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Global Economic Crisis and Brazil: What Are the Questions?

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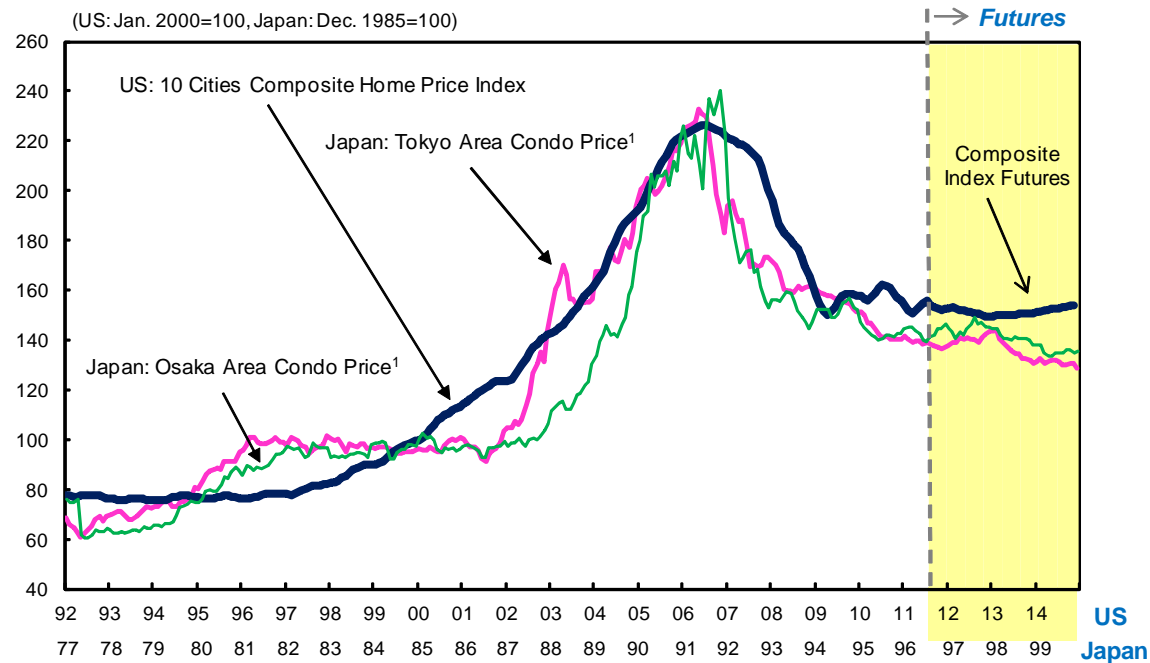
Global Economic Crisis

- Global Financial Crises
 - Centered in US and Europe
 - Is a collapse of paradigm/west model and governability?
 - What will be the social and political consequences of the financial crises?
 - Nature of the crises: burst of super-bubble?
 - Solution for each bubble was another bubble
 - Solving problems of liquidity to mask solvency problem?
 - Demand of financial assets is function of their prices during crises increasing the instability
 - Euro crises

Global Economic Crises

- Financial crises vs Balance sheet recession
 - Lenders problems: monetary policy can help
 - Another bubble?
 - It will take at least a decade of very low interest rate (subsidies) to save the financial system.
 - Borrowers problem: only fiscal policy can help
 - Families and business sectors are adjusting their balance sheet, deleveraging and increasing the excess savings (Richard Koo).
 - Prolonged slump
- Crisis of governability of US and Europe: economic and political vigor passing to developing countries?

Exhibit 1. US Housing Prices Mirror Japan's Experience

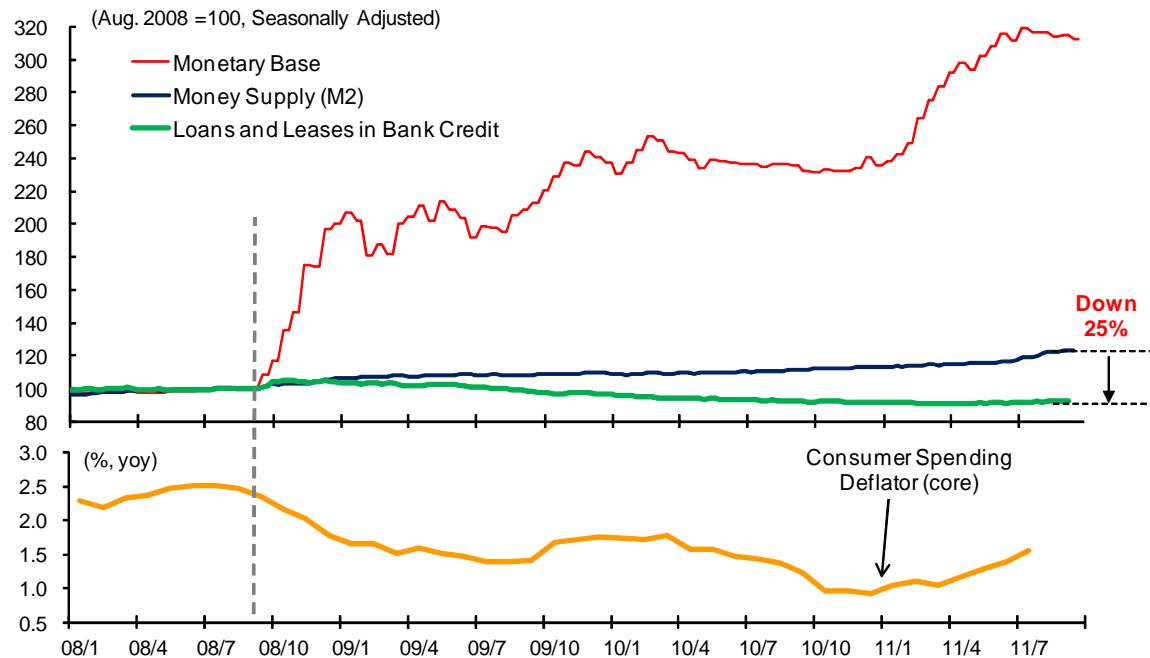


Note: per m², 5-month moving average

Sources: Bloomberg, Real Estate Economic Institute, Japan, S&P, S&P/Case-Shiller® Home Price Indices, as of Oct. 5, 2011

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

Exhibit 2. Drastic Liquidity Injection Failed to Increase Money Supply (I): US

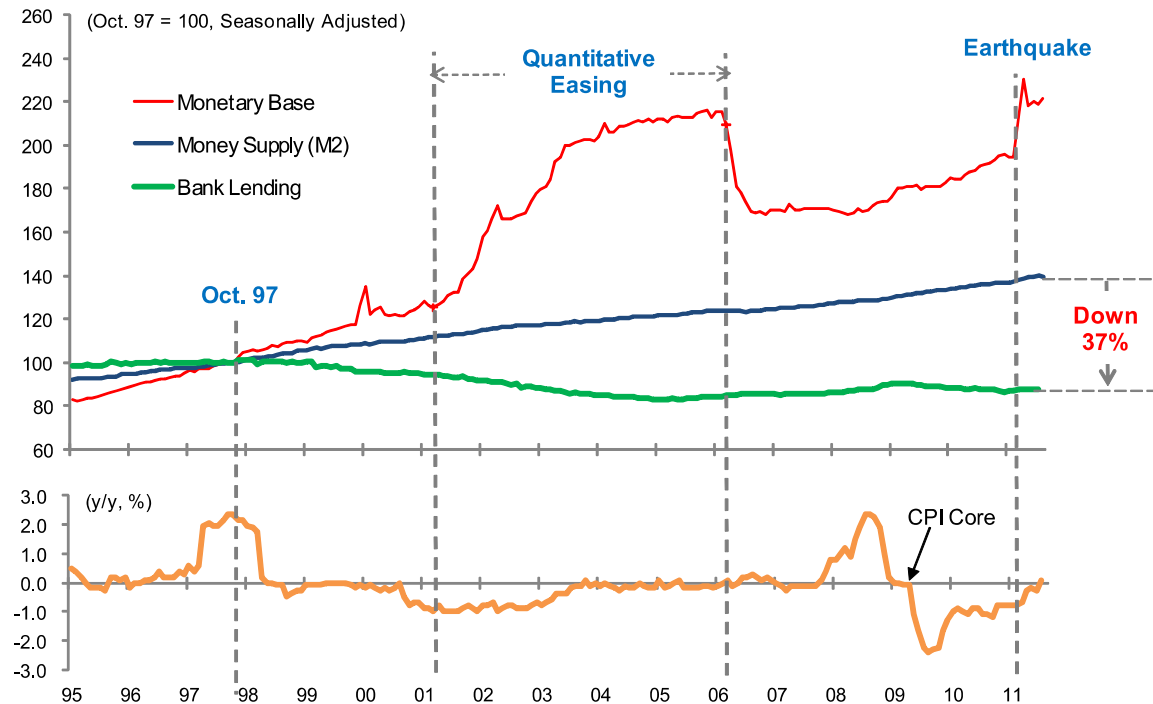


Sources: Board of Governors of the Federal Reserve System, US Department of Commerce

Note: Commercial bank loans and leases, adjustments for discontinuities made by Nomura Research Institute.

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

Exhibit 4. Drastic Liquidity Injection Failed to Increase Money Supply (III): Japan

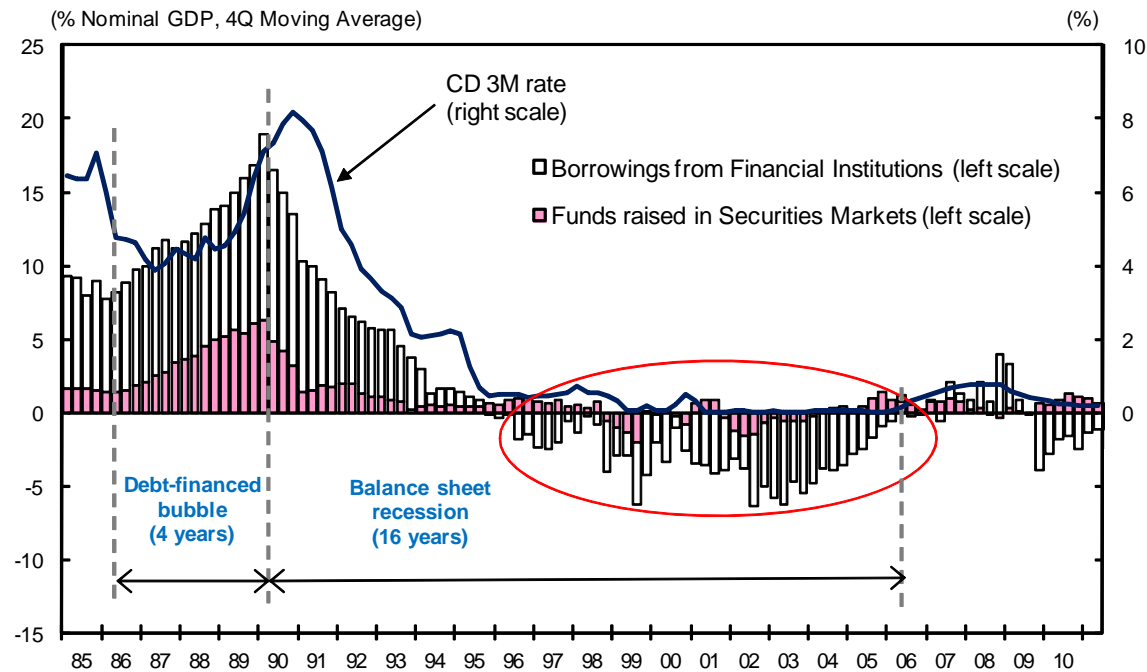


Note: Bank lending are seasonally adjusted by Nomura Research Institute.
Source: Bank of Japan

Source: Koo, Richard. “Two World in Balance Sheet Recession: Causes, Cure, and Politics. *Real-world economics review*, issue 58, 2011.

Exhibit 5. Japan's Deleveraging under Zero Interest Rates Lasted for 10 Years

Funds Raised by Non-Financial Corporate Sector

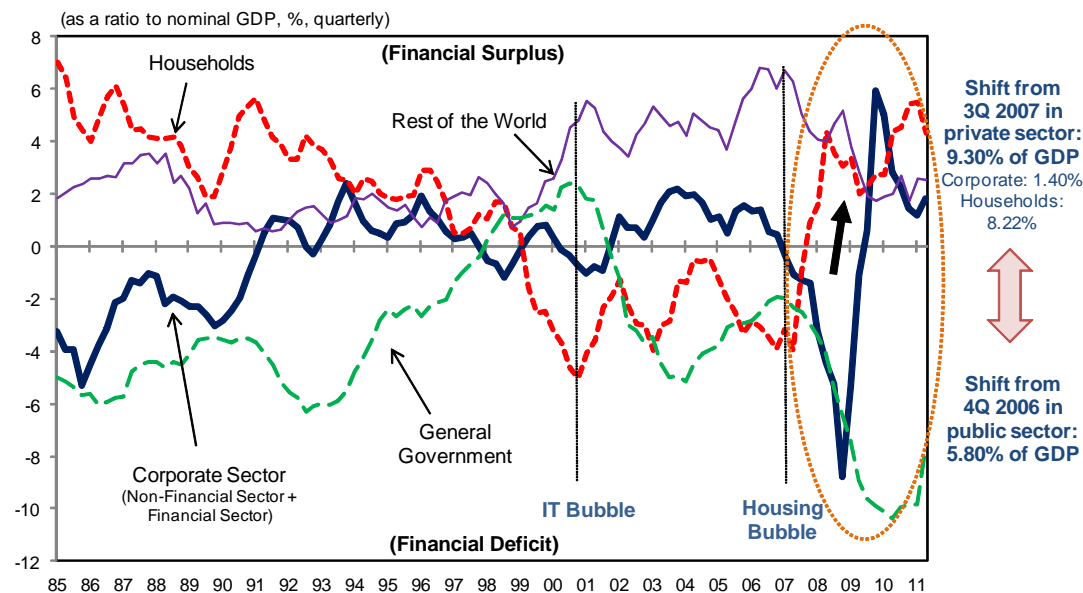


Sources: Bank of Japan, Cabinet Office, Japan

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

Exhibit 9. U.S. in Balance Sheet Recession: U.S. Private Sector Increased Savings Massively after the Bubble

Financial Surplus or Deficit by Sector

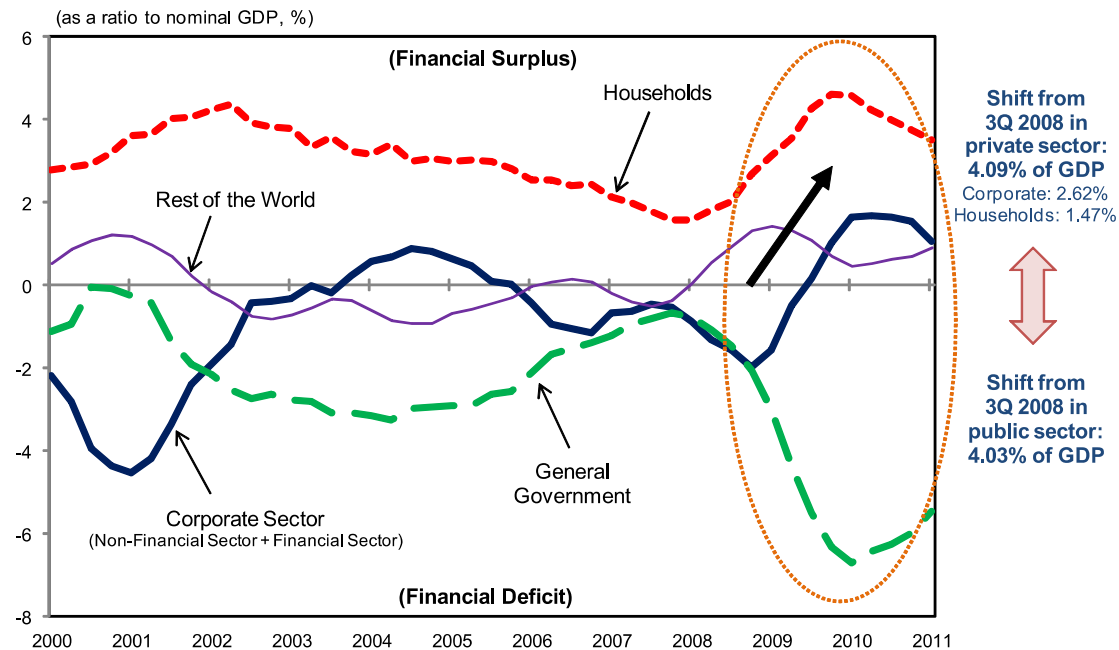


Note: For figures, 4 quarter averages ending with 2Q/11' are used.
Sources: FRB, US Department of Commerce

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

**Exhibit 14. Eurozone in Balance Sheet Recession:
Massive Increase in Private Savings after the Bubble**

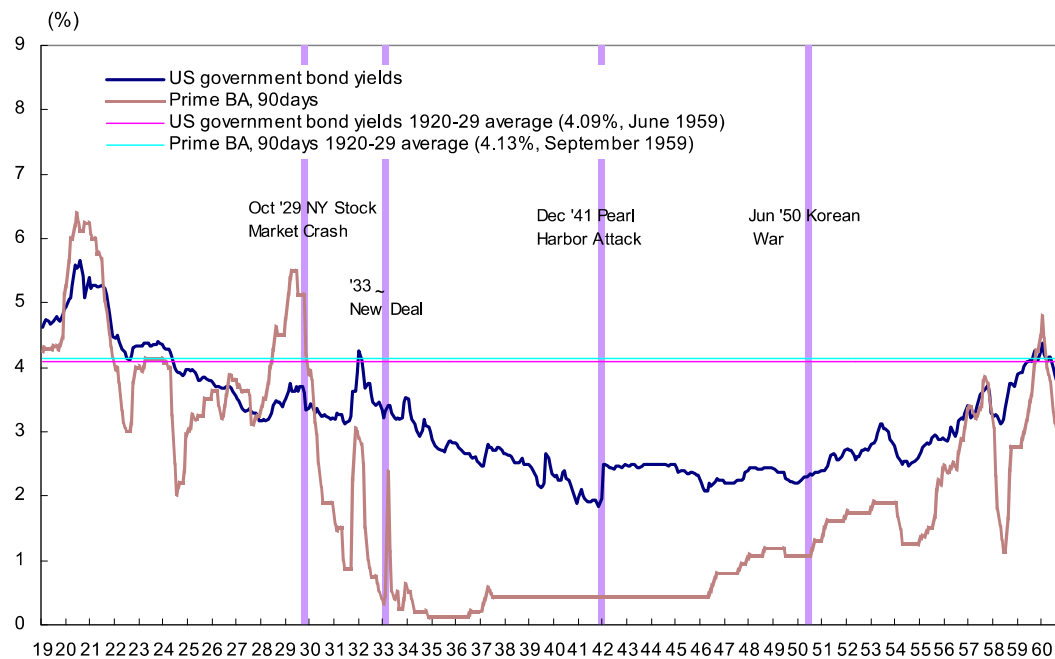
Financial Surplus or Deficit by Sector



Note: For figures, 4 quarter averages ending with 1Q/11' are used.
Source: ECB

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

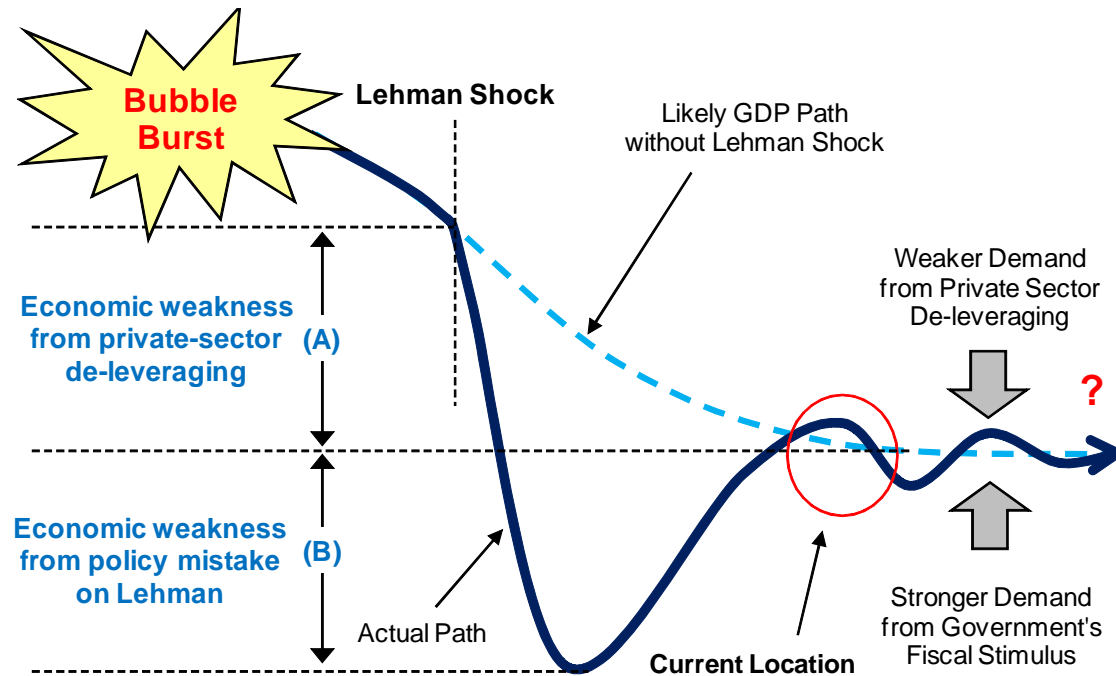
Exhibit 15. Exit Problem: U.S. Took 30 Years to Normalize Interest Rates after 1929 because of Aversion to Borrowing



Source: FRB, *Banking and Monetary Statistics 1914-1970* Vol.1, pp.450-451 and 468-471, Vol.2, pp.674-676 and 720-727

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

Exhibit 16. Recovery from Lehman Shock Is NOT Recovery from Balance Sheet Recession



Source: Nomura Research Institute

Source: Koo, Richard. "Two World in Balance Sheet Recession: Causes, Cure, and Politics." *Real-world economics review*, issue 58, 2011.

New Global Economic Order

- Hegemonic Interregnum (vacuum of dominant power, of ideology and of policy consensus, etc.)
 - Redistribution of power and leadership in world economy
 - From US hegemony to Chinese hegemony

The Economist: China will overtake USA in 2018 in terms of GDP in dollar.

Who will prevail in western Pacific: US Navy or rising industrial and naval power of China? And India?
 - From financial plutocracy to industrial plutocracy?
 - Historical similarity with the decline of British financial plutocracy and rise of American industrial power

New Global Economic Order

- From global capitalism to state capitalism?
 - Which model will prevail?
 - Decline of market led liberal globalization?
 - Rise of protectionism and nationalism?
- What will happen to capital movement and financial integration?

New Global Economic Order

- Greater external autonomy for peripheral countries
 - US declining governability and global governance/priority in next decades will be to revitalize itself.
 - Rise of New Nations States with rising vigor?
 - New international division of labor or reindustrialization and rise of new regional industrial powers?

Global Economic Order and Brazilian Development

- Brazilian historical experience during hegemonic interregnum
 - From Great Depression of 1890s
 - Immigration, end of slavery, Republic and take off of the construction of modern Brazilian society
 - From Great Depression of 1930s
 - Displacement of dynamic center and industrialization
- From Resilience to 2008 Crisis to Robust Growth?

Resilience of Brazilian Economy

- Very low export to GDP ratio;
- Large and dynamic domestic market;
 - End of “Labor Surplus Economy” and new dynamics of domestic market/mass consumption/new middle class

Resilience of Brazilian Economy

- Improving macroeconomic policy: From stability to Stability + Growth
 - Fiscal policy: small deficit and low debts that could afford to become counter-cyclical
 - Monetary policy: flexible, richer and expanded inflation targeting + plus
 - External reserves

Resilience of Brazilian Economy

- Beginning of growth cycle with favorable commodities prices
- Diversified manufacturing industry
- Natural resources and energy

Fragilities of Brazilian Economy

- Weak institutions: patrimonial state captured by bureaucracy and allied forces imposing very high taxation on productive sector
- Heritages from high inflation period: high level of interest rate and indexation of financial system
- Natural resources curse?
- Overvalued exchange rate and premature deindustrialization
- Low rate of investment/low saving rate of public sector

Why Brazil May Succeed

- In the last few years Brazilian GDP has been growing 4%, fast enough to propel the economy and turning easier to solve problems.
- The crises of US global governance and decline of conventional economic thinking, Brazil have to think by itself searching for a new model.
- “Slowly” Brazilian state are recovering capacity of strategic planning.
- Strong political demand of stability and growth by the large and better educated “new middle class”
- High potential growth (catching up)