Crisis Economics: A Crash Course in the Future of Finance

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Nouriel Roubini, and Stephen Mihm (2011). Crisis Economics: A crash course in the future of finance. Penguin Books Ltd, Price: Rs. 450, Pages 368, ISBN: 9780141045931.

The book by N.Roubini & Stephen Mihm reveals the methods regarding the recent financial crisis that has swayed the globe. They also speak on how this crisis could be put to use in improving future financial market. This book being an unconventional blend of history and economy throws light upon the inherently fragile financial system which is prone to collapse. It says that the economic disaster was probable and predictable but the politicians, policy makers, investors and market watchers had long neglected the facts and the indications of this devastation.

The book shows how we can grapple with the inherent instability of the global financial system, contemplate the pressure points of the system, learn from previous episodes and identify the course of global turndown. Blending economic theories, statistics and mathematical models, the book suggests the trick to counteract the crisis mess and stay out of the mess in future. The book is written in a lucid language. It examines why the recent crisis had hit the economy when it did; it says this crisis was our destiny and not a chance event. It narrates the history of older crises that have happened in the past and the economists who analysed them. It builds further, addressing the roots of the recent crisis. It also reflects the predictable pattern of the crisis. The book ultimately emphasises the reforms in financial system and how to avoid such type of crisis in future.

The first chapter narrates the past economic status of different nations. It talks about speculative bubble like Tulips Holland in 1630s, South Sea Bubble of 1720 and the first Global Financial Crisis of the 1980s. The book says that the crisis was neither the freak event nor the Rare Black Swan, but was commonplace, very easy to foresee and comprehend.

The second chapter ponders over the calm period of low inflation and high growth being termed as "Great Moderation". This is the prime reason that withholds the mainstream economists from talking about this crisis. It names a few renowned and a few less renowned economists who have spoken about the moderate period.

The third chapter explains the deep structural origin of the recent crisis. It has been much in vogue to hold the sub-prime crisis responsible for this economic drain. It highlights the efficacies in the financial systems that were sub-prime from top to bottom and was reliant on decade old trends and policies. The chapter narrates the rise of "Shadow Banking System" being a sprawling collection of non-bank mortgage lenders, hedge funds and other institutions that acted like banks but were never regulated like banks. The chapter introduces the problem of moral hazard adopted by market players for survival. It also introduces issues regarding regulations and corporate governance.

The fourth chapter compares this crisis with those in prior times. It narrates that the 2008 crisis had similarities to events that occurred hundreds of years ago but had been diffused by the governments acting as lenders of last resort.

The fifth chapter shows how and why the crisis went global and how it engulfed different economies such as Germany, Latvia, Ireland, Iceland, Dubai, Japan and Singapore. According to the authors the pandemics originated in United States and further spread to the rest of the world. The countries whose financial system suffered from similar frailties collapsed. This book is different from other writings on financial crisis as it broadens the canvas, showing a globally broadened crisis rather than being a local US crisis. This chapter reveals the myths and truths about global finance, international macro economics and cross-border implications of national monetary and fiscal policies. It also reveals the working of economies during normal and abnormal times.

The sixth chapter talks about how depression and deflation worsen any economic crisis. It throws light on monetary policies adopted by the central banks in the past to counteract the inflicted crisis. These crises have provided useful insights to the banks but the tactics adopted may prove disastrous in the end rather that contribute to controlling the crisis. The same goes with the fiscal policies.

The seventh chapter examines how policy makers used the taxation system to arrest the spread of crisis. This chapter evaluates the future implications of the most radical measures in terms of risk they may create in the long run. The book ponders over the role played by the governments in their attempt to stabilize after the crisis.

Chapter eight provides a state of the art blueprint of financial architecture to provide stability and enhance transparency in the system.

Chapter nine adds the long term reforms necessary for stabilizing the international financial system, the effective coordination among central banks binding regulation and supervision of commercial and investment banks, insurance companies, hedge funds, and derivatives. This chapter provides effective measures for the control of financial institutions and to reduce the popping up of asset bubbles. The capital and required liquidity of financial institutions is also discussed. Policy measures to reduce problems of moral hazards and to regulate fiscal costs of bailing out financial firms are suggested.

The tenth chapter proposes how to tackle serious imbalances in the global economy and suggest radical reforms of international monetary and financial order to prevent this type of crisis in future. It talks about reasons that have devastated the market economies over the last two decades. It narrates why only certain economies have survived and the rest have crashed. It raises issues like: How the current account imbalances have added to the financial block, What are the possible measures to resolve these issues, Is there any policy plan to restore the US dollar crash by global reserve currency, Whether IMF plays a role in global monetary decisions and Is it the lender of the last resort?

The book recognises the role played by the economic blocs to reform the finances. It argues that increasingly the powerful nations will profoundly shape the global financial system.

The concluding section keeps a close watch on the dangers that can possibly hit the world economy. The crisis has now ended but still the pitfalls and risks are large. The questions, will the global economy recover from the pitfalls or would the risks further engulf the economy, have been dealt with in the book. How would the governments deal with the debts? How would the public and private enterprises fight the debts? How would the increasing deflation affect the economies? Will the intervention of government be enhanced in the economies, would this contribute to economic upliftment? It looks forward on prospects that would help nations survive and thrive and not struggle and collapse.

The final chapters outline certain issues like: Effect of globalization on future crisis, Strategies to resolve global imbalances, Reformation of global capitalism. This book contributes to the resolution of restoration that has a reformed capital base. It suggests market oriented reforms that would not only liberate the endemic poverty but also stabilize the economy. The book offers a road map that guides the nations to stay away from financial crisis.

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