

# The Financial Turbulence: *Where do we stand?*

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# The financial turbulence: *Where do we stand?*

- *The world economy is now entering a major downturn in the face of the most dangerous shock in mature financial markets since the 1930s. We need to reflect on the stakes, how we arrived here, who is responsible, and what happened - Mr Sarkozy .*
- *The present crisis must push us to rebuild the foundation of capitalism. That implies especially leaving the myth of the omnipotence of the markets... We have to find a new equilibrium between the state and the market- Mr. Sarkozy*
- *Our 21st century global economy continues to be regulated by laws written in the 20th century - George W. Bush*
- *The sub-prime mortgage crisis has therefore played the role of a trigger but there was a good deal of explosive around –Jean Claude Trichet*

## The financial turbulence: *Where do we stand?*

- French President Nicolas Sarkozy and U.S. President George W. Bush met Oct. 18 to discuss the possibility of a global financial summit. The meeting ended with an American offer to host a

*Global Summit in December modeled  
on the 1944 Bretton Woods system*

that founded the modern economic system.

## The financial turbulence: *Where do we stand?*

- The world's **first global financial summit** will take place in the US on 15 November.
- Among those expected to attend the summit will be leaders from the G20 group of nations, which includes the G7 group of major industrial economies, as well as key emerging-market countries such as China, India and Brazil.
- The head of the International Monetary Fund, the president of the World Bank, the United Nations secretary general and the chairman of the Financial Stability Forum have also been invited to participate.

## The financial turbulence: *Where do we stand?*

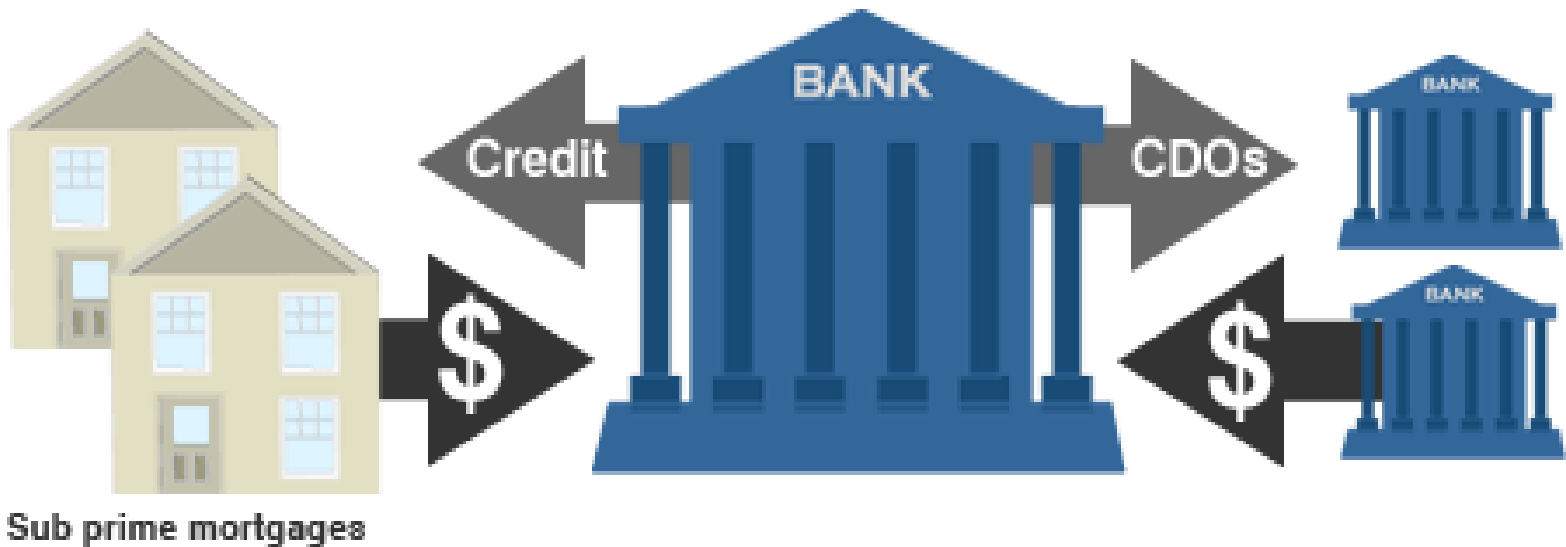
Indeed, the financial crisis that erupted in August 2007 after the collapse of the U.S. subprime mortgage market entered a tumultuous new phase in September 2008 that has badly shaken confidence in global financial institutions and markets.

Most analysts link the current credit crisis to the sub-prime mortgage business, in which US banks give high-risk loans to people with poor credit histories. These and other loans, bonds or assets are bundled into portfolios - or Collateralised Debt Obligations (CDOs) - and sold on to investors globally.

## GROWTH

Investment in high risk sectors

Asset-backed securities sold globally (eg CDOs)





## The financial turbulence: *Where do we stand?*

The financial problem has increasingly become an economic one, affecting production and consumption in the global economy

## The financial turbulence: *Where do we stand?*

intensifying solvency concerns have triggered a cascading series of bankruptcies, forced mergers, and public interventions in the United States and western Europe, which has resulted in a drastic reshaping of the financial landscape.

The April 2008 Federal Reserve engineered the emergency sale of a major U.S. investment bank (Bear Stearns) and increased broker-dealer access to emergency liquidity.



## The financial turbulence: *Where do we stand?*

Starting in August, Fannie Mae and Freddie Mac, the two giant government-sponsored enterprises (GSEs), came under heavy pressure over concerns about the adequacy of their capital

global financial markets were plunged into turmoil in mid-September following the bankruptcy of a second major U.S. investment bank (Lehman Brothers)

## The financial turbulence: *Where do we stand?*

In the next few days, market pressure drove the merger of another (Merrill Lynch & Co.) with a large commercial bank and the effective acquisition by the Federal Reserve of the world's largest insurance company (American International Group, A.I.G.) to avoid a disorderly bankruptcy.



## The financial turbulence: *Where do we stand?*

Subsequently, a number of other U.S. and European banks needed to be resolved through closure, nationalization, or merger with public support.

The authorities in the United States and Europe responded to this firestorm with a series of new initiatives.

## The financial turbulence: *Where do we stand?*

Notably, in early October, legislation was passed in the United States to set up a \$700 billion fund to purchase troubled mortgage- related securities from banks in order to contain risks of further losses from this source.

## The financial turbulence: *Where do we stand?*

- US government's involvement is **limited in size.**
  - US government's involvement is **limited in scope.**
  - US government's involvement is **limited in duration.**
- 
- The Government Is Focused On Preserving The Stability Of The Financial System
  - The Government Has Undertaken An Extraordinary Effort To Help Banks Get Loans Flowing To American Consumers And Businesses
  - It Is Vital That Financial Regulations be Updated To Meet The Realities Of Today's Global Financial System

# The financial turbulence: *Where do we stand?*

## EUROPE

- Facilitating the funding of banks, which is currently constrained.
- Providing financial institutions with additional capital resources so as to continue to ensure the proper financing of the economy.
- Allowing for an efficient recapitalisation of distressed banks.
- Ensuring sufficient flexibility in the implementation of accounting rules given current exceptional market circumstances.

# The financial turbulence: *Where do we stand?*

## G7 five-point plan

- The five-point plan is intended to protect major banks and financial institutions from failure and ensure they can raise capital from public and private sources.
- It includes steps to unfreeze the flow of credit and protect savers, although it did not reveal any specific measures.
- It pledged to take "decisive action and use all available tools" to support financial institutions.
- It also vowed to take all necessary steps to unfreeze credit and money markets;
- Banks can raise capital from public as well as private sources;
- National deposit insurance and guarantee programs are robust.

## The financial turbulence: *Where do we stand?*

- **AUSTRALIA:** *Latest:* PM announced an injection of \$7.4bn into the economy. Most of the money will come from a \$15.3bn budget surplus forecast for the current fiscal year.
- **JAPAN:** Parliament approved a 1.8 trillion yen (\$18bn) stimulus plan and the Bank of Japan put 4.5 trillion yen (\$45.5 billion) into the banking system.



## The financial turbulence: *Where do we stand?*

- **AUSTRIA:** government would provide up to 85bn euros (\$114bn) in interbank loan guarantees and up to 15bn euros (\$20bn) in equity to support the country's banking sector. The government had already announced a guarantee for all personal bank savings, applicable from 1 October.
- **BELGIUM:** The government agreed to guarantee bank deposits of up to 100,000 euros (\$136,000) - an increase of 80,000 euros.
- **DENMARK:** The Danish parliament approved a government-backed crisis plan which includes an unlimited guarantee to savings deposits.

## The financial turbulence: *Where do we stand?*

- **ESTONIA:** The government more than doubled its bank deposit guarantee to 50,000 euros (\$68,000), in line with other European Union member states.
- **FRANCE:** President Nicolas Sarkozy announced on 13 October the creation of a fund worth 40bn euros (\$55bn) to acquire stakes in French financial institutions and a guarantee of up to 320bn euros (\$437bn) on interbank loans that would run until the end of 2009. The loan guarantee will be offered to banks at commercial rates, and beneficiaries will have to sign up to certain "ethical" obligations, including on executive pay.

## The financial turbulence: *Where do we stand?*

- **GERMANY:** On 17 October the German parliament approved a 500 billion euro (\$675bn) financial rescue package. The plan includes a fund to provide up to 400bn euros in interbank loan guarantees and 80bn euros (\$109bn) to acquire stakes in troubled banks. Up to 500bn euros (\$670bn; £387bn) will be used to pour fresh money into banks and to guarantee loans between them.
- **GREECE:** The Greek government said on 3 October it would fully guarantee all bank deposits of citizens, but an official added that this was a "political commitment" and the banking system was not at risk.

## The financial turbulence: *Where do we stand?*

**IRELAND:** Ireland was the first government to come to the rescue of its citizens' savings, promising on 30 September to guarantee all deposits, bonds and debts in its six main banks for two years.

**ICELAND:** The government officially requested funding from the International Monetary Fund (IMF) on 13 October. Negotiations are also under way with Russia for a big loan to support the country's banking system. Moscow has offered more than \$5bn in emergency loans. The British government said the Bank of England would provide a loan of £100m (\$174m) to Landsbanki to help maximise payouts to its creditors in the UK.

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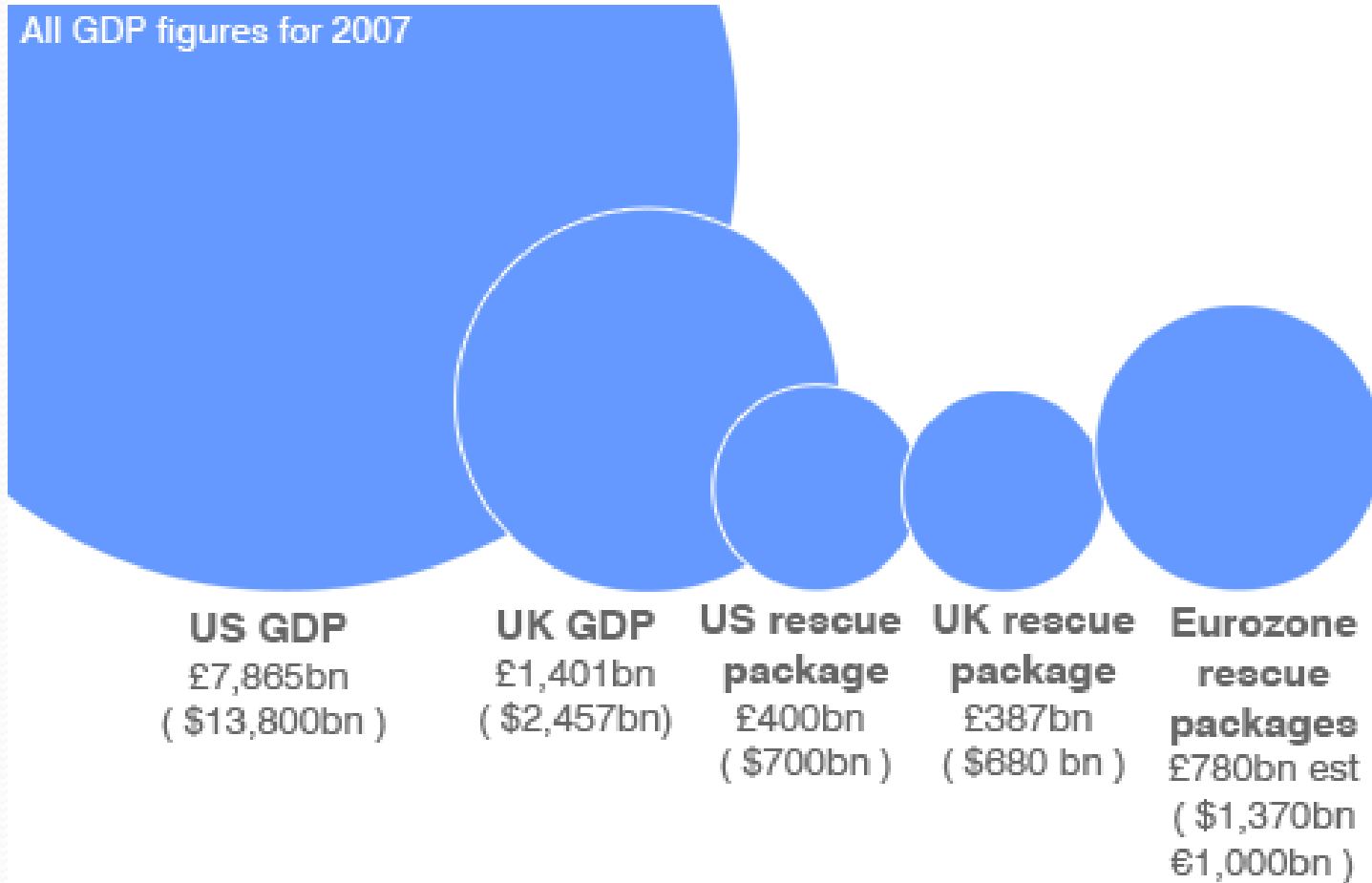
**NORWAY:** The central bank, also outside the eurozone, said it would issue up to 350bn kroner (\$55bn) in bonds to banks to help improve liquidity in the market.

**SWITZERLAND:** Switzerland takes steps to strengthen its largest bank, UBS, by giving it 6bn Swiss francs (\$5.3bn; £3.1bn) in exchange for a 9.3% stake. The bank will also be able to transfer up to \$60bn of toxic assets to a fund supported by the Swiss central bank. Credit Suisse was also offered government assistance but was instead able to raise 10bn Swiss francs from major global investors to shore up its position.

# The financial turbulence: *Where do we stand?*

## INTERNATIONAL RESCUE PACKAGES

All GDP figures for 2007

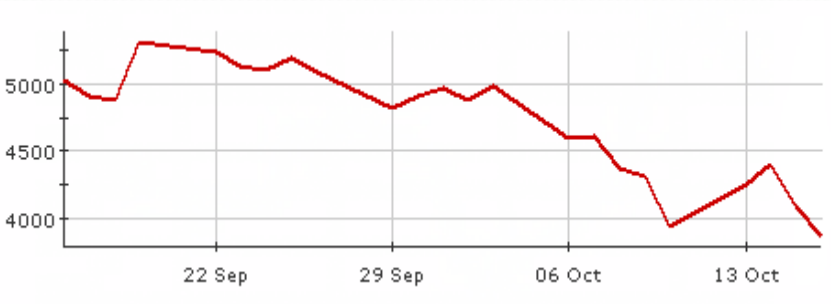


# The financial turbulence: *Where do we stand?*

<b>Bank</b>	<b>Date</b>	<b>Status</b>	<b>Website</b>
Fannie Mae	07 Sep	Nationalised	<a href="#"><u>Fannie Mae</u></a>
Freddie Mac	07 Sep	Nationalised	<a href="#"><u>Freddie Mac</u></a>
Lehman Bros	15 Sep	Collapsed	<a href="#"><u>Lehman Bros</u></a>
Merrill Lynch	15 Sep	Taken over	<a href="#"><u>Merrill Lynch</u></a>
AIG	16 Sep	Part-nationalised	<a href="#"><u>AIG</u></a>
HBOS	17 Sep	Taken over	<a href="#"><u>HBOS</u></a>
WaMu	25 Sep	Collapsed and sold	<a href="#"><u>WaMu</u></a>
Fortis	28 Sep	Nationalised	<a href="#"><u>Fortis</u></a>
Bradford & Bingley	29 Sep	Nationalised	<a href="#"><u>Bradford &amp; Bingley</u></a>
Wachovia	29 Sep	Taken over	<a href="#"><u>Wachovia</u></a>
Glitnir	29 Sep	Nationalised	<a href="#"><u>Glitnir</u></a>
Hypo Real Estate	06 Oct	Rescue package	<a href="#"><u>Hypo Real Estate</u></a>
RBS	13 Oct	Part-nationalised	<a href="#"><u>RBS</u></a>
Lloyds TSB	13 Oct	Part-nationalised	<a href="#"><u>Lloyds TSB</u></a>

# Stock Market

FTSE 100 INDEX: 16 September 2008 - present



NIKKEI 225 INDEX: 16 September 2008 - present



DOW JONES INDUSTRIAL AVERAGE: 16 September 2008 - present





# Commodities

## COMMODITY PRICES

Oil (\$)

Aug 08 -Oct 08



Gold (\$)

Aug 08 -Oct 08



SOURCE: Bloomberg



## The financial turbulence: *Where do we stand?*

There is also an ideological dimension. The United States is committed to free-market economics as a cultural matter.

The Europeans don't. For them, the state is the center of society, not the market. Thus, the Europeans were ready to abandon the market much faster than the Americans.

# The financial turbulence: *Where do we stand?*

## Georgia

Alongside with other factors, took place events will inevitably reflect on the country's balance of payment that has been very critical even before.

In the pre-war period - in the quarter II, 2008 current account deficit of the payment balance amounted to 900 mln. USD that is 2,2 times higher than the analogous index of 2007 and more by 14,4% compared to the data of quarter I of 2008.

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## Payment Balance of Georgia

- Current Account-II q. ( - 899 015 000 GGEL)
- Capital and Financial Account –II q. ( + 921 635 200 GEL)

International reserves = + 1,3 bn usd

International Investment Position = ( - 7 139 448,9 usd)

## The financial turbulence: *Where do we stand?*

It's worth noticing, that deficit in the trade balance of Georgia is still increasing with an unabated rate. Foreign trade turnover (excluding occasional trade) amounted to 5 bln. 236 mln. USD in January-August, 2008 that is 34,7% higher than the analogous index for 2007. Export share is 1 bln. 77 mln. USD and import share - 4 bln. 160 mln. USD.

Accordingly, negative trade balance of Georgia in this period reached near 3 bln. USD

## The financial turbulence: *Where do we stand?*

Eventually, deterioration of payment and trade balances is easily predictable and almost inevitable. Deriving from this, economy of Georgia will face a serious challenge in this context too that will become one more difficult examination in sustainability and require planning and implementation of adequate measures.

## The financial turbulence: *Where do we stand?*

### Loans issued by Commercial Banks (GEL)

	DATE		TOTAL	
	01.08.2008		5 570 972 000	
	01.09.2008		5 369 710 000	

# The financial turbulence: *Where do we stand?*

## Corporate Loans

- Trade -45,7%
- Industry-20,9%
- Construction -13.6%
- Three major sectors – Trade, industry and construction cover 80,2% of total loans portfolio



## The financial turbulence: *Where do we stand?*

- Deposits of physical persons reduced by GEL 260,0 mln (17,1%) by early September
- Deposits of Juridical persons reduced by GEL 129,0 mln (8,5%) by early September

## The financial turbulence: *Where do we stand?*

Total Foreign Debt, 30 June, 2008 - 6675.4 mln USD

- 2184.1 mln usd - Government,
- 242.0 mln usd - National Bank,
- 1873.5 mln usd - Commercial banks,
- 593.8 mln usd, - Other Sectors,
- 1782.0 mln usd - corporate debts.

## Georgia Donors Conference

- Representatives of over 70 countries and international organizations gathered in Brussels on October 22 at a one-day donors' conference to raise funds for Georgia's post-war reconstruction.
- State and private donors together have pledged USD 4.55 billion over the next three years to help Georgia in post-war recovery
- The sum includes about USD 3.7 billion from governments and USD 850 million from private donors:
  - Grants -2,5 bn usd
  - Loans -2,0 bn usd

# The financial turbulence: *Where do we stand?*

“Looking ahead, we will need to address the infrastructure chokepoints, and pay particular attention to **transports** and **energy** security.

Overall, while our banking system is healthy, well-capitalized, and liquid, we need to help it to the extent we can to keep **lending aggressively** to the economy, because that will be what eventually puts us on the path to recovery” - *PM L. Gurgenedze*

# The financial turbulence: *Where do we stand?*

- To restore the Georgian economy growth rate it showed in 2008, the economic team of the government and National Bank of Georgia should intervene in a timely and wise manner **to support commercial banks** which will then be able to provide loans to the developers and other dynamically developing branches
- Boost Investment climate by restoring investors confidence
- Sectoral Policy reshape
- Competitiveness policy introduction
- Comprehensive review of our tax system.



The financial turbulence: *Where do we stand?*

Thank you