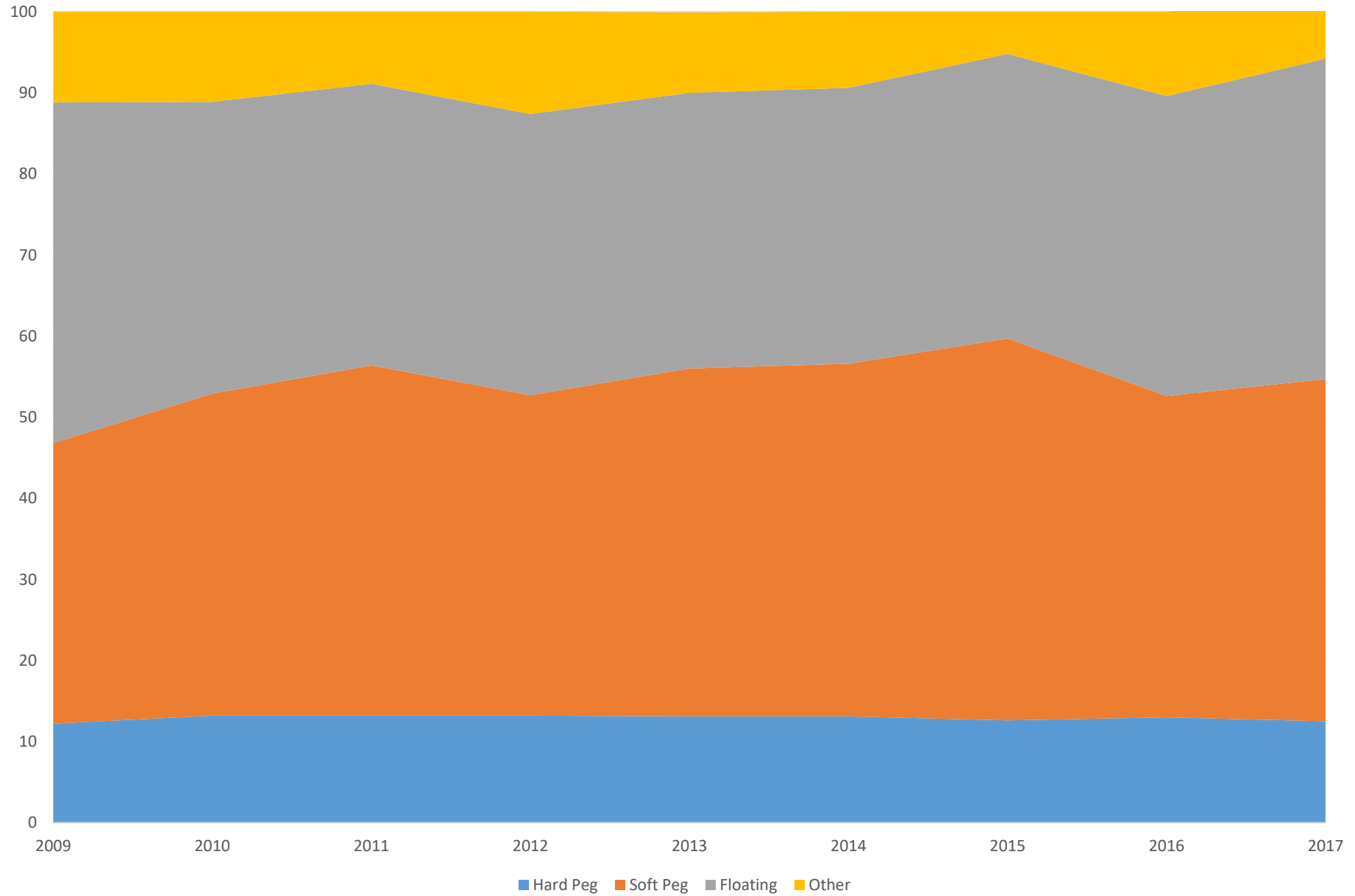
<sup>1</sup> Cross-border loans and local loans in foreign currency to non-bank borrowers. <sup>2</sup> By residence and immediate sector of issuer; all instruments; all maturities; non-bank issuers. International debt securities are debt securities issued by non-banks in a market other than the local market of the country where the borrower resides.

Sources: Dealogic; Euroclear; Thomson Reuters; Xtrakter Ltd; BIS locational banking statistics and global liquidity indicators; BIS calculations; authors' calculations.

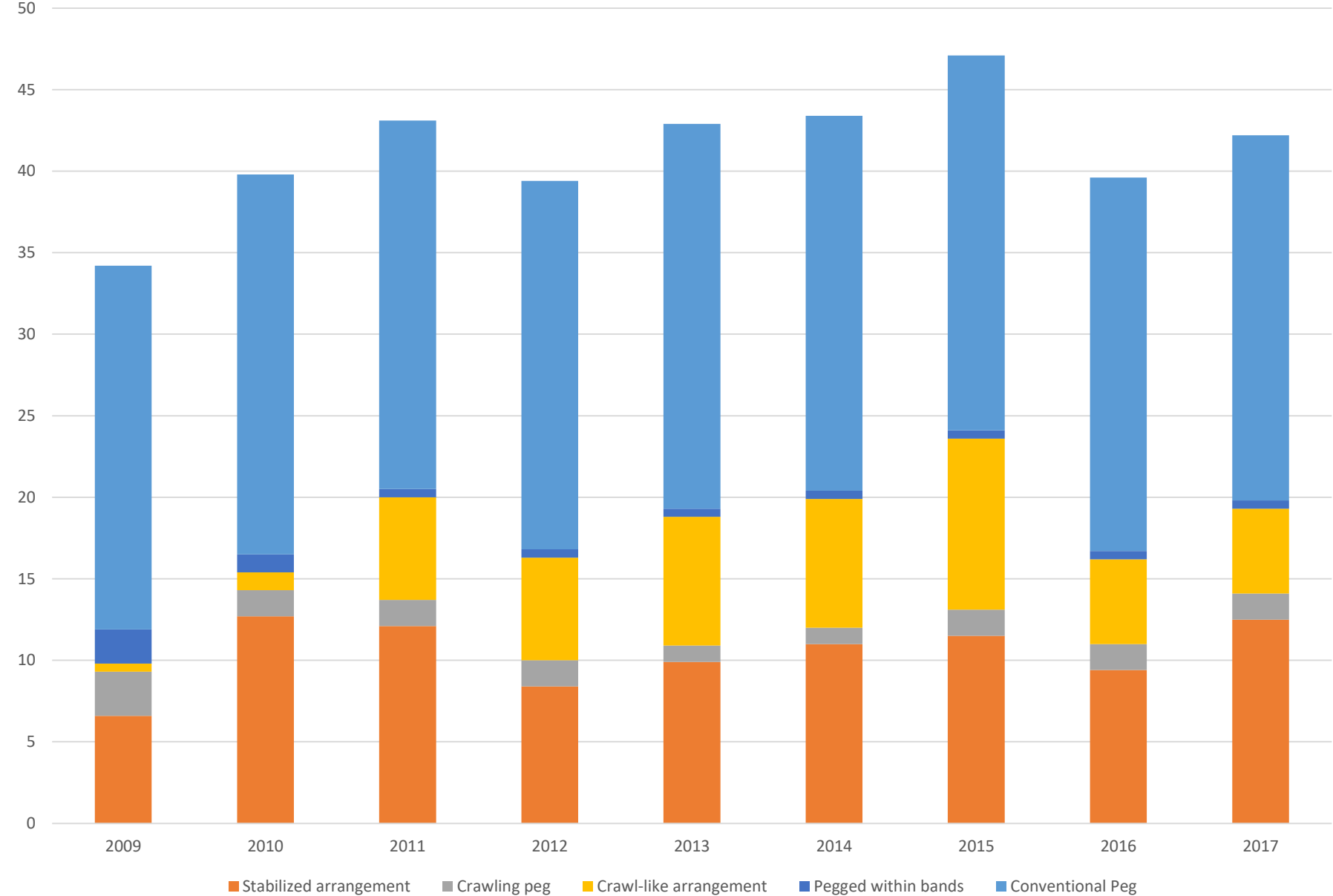
# Exchange Rate Regimes and Capital Flow Management

- EMEs that have harder inflation targets tended to suffer less from spillover effects (IMF 2018)
- There has been no increase in the proportion of countries that float their exchange rates and a slight drift toward de facto soft pegs

De Facto Exchange Rate Arrangments



Types of Soft Peg (as a percent of total)



# Governance of the Global Economy

- Reinvigorated: G20 and FSB
- Governance reform: International Monetary Fund, Bank for International Settlements (esp. China)
- Side-lined? World Trade Organisation, World Bank
  - Regional Trade Agreements, Chinese OBOR/BRI

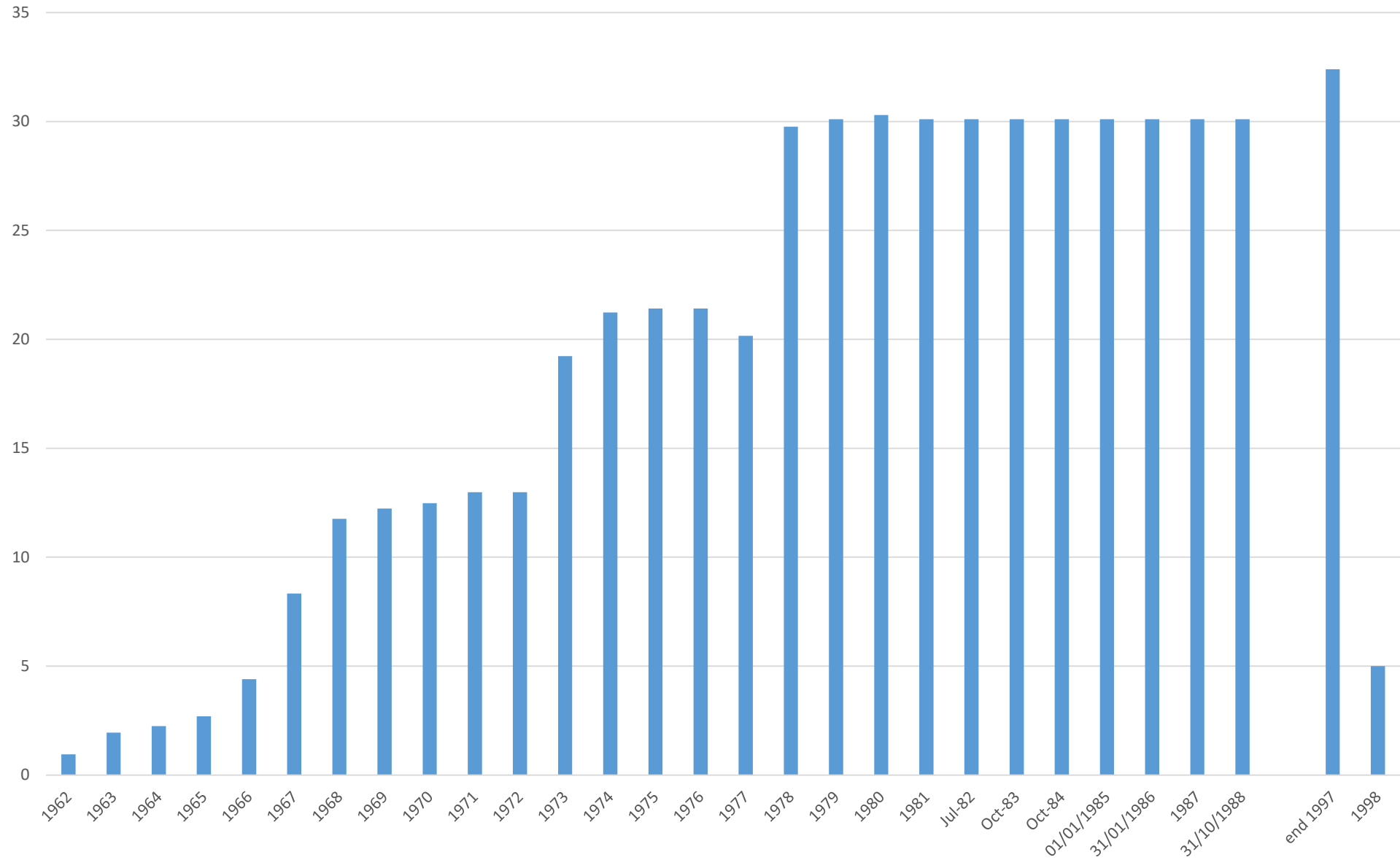
## Learning from 1970s

- Coordination problems, is 20 too big to maintain momentum?
  - 1970s: CXX ineffective
- Basel Process: long delays, backward looking, negotiated with banks, implemented just in time for the next crisis
- Basel III finalized December 2017, implementation expected in 2022-2027
- Reforming the SDR

# Global Financial Safety Net

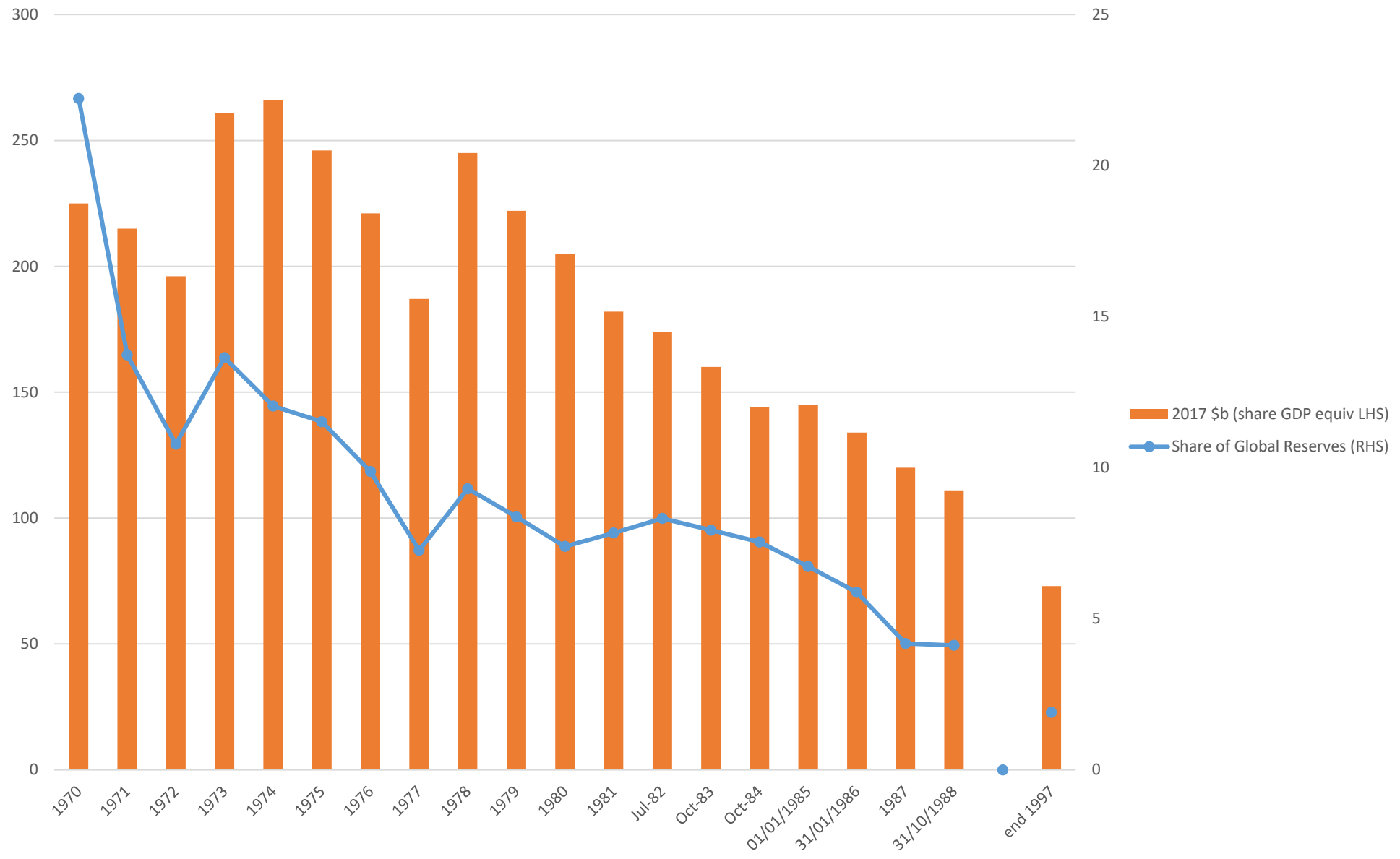
- International Monetary Fund (core outcome of 1930s):
  - stigma and uncertainty about conditionality (new non-conditional schemes expensive but not attractive)
  - bilateral focus of surveillance, advice
- National Foreign Exchange Reserves – global imbalances
- Regional Financial Arrangements: restricted, IMF Backstop
- Central Bank Swaps: restricted (Fed Swaps v PBoC Swaps)
  - Compare to 1970s: Multilateral swaps negotiated through BIS, Bilateral Fed Swaps

Federal Reserve Reciprocal Currency Arrangements (USD billion)

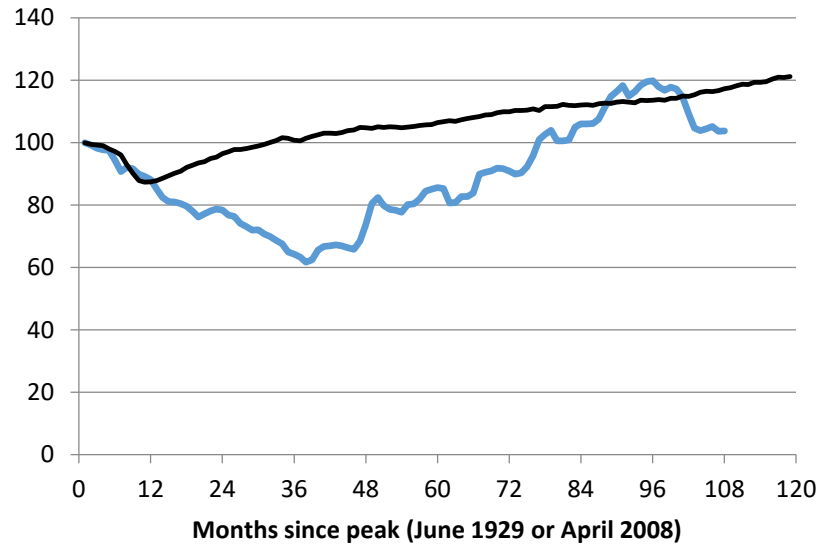




## Federal Reserve Reciprocal Swap Arrangements

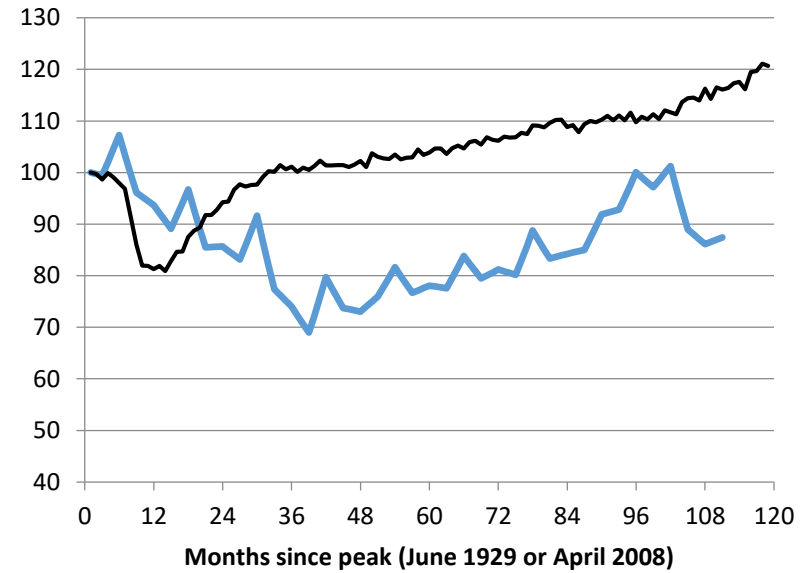


### World Industrial Production



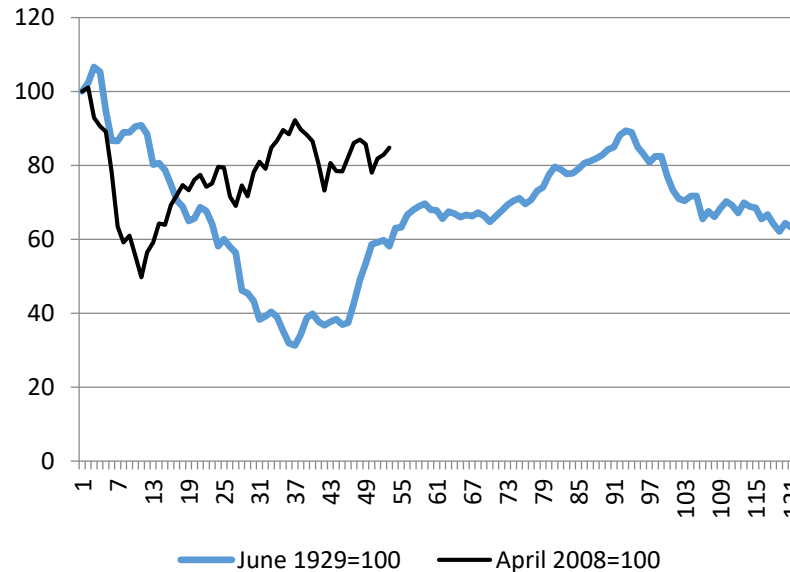
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### Global Equity Markets

# Conclusions

- Important lessons were learned
  - Sustain global liquidity
  - Confident leadership and cooperation
  - Maintaining open markets for goods and capital
- Initial Success seemed to demonstrate distinctive nature of GFC2008 vs 1930s:
  - no currency wars or trade protectionism
  - success of G20
  - broader and more intense international financial architecture
- Ten Years After: time to reassess?
  - Economic nationalism, trade wars, currency wars, global financial safety net

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