Fighting the 2008 Financial Crisis

How will History judge Central Banks ?

Rotary International Club, Geneva, 13 February 2020 / Jean-Pierre Roth

When markets opened, on Thursday August 9 2007, major Central Banks injected massively liquidity in their respective money market in order to avoid a global paralysis of the inter-bank activity. Rumors were surging in the US and in Europe about the solidity of large financial institutions having invested in the "subprime market". The financial crisis was born.

Who was guilty ? …the banks of course !

- they had given too much credit
- they took too much risk
- they were operating with too little capital
- they invested in opaque assets
- … and all bankers had become greedy !

but : Governments also made mistakes

- with low inflation due to globalization, monetary policies were too loose
- capital requirements had been reduced in order to expand credit
- excessive confidence in ratings and modelling
- massive support of the housing market in the US
- the euro operated as tranquilizer in the South of Europe

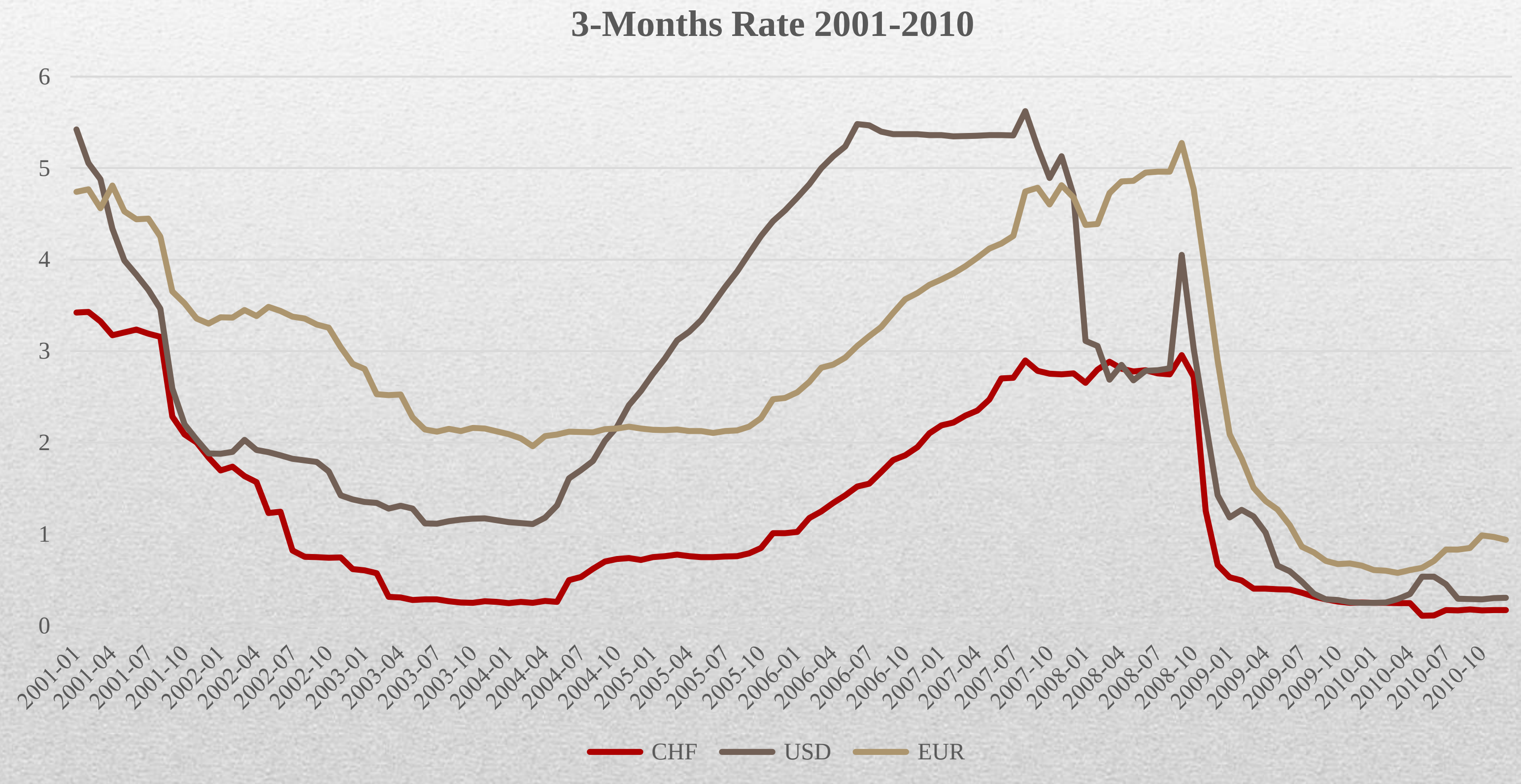
… the years 2000-2004 were dominated by an atmosphere of financial "benign neglect", which weakened the financial architecture

2007 : Central Banks started to act

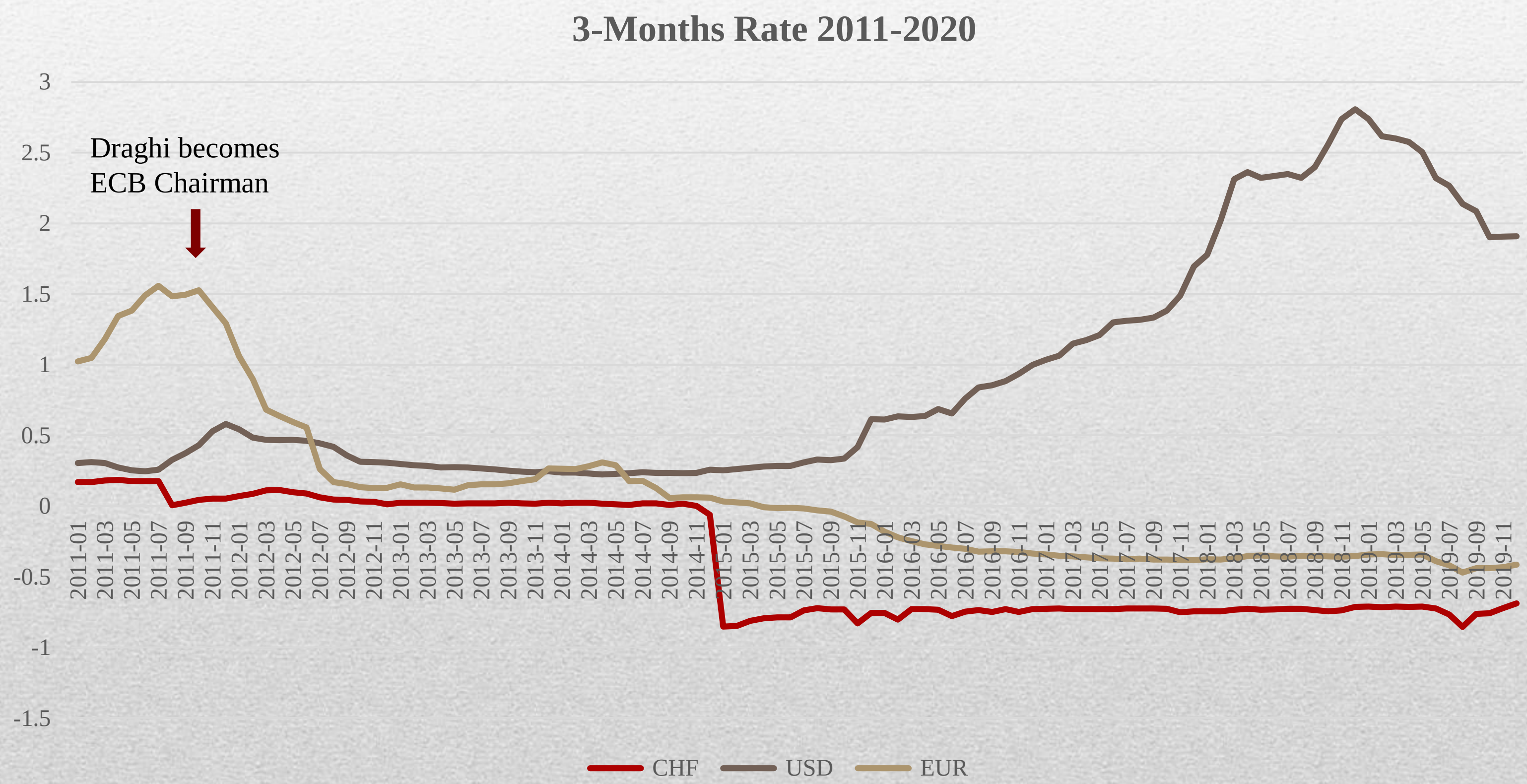
- **preventing financial stability top on the agenda**
  => unlimited support to systemic institutions
- **reorientation of monetary policies**
  => implementation of non-conventional policies
- **financial stimulus**
  => avoid a "credit crunch"
- **penalization of savings**
  => negative interest rates

… in one word : avoiding the mistakes of the 1930s

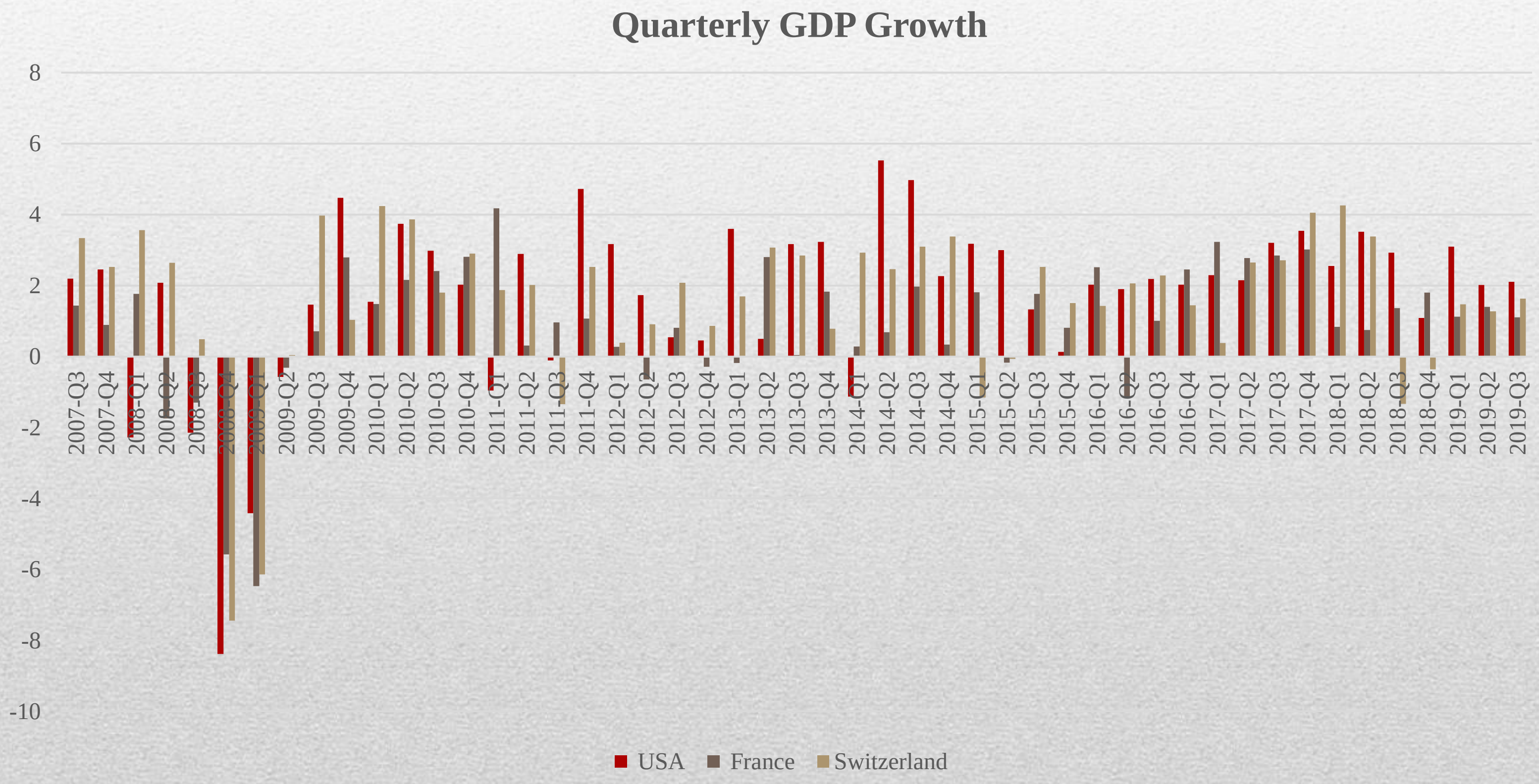
impressive impact on the market…



but the music went on…
… in Europe



… despite global recovery



…have Central Banks been too complacent? YES

- non-conventional policies should not last
  => we still live with negative rates
- coordination with Governments is an illusion
  => Governments prefer waiting and enjoy debt
- penalizing savings does not foster confidence
  => anxiety about future pensions
- lasting non-conventional policies generates speculative bubbles
  => stock market and real estate inflation

2020 : back to normal ?
NO

- **lasting imbalance of global savings / investment**
  => low real interest rate with us for years
- **Ms Lagarde's reassessment of ECB policy**
  => no revolution to be expected
- **will confidence in the banking system be restored ?**
  => no early signs so far
- **public debt increasingly a problem**
  => pressure on Central Banks no to raise rate

Central banks prisoners of the negative rate trap !

Consequences for Switzerland

- **ECB policy forces SNB to maintain negative rates**
  => fragility of pension funds
- **political pressure on Switzerland as surplus country**
  => risks of discrimination
- **no fascination for EU membership**
  => bilateral agreements at risk
- **Swiss franc remains strong**
  => continuous SNB interventions