

GLOBAL FINANCIAL CRISIS AND INTEGRATION INTO WORLD ECONOMY

Prof. Constantin IONETE, PhD
Member of the Romanian Academy

❖ Mr. Calin Stoica - Diaconovici maintains that "the U.S. image has suffered considerably in the last ten years and the economic crises has brought only resentments to the Wall Street. Andres Martinez, director of the NAF, believes that this century will be an American one. From a military point of view, USA are hard to beat, because they produce 25% of global GDP, with only 5% of the Earth population.... But the best measure of a future domination is the maintenance of the American culture."¹

According to international researchers, global economic recovery depends on the support of governments and central banks, but if they withdraw their recovery programs then the entire commitment will fail. Moreover, rising unemployment, deflation and state markets hinder global economic recovery.

Estimates of large institutions IMF, World Bank, European Commission and the American States report a slight increase of 3.1% of the global economy.

The reference rate in the U.S. is approaching zero, according to estimates presented by Resource Investor. "Although many predicted that interest rates will rise in 2010, I think the FED will be forced to keep down the rate of deflationary pressures. Any increase would cause panic in the markets, and this is the greatest fear of the FED", as Jason Hamlin claimed. European Bank warned that imbalances in the global

economy, that fueled the financial crisis may deepen again and threaten the recovery. The institution officials warned that the Government acts to bring economies on a growth track, despite stimulus measures taken recently, writes the Financial Times. One of the greatest threats is the unemployment problem, which is a worldwide problem. According to Resource Investor, global unemployment rate will exceed 10% in 2010.

In late March 2010, International Monetary Fund Chief, Dominique Strauss Kahn, presented a speech in Bucharest, subject to the stability of Europe in cooperation with USA.

Starting from the fact that Europe needs to be unified, he believes that "the United States must work together with the European ones, because otherwise Europe would fall behind. This implies cooperation and coordination "in order to avoid the same situation in ten years". He also revealed euros' weaknesses. "Globalization is a reality we can not escape. If Europe fails to take swift action, in 10 -20 years may become a secondary league player. "

"The crisis erupted in the U.S. housing sector, the most sophisticated market. I learned that the financial system needs tougher regulations and a harsh surveillance. In the last 10 months we have done a lot," said Mr. Strauss Kahn.

Mr. Strauss Kahn's initiative is an important one, because it supports the creation of a special fund in the banking system, financed by contributions paid by the banks, depending on risk.

"We put a kind of bank charges, to discourage the risky behaviors and to

¹ XXI Century, forecasts. Time Magazine and America Foundation.

avoid a situation where taxpayers are forced to support the financial system."

assess "the outlook for the main macroeconomic indicators in 2010":

The European Commission, from what he calls weak savings - accurately

Table no.1. The outlook for the main macroeconomic indicators in 2010

Country	Economic Growth (%)		Unemployment rate (%)		Annual inflation (%)		Public Debt (% Of GDP)	
	2009 *	2010 **	2009 *	2010 **	2009 *	2010 **	2009 *	2010 **
Germany	- 5.0	1.2	7.7	9.2	0.3	0.8	73.1	76.7
Greece	- 1,1	- 0.3	9.0	10.2	1.2	1.4	112.6	124.9
Spain	- 3.7	- 0.8	17.9	20.0	-0.4	0.8	54.3	66.3
France	- 2.2	1.2	9.5	10.2	0.1	1.1	76.1	82.5
USA	- 2.5	2.2	9.2	10.1	-0.2	0.2	-	-
Czech Republic	- 4.8	0.8	6.9	7.9	0.6	1.5	36.5	40.6
Hungary	- 6.5	- 0.5	10.5	11.3	4.3	4.0	79.1	79.8
Poland	1.2	1.8	8.4	9.9	3.9	1.9	51.7	57.0
Romania	-8.0	0.5	9.0	8.7	5.7	3.5	21.8	27.4
Bulgaria	- 5.9	- 1.1	7.0	8.0	2.4	2.4	15.1	16.2

* Estimates, ** forecasts
Source: European Commission

U.S. cooperation with the EU is a multilateral development force.

❖ Gradually overcoming the global financial crisis in United States

President Barack Obama faced since the beginning the global economic crisis and its deep resistance, but this was gradually overcome with the first results. He also spurred the residential market conditions in which measures were threatened by unemployment and the prescription of mortgages. The number of foreclosure cases reached 3 million working places.

When the President faced the economic difficulties, he was prepared to act through several government constraints on the banks and on the operations carried out in the banking

sector. Restrictions were created for the largest financial institutions of state.

As banks would become so large as to constitute a threat to the global economy, Obama supports measures proposed by Paul Volker, former Chairman of the FED, decades ago, whose vision with a long term impact, supports the elimination of risky banking activities but favors however the Treasury operations. Volker wants to limit the transactions with their own assets, made by the commercial banks, to restructure banks' bets using equity. Administration officials want "walls" between different divisions of financial companies, to ensure that banks are indirectly subsidizing hedge transactions through other branches with deposits insured by the state. Are concerned primarily the giants, Bank of American, Wells Fargo and JP Morgan Chase,

controllers of a large part of U.S. deposits, plus Goldman Sachs and Morgan Stanley and Citigroup, present on Wall Street.

Once the proposal entered into force, larger banks may be forced to transfer the activities from the traditional sectors to other investment divisions, where the transactions are made, the titles are sold to customers, and the banks are betting on the markets. Structures investment banks have increased considerably in recent years and have become profitable.

The banks have new rules, to hold and manage blocks of hedge funds, private equity and real estate investment.

In the daily paper the Guardian, Catalina Apostoiu published the following passage from her article: "The imposition of restrictions on commercial banks' high-risk transactions would result in restricting the size of the institution, which is "too big to collapse" and prevent further financial crises. Volker's important measures refer to partially reintroduce the division between commercial and investment banks.

The Republican Mike Johanus believes that the proposed legislation does not lead to the collapse of Bear Stearns and AIG. Bankers argue that trading with their own assets is impossible to define and leads to partial re-division of the commercial and investment banks. Government officials will try to implement new regulations in foreign banks with U.S. operations.

Banking Committee Chairman, endorses Obama's new proposals, but he considers them to be delayed, as well as launching several ideas is seen as a mistake.

Volker warned the Committee that if the Congress disagrees with the imposition of restrictions on risky activities, there will be many financial disasters.

However, the first problem continues. Bank of America offers bonuses of \$ 4 billion. The management

of Bank of America has spent over \$ 4 billion last year for the salaries of the employees traders and investment divisions (the Bank pays 300,000 - 500,000 U.S. dollars to each person). The payments represent 19% of the \$ 23 billion revenue, achieved by the bank from investments and from the banking divisions with capital markets operations. Salaries in 2009 are close to those granted in 2006, with high payments. In the fourth quarter of last year the Bank recorded a loss of 5.2 billion dollars.

❖ **Barack Obama: fundamental changes in the banking system**

Obama, by reducing the risks assumed by the banks – which depend on the regulatory mechanisms, defines the bank transactions with his own assets.

Obama's proposals include also the plan to reduce the transactions with his own assets made by banks, which are supposed to strengthen the U.S. financial system, and to avoid repeating the credit crunch that led to the current global crisis.

The transactions with the own assets aren't carried out in clients' interests. They will have the authority to require the regulatory bodies of the banks, information about specific transactions, whether they are made in the interests of customers.

When they are not made for the client, the regulators ask the banks to give up that position on the exchange. Also, the banks are prohibited from investing in hedge funds and private companies. The American president will also cover the lending process and will try to limit it, to avoid the new "bubble" phenomenon.

Obama's plan verifies the size of the banks and aims to extend the 10% currently required only in terms of market share of deposits and other liabilities. The target wants to limit the activity concentration, which unfolded over the

past 20 years and increased during the crisis, and the healthy banks wanted to buy the banks threatened by bankruptcy.

A remarkable success in engaging projects of the President is the approval of the Congress's lower house regarding universal health insurance. The policy initiative dates back nearly a century, but without any results, so far the votes were close, 219 "for" and 212 "against". This law was not supported by any member of the Republican opposition, even though they have vowed to enter it into force law. The enactment in force since 2014 guarantees health insurance for 36 million Americans, in applicable terms.

According to the target, 95% of Americans, aged 65 years have sickness insurance. If an American citizen is not included in programs such as Medicare or Medicaid - programs for poor people – he is required to promote a health insurance, otherwise he has to pay a fine, which is applied annually. The insurance companies can't refuse to end payments for individuals and especially for kids who are already sick.

According to the Congressional Budget Office, the health insurance reform will cost 940 billion dollars in ten years and in the same time, will reduce the budget deficit by 138 billion dollars.

❖ **Preparation of financial markets reform**

The long analysis of reform of the U.S. financial markets has reached the limits of knowledge and operational radical transformation of the banking system, in order to prevent long-term return and the difficulties posed by the banks' return to a compromised system. Knowing this, the President Barack Obama submitted to the U.S. Senate debates, the current form of the financial market reform. The Wall Street Journal writes: "The measures include provisions that the banks' profits will be strictly controlled, and capital requirements will

be higher, but the executors' payments must have reasonable values. Once the project is passed, the financial products will be supervised and the authorities may divide large institutions. The bill presented to the Senate by the Banking Committee Chairman, Mr. Christopher Dodd, will divide the participants into winners and losers.

The winners from small banks will compete with large companies and new capital restrictions. ECB (EDF) and the FDIC redefine their tasks. Big financial companies will contribute to a fund of 50 billion dollars to cover possible losses.

The application processing implies drastic and necessary measures, such as: financial products are supervised by the Government, large banks under the supervision of prosecutors, FDIC Central Bank redefines its powers in many ways, a consumer protection agency is created inside the FED, a council of nine members is responsible for the financial stability; the involvement of banks in trading operations is limited, as well as in investments in hedge funds and private equity.

European Central Bank President, Jean-Claude Trichet believes that the process of the European economic recovery in the global recession will be moderate, in an insecure and irregular background.

The President of the European Central Bank says: "The recent decline of the international trade was very pronounced, rapid and synchronized. He has exceptionally added:" This means that the European recovery process, a commercial superpower, will probably be uncertain."

According to the President, the withdrawal of the extraordinary support measures introduced by the ECB system, during the crisis will depend on the medium-term prospects "The world economy - says the author - just started to emerge from a prolonged period of turbulence. In the ECB, the gradual

withdrawal of the exceptional measures which support financial system will depend on medium-term prospects." He also believes that long term measures will boost the trading activities of the banks, but in the same time will stimulate less their role in corporate and consumer lending sector.

Lending is not currently constrained by a shortage of liquidity in the financial system. As President Trichet says, "In several euro area countries general standards for lending companies began to relax."

European Central Bank warned that the imbalances from the global economy, which stimulated the financial crisis, risk to deepen again and to threaten the recovery.

Spain is under surveillance for a long time but this doesn't imply anything. This time, Spain demotion for long term loans by the credit rating agency Standard & Poor's, has surprised the financial markets.

Madrid authorities have given assurances that Spain will not have problems with the repayment of the debt amounting to 16.2 billion euros, due in July. Jose Manuel Camp ensured that the rating review will not affect Spain's problems. As regards the European lenders, they have an exposure of 240.5 billion dollars in Portugal.