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**ECONOMIC DAY**

**SESSION:**

**RETROSPECTIVE OF WORLD CRISES**

**JUNE 5, 2009**

**(17:00-19.00, Pavilion 3, Amphitheatre)**

**St. Petersburg, Russia**

**2009**

**Description:**

In past centuries, the world has seen numerous examples of how to deal with economic crises and recover. The world's leading academics will analyze lessons from the past and discuss possible ways to avoid making the same mistakes and foresee what's coming next.

**Moderator:**

**Alex Pivovarov**, Anchorman, JSC NTV Television Company

**Panellists:**

**Nouriel Roubini**, Professor of Economics, Stern School of Business; Chairman, RGE Monitor, New York University

**Vladimir Mau**, Rector, The Academy of National Economy under the Government of the Russian Federation

**Lord Robert Skidelsky**, Chairman, Centre for Global Studies; Fellow of the British Academy

**Jyrki Koskello**, Vice-president International Finance Corporation

**Lee Ohanian**, Professor, University of California, Los Angeles

**Niclas Sundstrom**, Senior Advisor, BP and Goldman Sachs; Director, Finisterre Capital Advisory Board

**Stephen Jennings**, CEO, Renaissance Group

**Aleh Tsyvinski**, Professor, Yale University

**Ksenia Yudaeva**, Chief of the Centre for Macroeconomic Studies, Sberbank of Russia

**Vladimir Sokolov**, Professor, Higher School of Economics

**Transcript:****A. Pivovarov:**

Dear ladies and gentlemen, good evening! So, the topic of our meeting: Retrospective of world crises. But first of all, one technical announcement. I hope everyone in the hall has a box for voting as we will need them to answer one essential question. Please, make sure you have them. Besides, as I can see by

the number of those gathered in comparison with previous panels one can make a conclusion that during crises people are more interested in the future than in the past. However, as well as I understand, and in our general opinion if we don't compare this crisis with the ones that have passed, with the Great Depression, with the crisis of 1970s, with other crises, we will never be able to give a clear definition to the things happening today. Without it we won't be able to understand how to react on this crisis, what anticrisis measures are to be taken and which of them, on the contrary, can be considered dangerous and must be rejected. Without it the fight with crisis can be apparently reduced to a set of symptomatic measures, symptomatic treatment that can obviously lead to aggravation of the illness. We need to find out why the current crisis has spread with such a speed and was rather unpredictable. We need to clarify if it is a structural or cyclic crisis or, maybe, a crisis of a new type. Maybe that is the beginning of the 4<sup>th</sup> stage of general crisis of capitalism Marx wrote about. I would like Vladimir Mau to be the first member of our panel to talk on this topic. I give you the floor.

**V. Mau:**

Good afternoon, thanks a lot. You know, it seems to me that this crisis is exceptionally interesting for historians of economics that use history for studying the future. It seems that it is really interesting to consider this crisis in line with great crises of the past which as to the 20<sup>th</sup> century in my opinion can include the Great Depression of the 1930s and the events of the 1970s. I mean stagflation processes and the processes of deep structural transformation of western economies in the period of 1972-1981. Thus this is a large system crisis and I think that it possesses three characteristics as all the "great crises of the past". I will enumerate and give a more detailed description of them.

"The Great Crisis", first of all, is an intellectual one. That is the crisis of perceiving the reality. Secondly, any problem of great crisis is a problem of changing the regulatory model. And the third problem which was already mentioned by our moderator is a combination of cyclic and structural character of the crisis. You know that when all the large-scale crises begin we try to fight with them as in the previous 50 years: it means that economists and politicians get ready to the past crises as well as generals prepare for the past wars. Hoover and Andrew Mellon also used to wait for the end of the crisis, tightened monetary policy and, all in all, waited for everything will work out on its own. And at some time it really seemed that everything would get resolved but after it the crisis even aggravated. A similar situation took place in the 1970s when they tried to overcome inflation with the help of traditional Keynesian regulation methods for pumping economics with money until the model had changed completely, the paradigm had changed and Paul Walker came to radically change the approach to treatment of illness. In this respect I think that in terms of historical analogy we are still in

the situation of President Herbert Hoover. We still discuss this crisis in terms of Keynesian monetarism, we still discuss this crisis using terms that belong to the 20<sup>th</sup> century and not to the 21<sup>st</sup> one. Sure, the Keynesian theory has its very interesting discoveries and advantages. But as for me it is absolutely prospectless to reduce this crisis to the problem of "more state or less state" continuing this endless discussion whether it is a government failure or market failure. I don't want to offer another paradigm; I just want to state that the new paradigm with respect to our current economy is still not found. That is a key problem. I don't know what this paradigm is; I just know that we are still in the beginning of the 1930s, if we use this analogy, and not in the mid-1930s. And hence comes my much more sad and pessimistic answer to the question about the end of the crisis. It seems to me that quite much time will be necessary for us to conceive the depth of those structural transformations that we are to realise.

The second problem in this connection is the issue of regulations. If we turn to the great crises of the 20<sup>th</sup> century once again we will see that during all of them regulation problems were resolved. The 1930s marked the transition from classic capitalism to the regulated one. Today somebody has already mentioned in these terms the models of Roosevelt, Nazi and Stalin. Considering all the conventionality of such a comparison it is still possible. These were the attempts to define a new regulation model which would suit the new century. These were the models of countries that were resolving problems of pursuing development and had substantially higher budget dependence on the GDP than the more developed countries. In that way, the 1970s also resulted in a new paradigm of regulations which is called either Reaganomics or Thatcherism but that is just the point: this was a period of significant decrease of budgetary dependence on the GDP and, moreover, the countries that managed to solve the problems of economic breakthrough had the least budgetary dependence on the GDP than the more advanced countries.

And, finally, the third factor I want to draw your attention to during this short introductory speech that is the problem of cyclicity and structure. Like all the other "great crises" this one is sure to bear the elements of cyclicity. It was really connected with rapid development of economy, with that boom that we observed the previous five years. It is characterized by a much more serious structural transformation which is much more important relating to the modern Russia. We understand that the depth of the downturn which is the most significant among the G20 states is mostly connected with the structure of Russian economy. We also understand that in conditions of economic boom we could not even get closer to the problem of economical structure shift, to start of the project that is alternative to the raw materials approach in the structure of our economy. We are facing a very interesting task and I don't know whether we will be able resolve it or not. Is it possible to initiate the structural shifts in

conditions of the economical crisis? But this is a problem we still have to work on.

I want to stress it out one more time: I think that our main problem, our main challenge is the intellectual one. Just think about it: in the beginning of the 1990s we were resolving a task that was unprecedented in global history – transition from totally regulated economy to the market one. But today, looking back at that period of time we understand that intellectual task was not very complicated. Well, all in all, macroeconomic stabilisation is, according to Gaidar, a task for fools, no special institutes are required there. One must possess political will and police in order to suppress social unrest when realising macroeconomic stabilisation. Challenges we are facing today are much more complicated and, let me repeat, it seems to me that we are still not ready for its systematic solution in terms of intellectuality. Thank you.

**A. Pivovarov:**

Vladimir, I have one more question to you, just to save your vocal cords. I suppose you answer will be short. You say that it will take a lot of time before we will become aware of these structural measures that are to be taken. Can you give an approximate evaluation of how much time, how many years it will take?

**V. Mau:**

No, of course, it is impossible, I can only say... You know, there is one thesis in the economics, it may be disputable but I always adhere to it. In economic issues only economical history is real; everything else is just models and fantasies. So, the previous two crises lasted decades, the previous two system crises spanned decades.

**A. Pivovarov:**

Thank you, we will certainly get back to the issue of duration of the current crisis and possible ways of resolving it. And I also want to elaborate the topic of "Keynesian theory" that was mentioned by Vladimir Mau several times. Indeed, one of the first and most operative measures for fighting the crisis in most of the countries including Russia was an immediate release of substantial amount of liquidity to the economy and interference with those spheres that were considered to be regulated only by market relations before. Of course, a number of people had the feeling, and it has been written a lot about it, that the crisis walks along Europe; not even the crisis, the crisis is there of course, the ghost wanders about Europe along with the crisis, the ghost of Keynesian theory. The question is what kind of Keynesian theory it is. Whether it is classic Keynesianism, or any of its new interpretations or, as the

Minister for Finances of Germany states it, "vulgar Keynesian theory". Fortunately enough one of our respected guests is a person to whom we can address all these questions, this is Mr. Skidelsky. You bear the same title Keynes bore – you are the acknowledged specialist and author of a multivolume edition on Keynes. As far as I know you even live in the same house where Keynes died. Is it true? Please tell us from this point of view, is Keynes really dead or as they said about Lenin during the Soviet era, is "more alive than all the living"?

**R.**

**Skidelsky:**

Thank you very much. I'll try to answer that question as briefly as possible, but I'd like to approach it in my own way, by comparing the present economic downturn with the Great Depression of 1929 - 1932 when Keynes first advanced his new theories under three heads: structure, recovery measures and deep causes. And that will give us some perspective on what's going on and what a durable recovery will involve. On the structure of the two crises, I think the following points can be made. First of all, both crises originated in the United States. Secondly, both were preceded by a big increase in leverage. Third, both were triggered off by a financial collapse. Fourth, both were preceded by a rise in real interest rates - to five percent in 1928 and to five percent in 2006. But five: the locus of the financial collapse differed. It was in the stock market in 1929 and in the banking system in 2008 and that reflects the structural difference in methods of financing investment. However, in both cases the financial collapse was an induced response to events in the real economy, though these were connected with the way the real economy was being financed. In the late 1920s, you are talking about a collapse of commodity prices which, of course, affected farm mortgages in the United States because the rural community was very big in the United States and that reacted back on aggregate demand. In 2008 you are talking about the collapse of house prices, which fell by twenty-five percent between 2006 and 2008 with a consequent default of subprime mortgage holders and that had a direct influence on the banking system and then through the banking system also on aggregate demand. But the structure of the collapse was very similar in both cases.

So, then I come to my second topic, where Keynes does come in to the picture, and that is a comparison of recovery measures. Now, policy makers in 1929 and 1932 lack the intellectual resources, something that Vladimir Mau has mentioned to respond effectively to the run of their economies. Governments tried like mad to balance their budgets. They allowed banks to fail, they allowed mortgage holders to default and there was also severe constraint which I think hasn't been mentioned sufficiently, in that, most countries were on the Gold Standard and the existence of the Gold Standard prevented sharp cuts in interest rates for the first two years of the crisis. A classical example

of a "do nothing" approach to the economic crisis was the treasury view. This was the view that the extra spending by governments would be ineffective if governments borrowed the money from the public this would only divert money that would have been spent in any way by private agents: printing new money would be merely inflation. Keynes pointed out that that these arguments would only be true if everyone who wanted a job was already employed. If there was mass unemployment then neither of these arguments were valid. Today the intellectual climate is different because we've had Keynes and all countries that have had stimulus packages both monetary and fiscal. But there are still strong traces of that old treasury view in the economics profession, especially in the branch located in Chicago. Economists like Eugene Fama, John Cochrane and Barrow have suggested that the multiplier from a stimulus would be zero or even negative and, of course, that has enraged Keynesians like Paul Krugman who accused these economists of living in the Dark Ages. The debate has got rather impassioned. You can follow it in various blogs where the economists slag off each other as well as historians on the way. But the issue is more complicated than just black and white because the effects of any stimulus depend partly on the expectations held about government policy. If the solvency of the government is questioned, one could have something called psychological crowding out. The truth is, it is difficult to get economies out of the hole once they've fallen into it. And the important thing is to take precautions against falling into a hole. Once you are in the hole, you know, things become really difficult.

Then I come to my third and last point. Now that we are, or maybe, over the worst of the crisis, attention has switched to trying to understand its deeper causes. And there are two theories which can be distinguished from each other. One is the money glut theory. The other is the saving glut. The first blames the crisis on loose fiscal and monetary policy, which enabled Americans for too long to live beyond their means. In particular, Alan Greenspan, chairman of the FED in the critical years leading up to 2005, kept money too cheap for too long allowing an asset bubble to get pumped up till it burst. That's one explanation. The second explanation sees cheap money as a response to the global saving glut, which originated in East Asia and the Middle East. The exorbitant privilege enjoyed by the dollar as the world's key currency allowed the Federal Reserve to pursue expansionary monetary policy to push domestic demand beyond domestic output, thereby absorbing foreign excess savings being hurled at the United States. But both the current account deficit and the debt-financed domestic housing boom were unsustainable: it was a race between whether the dollar or the housing market collapsed first and as we know it was the housing market which did. Both theories, it's interesting to mention these theories, because they are re-runs of exactly the debates about the causes of the Great Depression. On the one side, the conservative economist Lionel Robbins, argued that the depression originated in the

credit expansion started by the Federal Reserve Board in 1927, partly to offset our recession.

This unleashed an orgy of speculation which couldn't be checked by the dear money subsequently imposed. And Keynes was the first and, for a time the only economist, who identified the saving glut was at the heart of the crisis of 1929. The idea that slumps originate in saving running ahead of investment was at the heart of his "Treatise on Money" published in 1930 and in a modified form his "General theory of Employment, Interest and Money" published in 1936. So, the two interpretations reflect different views or models of how the economy works. The traditional monetarist view assumes that markets are relatively stable in the absence of the government interference. Keynes's view is that they need to be stabilised by policy and well-designed institutions. Well, I favour the Keynesian view of this but they have opposite implications for policy and we'll need to choose between them as we emerge from the present crisis.

**A. Pivovarov:**

Thanks a lot. At least I don't have any doubts that Keynes is still alive. As we are in Russia it would be especially interesting for us to consider this world crisis concerning its effect on the Russian economy and realise how it evolves in Russia compared with other countries in Europe and America. I would formulate this question very simply: Is Russia different? And if so, what is different?

**V. Mau:**

<inaudible> Talk about <inaudible> What economists do know is what prolongs the crisis. When I think about this crisis, the first thing I think about <inaudible> of the 20th century <inaudible> what happens next. <inaudible>

**Somebody from the floor:**

I'm sorry to interrupt you for one second. Mr. Skidelsky has to leave us now because he is late for a plane. I'd like to say thank to you for your attention and participation in our meeting.

**V. Mau:**

<inaudible> world economies <inaudible> Russian government <inaudible>

**A. Pivovarov:**

Thanks a lot for your speech. I want to go on with the comparison that you have already mentioned, the comparison of the current crisis with the Great Depression. It is surely the first thing that springs to

mind and it is used not only by economists but also by Mass Media almost every day. Current events are compared with the 1930s in the United States of America. Here we have one of the most renowned specialists in that Great Depression, I don't think anyone will deny that the current one is also great. Mr. Ohanian, I want to understand: what do we actually get from the comparison with the Great Depression? Does it help us somehow? Or vice versa, does it produce any additional limitations to our vision of what is going on now? In other words, does it inspire or frighten us? What does it give us and is it reasonable at all?

**Lee Ohanian:**

First, let me say thank you very much for the invitation. It is a pleasure to be here and to address you about crises and about comparisons to other, historical crises. Many comparisons have been drawn between our current crisis and the Great Depression of the 1930s. Many of those comparisons lead us to wonder whether our recovery from the current crisis will persist year after year after year, much as the Great Depression persisted. The Great Depression started in 1929 and we didn't return to full employment until thirteen to fourteen years later.

Let me begin by noting two significant differences between today's crisis and the Great Depression, which I think are often overlooked when discussing our current crisis. These two differences regard the severity of the two episodes and also the relative importance of financial factors at the onset of both of these crises. In terms of the severity of the two episodes, there really is no comparison. The current crisis is about one and a half years old in the United States and, at comparable time during the Great Depression, that is after one and a half years, the fall in employment and industrial production was about four times as large as it is today. This episode is closer to the fairly severe recessions that we had around the world during the early 1980s and the mid 1970s. Thus far it's not even close to what we saw during the 1930s. The second difference, that's often overlooked, is the relative importance of financial factors at the onset of the crisis. Economists use a number of indicators to gauge the relative importance of disturbances and (inaudible) in financial markets and how those disturbances depress the market and impact on output. Three of those indicators are changes in interest rates between safe assets and risky assets; changes in the volume of financial intermediation and lending; and changes in asset value, such as stock prices or housing prices relative to output. And believe it or not, all of those indicators are much worse for this episode than for the 1930s. In the Great Depression there was hardly any increase in risk spreads in the first one and a half years... And believe it or not, the decline in the

stock market measured relative to real output is worse today than it was in the 1930s. Similarly, a decline in banking and lending in bank inter-mediation today again, comparatively speaking, is much more severe. That is, in today's episode relative to the Great Depression. Now, given those differences, what I'd like to talk about now are what these implications have for how we go forward and what our recovery might look like. As Alik mentioned, there's new research that's indicating that the deepest and most prolonged crises are those that tend to be associated with government policies that largely prevent the normal economic forces of supply and demand from working properly. The most rapid economic recoveries are those associated with government policies that essentially foster the efficient allocation of resources and foster the normal working of supply and demand. We have a number of episodes we can point to for both of these. Alik mentioned Japan in the 1990s. In the United States in the 1930s, government policies substantially continued the depression by artificially raising wages and prices in many industrial sectors. When we think about the 1930s, and this is very different from what we see today, unemployment remained very, very high, year after year after year, and real wages were also very, very high, year after year after year. And this is a pathology from the standpoint of economics. People wanted to work, particularly at those higher wages. Why weren't people able to find jobs that time? Recent research is indicating that it was because government policies prevented those wages from falling and the labour market from functioning properly. Mexico is another example of a country that had a crisis and had a prolonged recovery. In fact, per capita Mexican GDP today, adjusted from normal trend growth, is still far, far below what it was in the early 1980s. Mexico had a banking system, which they continued to promote with government policies that prevented the efficient allocation of resources, that propped up weak banks. Weak banks propped up weak lending to impaired companies, much like Japan in the 1990s. In contrast, Chile had a crisis in the early 1980s, which was followed by a very brisk recovery. Chile is one of the true success stories in Latin America. Chile paid the price. They privatised a number of banks: there were a number of bankruptcies, but productivity growth was very, very rapid.

In terms of thinking about where we might go from here, in my view, it's very hard to say. At least in the USA, some policies suggest the possibility of artificially raising wages, for example the employee freedom of choice act, which would significantly increase the rate of unionisation in the USA. And there is policy aimed at bailing out institutions that are deemed to be too big to fail, such as General Motors and Chrysler. These prevent the natural reallocation of resources across producers that are less efficient to producers that are more efficient. As we go forward, if we do see policies that would promote the efficient operation of markets we can be reasonably optimistic. However if we see policies that try to forestall or try to help out or manage the crisis and so preventing the efficient reallocation of

resources, then we may be in for a much longer process.

**Somebody from the floor:**

Lee, now I will ask you a question to which I want to get a one-world answer: yes or no. Let me repeat once more so that it is translated. Now I will ask you one question and ask you to answer with one word: yes or now. Is the current crisis worse than the Great Depression?

**Lee Ohanian:**

Far less worse.

**A. Pivovarov:**

Great thanks for you "less worse". How should we understand it? In other words, when was it worse: then or now?

**Lee Ohanian:**

Today's crisis is much less worse than the Great Depression and hopefully it will continue to be much less worse than the Great Depression. We are not even close to what we saw in the 1930s.

**A. Pivovarov:**

Thank you for your optimistic forecast. Let us continue our comparison of the current crisis with the crises that took place within the last 15-20 years. Vladimir Sokolov, it's your turn.

**V. Sokolov:**

Hello. I would like to draw some parallels between what happened in Mexico in 1994, in Asia in 1997 and in Russia in 1998. So I want to talk a little about the classical small-open economy crisis and point out a few common factors that lead to the crisis, in government policy response and in the outcomes.

So economists always find it perplexing to bring in the fundamentals, which are often not that bad in the crisis. For example when <inaudible> talked about the Mexican crisis, he said that fundamentals could not account for the crisis in Mexico. <inaudible> said that the punishment was much stronger than the crime. Of course, by certain metrics, economies were in a bad state: let's say, Mexico ran a big current account deficit, but on the other hand, fiscal discipline was very high. Still, the crisis happened unexpectedly, provoking different theories to explain it. Let's turn to the Asian crisis, where they were

very much braced tigers. They ran current account surpluses, but as economists point out there were big problems in the private sector: there were financial vulnerabilities; balance sheet imbalances; heavy external borrowing and, most importantly, the moral hazard, whereby private businesses were backed by implicit public guarantees, which lead to poor screening of investment projects and, in the end, bad investment. This, in some ways, draws parallels with the Russian 2008 crisis, when, in 2007, we had quite a big surge in external borrowing by the private sector and especially the banking sector. It actually exceeded the current account surplus that Russia ran in 2007, and it followed on from the capital account liberalisation in 2006. Arguably, moral hazard was also quite high, so maybe this is a fundamentals problem which runs parallel to the Russian 2008 crisis.

In the Russian '98 crisis, one of the other fundamental factors that economists often mention, was the currency misalignment. For a while, Russia ran quite a successful exchange rate stabilisation policy to decrease the inflation rate, which succeeded. However a downside was the rouble overvaluation. This, combined with short-term debt that exceeded reserves, as well as the IMF package in the months before the August crisis and the subsequent attempt to extend the maturity of the government short term debt didn't help matters. In the end, we had a simultaneous devaluation and a default on domestically-dominated government debt.

This is not happening now. In Russia we have quite large reserves and government debt is quite modest. So the major problem that economists identify from the fall is the private sector debt. According to certain accounts, the devaluation that we witnessed and that swapped from the state reserves towards the private sector (the commercial banks) was an attempt to clean up the balance sheets to cure the currency mismatch, in order to have assets in terms of foreign currency.

So the government response. In the Mexican case, economists identified a so-called postponement, or procrastination, of the situation. The government decided to run down the reserves, but they didn't succeed. The outcome? Bank panic, loss of credibility and devaluation of the peso. In the Russian case, we have successfully managed to defend the currency pack and to restore its credibility. This is attributed to the positive sides of the current management of monetary policy. As regards the Asian crisis, the government responded by attempting to use the IMF package, accompanied by a tightening of monetary policy - high interest rates and high discipline on the fiscal side. The same thing happened in Russia in '98. So the Duma accepted strict fiscal measures. We don't have that situation today in Russia, but on the other hand, it seems that our authorities are running expansionary policies, similar to those of Western countries, which use financial reserves in order to smooth the impact of the crisis.

This introduces two interesting points, which make Russia unique. Economists identify several factors related to government response. One, which Oleg mentioned already, is the trade off between a quick

market solution and government-led easing of the problem. The question is: if we use the reserves, is the idea to insulate the economy from adverse shock, or is it to delay this creative destruction. Are we just procrastinating and putting off necessary adjustments to the new situation? The second question concerns moral hazard, which was quite severe in the case of Mexico and the Asian countries. Nevertheless, it was still complemented by positive sides, notably when international institutions came in and imposed strict measures. (Although on the other hand, knowledge that they will step in encourages moral hazard in the first place.) In the Russian case, we don't have to worry about the help of international institutions because we have large reserves. Also, because we don't have to resort to external help, we don't need to impose strict conditions. Rather than hardening the constraints on firms we are softening constraints on them. That's an interesting discussion to pursue, I think, to see whether financing the crisis by running down the financial reserves is increasing or decreasing moral hazard in the current situation.

**A. Pivovarov:**

Thanks a lot, Vladimir. I would like to continue our talk about the measures that Russian government has to take in order to overcome the crisis and its consequences as fast as possible. It seems to me that nobody doubts that the need for structural changes in the Russian economy was revealed by the crisis in a more acute way than it used to be. But here we get one more question: in general, it is already proved that during the periods of growth and stability important structural reforms in Russia are not implemented. As Mr. Chubais has already told on our previous meeting: the higher oil prices the less Russian authorities are ready to implement any structural reforms. The question is the following and I want to address it to Ksenia Yudaeva: are Russian authorities capable of implementing structural reforms during the crisis period, during the downturn time?

**K. Yudaeva:**

Thanks a lot. I would like to point out that five years ago the market of bribes estimated, in my opinion, at four billions per year. Considering the growth of well-being of Russian citizens those 100 billions that were spent by the Central Bank last year in order to prevent such grave consequences of the crisis look like a rather reasonable price people want to pay for things to change for the better. And let's get down to the question now: well, generally speaking, indeed, a peasant needs a thunder to cross himself and wonder and therefore we start actions that are directed at elimination of negative consequences a little bit too late. It seems to me that is something connected with our psychology.

Not to react <inaudible> Well, if we turn back to history we will see that indeed, that's during crises

that some transformations happen here. The crisis of 98 resulted in rehabilitation and strengthening of our banking system and this, in turn, helped to prevent a large-scale crisis of non-payments and absence of liquidity. Crisis is a time for making solutions connected with those particular problems that were uncovered by this crisis. From my point of view, the problem of Russia today is that when people speak about reforms to be implemented in Russia they usually mean reforms in those spheres that are not directly connected with crisis. Well, there is a list of reforms, and everyone starts to enumerate: "healthcare, education, pension system", etc. Surely, all these spheres already feature rather significant negative consequences but neither of them are directly connected with the crisis that is going on now. And what is more, in some cases, let's say, in relation to the pension reforms, those reforms, that are usually offered, from the point of view of the crisis we are observing nowadays, don't look like economically viable. Thus, the transition to accumulative system in the period when the market went down for about 80 per cent and America has 401k of steel, 201k and everything is hanging on a thread, we won't be able to motivate the citizens of Russia to shift for an accumulative system during such a crisis.

**A. Pivovarov:**

Well, you also reminded of a Russian saying I wanted to repeat now: "A peasant needs a thunder to cross himself and wonder". But here is one person who the people call the "Doctor Doom", "Doctor Fate", because long ago before there was thunder he said that it would be and it would be necessary to do something about it. I have a question to Mr. Roubini: by what signs and when did you understand there would be a crisis? And as we understand now that you have forecasted it so distinctly can you tell us when it will finish and what Russia will have after it?

**N. Roubini:**

Well, first of all, I would like to say that I was not the only one who was worried about imbalances. There were many other scholars that talked about these imbalances.<inaudible> to try to figure out when the crisis is over and what needs to be done <inaudible> financial crises in general I had to summarize it and it's a bit extreme, I would say it's too extreme views <inaudible>

**A. Pivovarov:**

Nouriel, and how do you think, will it take more time for Russia to overcome this crisis than, let's say, for the United States?

<inaudible>

**A. Pivovarov:**

Thanks a lot, Mr. Roubini, I know that a great number of people in the government would find interest in your point of view. In our talks about crisis and about how it came, what it resulted in and how it is felt now, we are sure that special interest presents the experience of those people who were at the front line when this sudden crisis attack happened, of those who were directly impacted by the advance troops, as I put it already, at the front line. I want to address you, Stephen, it is very interesting how you handled this strike. Forbes magazine wrote that you are the man who managed to walk on the verge and escaped falling.

**N. Roubini:**

In my view we are living in the world with <inaudible>

This huge convergence and the associated relative decline of the West have created many of these imbalances. Lord Skidelsky quite quickly identified the fundamental underlying imbalances that enabled this crisis to happen <inaudible>

Since emerging markets didn't trust their own financial systems and didn't trust their own currencies, they wanted the whole vast amounts of dollar reserves to effectively credit a huge subsidy of capital flows to the West. <inaudible>

**S. Jennings:**

How did we adjust? We adjusted very differently to the way in which US investment bankers adjusted. This is because Russia has a market economy: we would sink or swim, relative to our own endeavours and our own efforts. This is how it should be in a market economy. That meant that we were forced to cut costs, build liquidity and to refocus extraordinarily quickly. That is the same pattern I see with our industrial clients, both in Russia and in the other emerging markets, where we operate. The adjustment process occurs without anaesthetic. <inaudible> I think that was a good thing for our business, I think it's a good thing for our clients' businesses. <inaudible>

**A. Pivovarov:**

Thank you very much. It is pleasant to hear that crisis is perceived as a good thing in some sense. I would like to continue discussing the subject of personal impressions on the effects of the crisis. Mr. Koskelo, I've got a question to you. That's not the first crisis in conditions of which you have to work. What can you say about it, about the ways of overcoming it relying on your experience with other

crises during the last 15 years?

**J. Koskelo:**

First, thanks for inviting me. Unfortunately, Steve said much of what I was intending to say. But I was following the conversations earlier on and I'm very much in Steve's camp. I think we can look at the past, but unfortunately, or perhaps fortunately, I think that today we are in many ways facing a new world order. <inaudible> In my lifetime, on behalf of the ICF, I handled the Asian crisis, the Argentinean crisis and the Russian crisis, from a practical point of view. <inaudible> At that time, these countries were facing crises like those we face today during this global crisis. But the question is: what stage of the crisis are we currently at and on what part of the globe? Certainly, in Europe, people are aware of the crisis, but the on the other half of the globe, countries are still partially in self denial. I think what we've seen is, unfortunately or fortunately, a global scheme that is much more interconnected than it ever was before. If we look at the situation ten, twenty years ago, when we had the Asian crisis, where was China? China was next to nothing. Where was India? It was very, very marginal. <inaudible> And, as Steve said, I would like to ask the question: where are we going to land? If we're trying to assess this crisis and find a way out using the US consumer model, then I think we're just being greedy. <inaudible> I would like to broach another subject, which curiously hasn't yet been posed today. Let's examine the investment that global leaders, and indeed everybody, engaged in over the last thirty years, and I'd like to pay particular attention to the last ten years of investment in the real sector. <inaudible> Or are we already trying to fix the financial system? <inaudible> We all saw how dramatic the changes in the global exports were about three months ago. Japan dropped by about fifty percent and everybody who was in the export business went down. The question is: how much of that was the result of global confidence in terms of no demand? How much of it was it caused by cross-border problems in terms of funding? <inaudible> And if you look at the cross-border lending problems that we have in Eastern Europe and in Latin America, I wonder who's going to provide all that money. Or are people just going to write it off? Because that is the one fundamental big overhang that we have today. Unless we somehow restore global confidence, we are not going to come out of this crisis for a long time. Is that going to be the job of the G20? Certainly Russia can play a major role. <inaudible>

**A. Pivovarov:**

Thanks a lot. Niclas, I have specially left you to the end of the talk about how it will affect Russia and how it affects Russia already. You are the person who can boast that he observes all of it from aside

and who is involved in it at the same time. Today we have talked about in the events of the past. Violating the subject of our discussion I would like you to talk on the future of the Russian economy. For example, today the President has said at the opening of the Forum that it is still too early to drink champagne. Maybe, in accordance with this analogy, it's already time to put it in the fridge... <inaudible>

**N. Sundstrom:**

Those who don't risk, don't drink champagne... <inaudible>

**N. Sundstrom:**

<inaudible> The banking crises with which we are currently struggling over the world are rather similar to those that took place in 1931-1933 and to the European financial crisis of 1931. <inaudible> And this goes somewhat towards explaining the severity, the incomparable severity, of that crisis, compared to what we are dealing with today.

And now in terms of looking forward. Yes, I was asked to think a little bit about what might be the main question marks or debates: to consider what we may enter and what we already entering in to. I found it interesting just thinking very quickly about this subject, knowing that there is huge demand out there. If you attend as many conferences as many of you do, there is a huge desire to think that soon everything will return to normal: old growth models will be back, America will be back up and running and so on. However I think we will very quickly encounter a number of question marks, many of them which will have already been mentioned today. First of all, the explosion in the West, in the industrialized western countries. <inaudible>

Another point is the expansion of the State that has happened very rapidly in many countries. <inaudible>

Finally, we should consider all the points that my colleagues have brought up regarding changes to the global structure. <inaudible>

Just a final word on Russia. I completely agree with what was said earlier <inaudible>.

I think we have seen another big plus today during this forum, and that is a very strong intellectual openness to use this crisis in order to test new ideas. <inaudible>

**A. Pivovarov:**

Niclas, thanks a lot, I will surely provide some additional time for all the participants to comment on their colleagues' speeches but before it, in order to have a little rest and create one more topic for

comments, I would like to ask everyone to get their remotes and to declare the topic of voting. First of all, it needs to be turned on as it is indicated in this manual: you need to press the green button and make sure that the light is on. On my remote it is red already. So, now you will see a question and variants of replies. You need to choose one of the replies' variants and press the corresponding button under the proper number. After you have pressed this button you won't be able to press any button again. The question is very simple: "How long, in your point of view, the current crisis will last?" One year, two, three, ten years and the most "optimistic" answer – "I won't live to see it". Please, now you can see the red line, before it reaches the right edge of the screen you need to press the corresponding button. Sure enough I would like this metronome to calculate time till the end of the crisis. So, the first place goes to 2 years. The second one goes to 3 years, the third one – 10 years, then we have one year and one per cent of those present here now don't expect to survive this crisis. Dear participants, if anybody wishes to comment these results or present some other comments, please, raise your hands and I will give you a word. Nobody has any comments? Yes, Vladimir, please.

**V. Mau:**

I had a short picture in my presentation - I wish I could run it. I plotted recovery patterns for those small, open-economy crises which I described, and luckily most of them demonstrated the so-called "reshape" pattern of recovery. During the 1998 crisis, Russia was a champion in terms of the recovery of GDP performance; it was the fastest. But this crisis is a global one and first of all global demand fell considerably, which helped the small open-economy crises of the previous year and helped to maintain export rate growths. With particular regards to crises in Mexico, in Asia and in Russia in '98, we can see that there was a quite steep real-effective exchange-rate devaluation, which economists believe increases the competitiveness of a country. In Russia, I think that the current rouble devaluation was not strong enough. <inaudible>

**A. Pivovarov:**

From my point of view I can say that such an evaluation may be called moderate optimism. Is that right, Vladimir?

**V. Mau:**

Well, yeah, you are right.

**A. Pivovarov:**

It seems to me it reflects some hope still. And in a way I understand... The crisis definition. Therefore if the crisis gets the W shape, or, as Ksenia likes to say, the endless W shape, then in some point of time it may seem that it's finished already although it hasn't start at all.

**A. Pivovarov:**

You keep on frightening us that crisis has not yet started. Are there any other comments of the participants?

**K. Yudaeva:**

I can give my comments. Concerning the results of voting in comparison with those that we got on the previous section meeting. The majority of people have also chosen "F" there. So I think that this forum serves for producing consensus in relation to degree of the crisis we are in now. And "W" is rather pessimistic.

**A. Pivovarov:**

Thanks a lot, it is a very optimistic speech even as compared to me. Maybe someone of the audience wants to give his own comments?

Yes, please, the microphone. Introduce yourself, please, and I ask you to talk not more than one minute.

**S. Pakhomov:**

Sergei Pakhomov, Chairman of the State Debt Committee of the City of Moscow. I think from a civilization perspective, we all live in a non-stop crisis. We take too short a retrospective of the crisis: if we look into the long history of civilisation, we can see that all those previous crises were solved in a very simple way: cancellation of debt; expropriation of creditors; expropriation of investors, cancellation of <inaudible> Why you think the solution for the present crisis will be any different? And perhaps the sooner we do it, the better?

**A. Pivovarov:**

I hope we are not going to start from the very beginning. So, any answers?

**V. Mau:**

My interpretation is that, if the crisis is a crisis of leverage <inaudible> Of course people say you are destroying creditor's rights, and this and that, but the reality is that, first of all, bad liabilities of household mortgages are bad assets for banks. <inaudible> There is always an element of moral hazard, people make mistakes, and then they get <inaudible> But you need to restore the growth of the economy, so I do agree that probably the best solution to excessive debt is reduction or conversion of those debt claims into equity claims. And that is what needs to be done.

**A. Pivovarov:**

Does anybody else want to answer? Any more comments? Then I will let myself close this meeting... There are some comments, aren't there? Excuse me, I didn't notice it. Yes please.

**E. Kogan:**

The question is the following. If you let me, I will ask this question in Russian. Does the current crisis present certain change of the paradigm in the work of corporations managers ? In other words, let me comment, the fact is that during the last several decades the most important task of the top-management was always considered to be a growth of market capitalisation of business. Today it is likely that a new paradigm will appear. First of all, it will be cash flow, i.e. exactly the flow of income of the corporation. And the growth of capitalisation is not so important. If it is possible, comment on it, please.

**A. Pivovarov:**

It seems to me that this question applies to Stephen.

**E. Kogan:**

Maybe, yes.

**S. Jennings:**

I think clearly one aspect of management that would shape how the crisis benefits itself would be the specific incentives of <inaudible> within investment banks, within other agents in the financial system. And this has really highlighted the <inaudible> agency problem between shareholders and

employees, and obviously <inaudible>.