

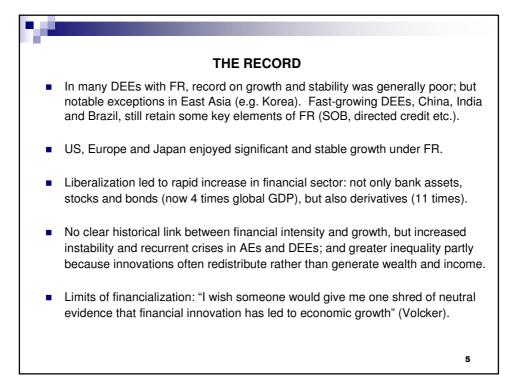


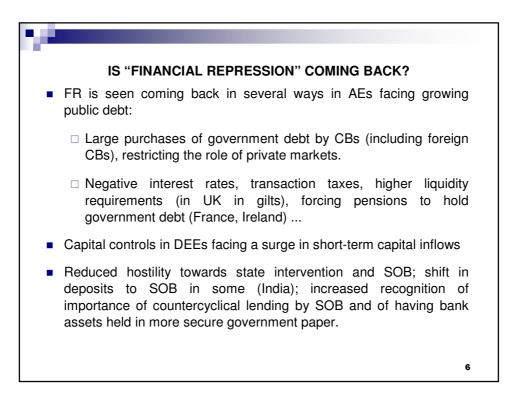
## POST-WAR "FINANCIAL REPRESSION"

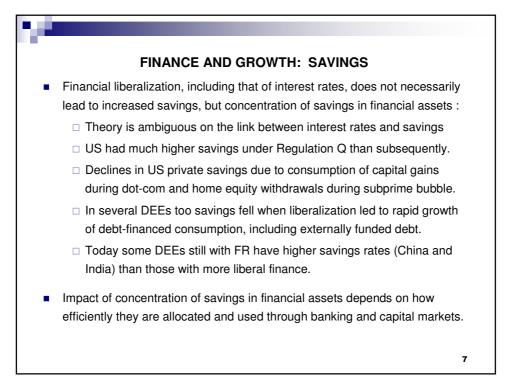
- Key elements:
  - 1. Extensive state ownership and management of banks
  - 2. Ceilings over deposit and credit rates and rates on government debt
  - 3. Directed credit allocation, differentiated lending rates.
  - 4. High and often non-remunerated reserve/liquidity requirements
  - 5. Capital account restrictions and exchange controls
- Cheap finance to governments. US Regulation Q (no interest on demand deposits and cap on savings deposits); negative rates on government debt; liquidation of war debt by 3-4% of GDP pa in US and UK during 1945-1980.
- In many DEEs and some AEs another objective was to promote rapid industrialization. In Japan moral suasion was used.

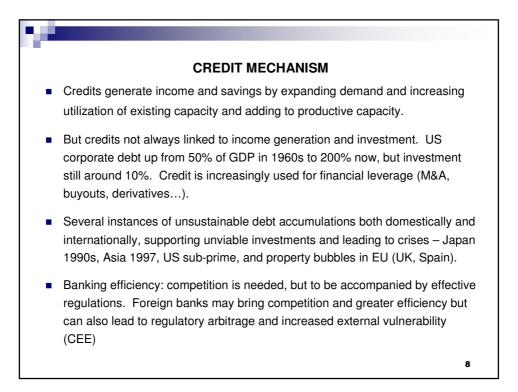
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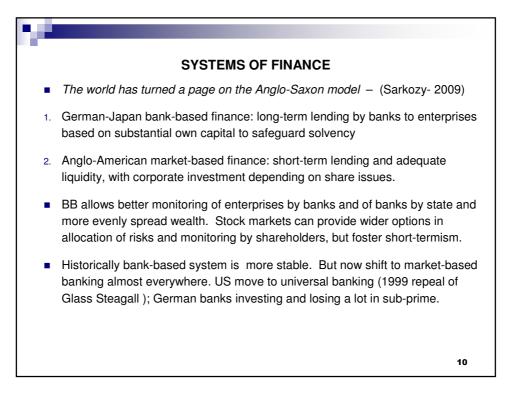




## CAPITAL MARKETS

- "There is no such thing as liquidity of investment for the community as a whole ... Capital markets provide liquidity to make investments which are 'fixed' for the community more 'liquid' for the individual" (Keynes)
- But, these liquid markets are also highly speculative and subject to volatile expectations and herd behaviour, creating bubbles unrelated to fundamentals and boom-bust cycles (US dot-com) and DEEs (stock market cycles in the 2000s).
- Search for yield and liquidity is pushing individual and institutional savers to capital markets almost everywhere. To meet competition, commercial banks are also tempted to go into securities, liquefying their non-traded claims via securitization (US subprime) or investing in securities (Germany). Increased exposure of banking to capital market volatility – also in some DEEs.

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## THE GLOBAL DIMENSION: CAPITAL FLOWS AND FINANCIAL STABILITY

(Bernanke): "Looking back on the crisis, the United States, like some emerging-market nations during the 1990s, has learned that the interaction of strong capital inflows and weaknesses in the domestic financial system can produce unintended and devastating results. The appropriate response is ... to improve private sector financial practices and strengthen financial regulation, including macroprudential oversight. The ultimate objective should be to be able to manage even very large flows of domestic and international financial capital in ways that are both productive and conducive to financial stability."

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