ADDRESS TO CEEF FUNDRAISING DINNER

JOHANNESBURG COUNTRY CLUB

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Dear Friends

In the light of the present circumstances, where every day each one of us is called upon to articulate views on trends in the global economy, it is fairly safe to declare, “We are all economists now”. And, in view of the size of stimulus packages across the world, it may even be safe to declare, as Ronald Reagan did in 1971, “We are all Keynesians now”.

Commentators of every hue are falling over each other to conjure up the most apt description of the nature of the crisis….. and analogies abound.

My favourite for now, is the description by Graydon Carter,

> As far as the global economic crisis goes, part of me thinks the U.S. has gone off a cliff pretty much the way Wile E. Coyote does in the Road Runner cartoons. He doesn’t drop immediately; he’s suspended in midair.

> He knows he shouldn't be out there, but he's not plunging! Filled with hope, he begins to gingerly tiptoe his way back to the ledge. He's almost made it—he's not going to fall! And then, with a puff of dust, he's gone, plummeting far, far down into the canyon. As a nation, we might just be in the tiptoeing stage: we know we've screwed up big-time, but we're praying that we can get back to the ledge before gravity takes over.

Perhaps the most over-used analogy is that "we are sailing in uncharted waters." Fair enough, the waters are quite uncharted. So shouldn't we, as rational beings, pause and ask how we got the global economy into these waters? There are four possibilities that present themselves

- As with Coyote's Road Runner, the global economy (and not merely that of the USA) went over the cliff, into the canyon where below were these uncharted waters; or
- We were actually flying past, rapidly lost altitude and crash-landed in these hostile, uncharted waters; or
- We lost direction, could not navigate our way through anything, couldn't read the instruments and ended up in these awful uncharted waters; or
- Perhaps somebody steered us into these waters intentionally.

Would any present wish to judge between these four options and clarify for all the world that we are seriously in the wrong place? The observation that we should agree on is that after repetitive turns and bumping into things, we must reluctantly conclude that we are trying to navigate ourselves out of this place with quite the wrong equipment, technique and skills. In plain English, we are floundering.

A few selective indicators comparing trends in selected countries over the past twelve months tells the story:

The budget figures for the USA for example, show an increase in the budget deficit from 2.4% in 2008 to 13.7% in 2009. Similarly, the budget deficit for Britain increased from 3.2% to 11.3% over the same period. Saudi Arabia provides somewhat of a starker example of just how acute the situation has become. In the space of just one year, its budget balance went from a 12.8% surplus to an 8% deficit. Its current account balance moved from a 22.8% surplus to a 7.9% deficit – this too in just 12 months.

These are not the worst, by a long shot, but they present the picture of the speed of transition from well-managed economies with a positive picture to one that tells the story of countries heading rapidly into the abyss.

Over the past decade, Ireland was held up to all as a country that has mastered the challenge of development. Since January this year, Ireland has been hit by wave upon wave of negative announcements. First, the luxury brand Waterford Wedgewood was placed in receivership. Then, Dell announced the closure of its computer factory and then the government had to nationalise the Anglo Irish Bank, its third-largest lender. Suddenly, a country that ran fiscal surpluses for many years, now faces a fiscal deficit of 9.5% this year, and after a decade of high growth faces a contraction of at least 4.5% this year and from virtually full employment suddenly has shifted to unemployment of at least 10%.Without a shadow of doubt, the Irish economic bubble has burst.

The story for a number of countries appears to be as gloomy.

In the face of all of this, South Africa may not be doing too badly. However, while our economy may not be deteriorating at a rate as intense as so many other countries, we continue to monitor signs carefully. As I mentioned in my budget speech this year, consequences are felt everywhere. When global automobile production decreases, the factory in the Eastern Cape making catalytic converters for cars is affected. So, too, is the mine in Rustenburg producing platinum for the converters. The worker in the factory and the miner in Rustenburg are now without work. And the woman who runs the little vegetable stall outside the mine is making less money each week. Their families, all of them, face a future made more precarious by the vagaries of global finance.

The key global challenge is whether we have the wherewithal to extricate the economy from these hostile uncharted waters. In this context we have to look to the actions, or more particularly the stimulus packages of the world's largest economies. There are, according to Kemal Dervis, the Administrator of the UNDP, four measures that we should use together:

“First, public authorities must restructure and rewrite balance sheets in the financial sector, when necessary by taking over banks, instead of waiting any longer. Second, public expenditure must replace faltering private demand to reverse the downward spiral before it becomes a rout. Third, this must be done with international co-operation so that the global current account imbalances that contributed to the crisis will diminish rather than increase. Fourth, there must be aid to the most vulnerable so that they will not be pushed into destructive despair.”

This is a fairly useful measure against which to evaluate the stimulus packages. Few of these have escaped detailed criticism. In a recent article, Joe Stiglitz raises the following concerns about the stimulus package of the USA. He argues:

- Delaying bank restructuring is costly, both in terms of the eventual bail-out costs and in terms of the damage to the overall economy.

- Governments do not like to admit the full costs of the problem, so they give the banking system just enough to survive, but not enough to return it to health

- Bankers can be expected to act in self-interest on the basis of incentives. Perverse incentives fuelled excessive risk-taking, and banks that are near collapse but too big to fail will engage in even more of it.

- Socialising losses whilst privatising gains is more worrisome than the consequences of nationalising banks.

- Don't confuse saving bankers and shareholders with saving banks.

- Trickle-down economics almost never works. Throwing money at banks hasn't helped homeowners; foreclosures continue to increase.

- Lack of transparency got the US financial system into this trouble, and lack of transparency will not get it out.

Perhaps less effusively but with the same amount of detail, there is a similar critique of most Western European stimulus packages. Over and above the points raised by Stiglitz, there are repeated questions about the risks of a liquidity trap, whether the stimulus will create the necessary improvements in effective demand, whether there is a matrix to measure whether the stimulus may not aggravate the exit route and whether there is sufficient co-ordination because the alternative – essentially beggar-thy-neighbour policies – will leave the global economy trapped in a hostile environment for so much longer.

In this context the shining beacon is the quality of the stimulus announcement of a $589 billion package by China that has been widely vaunted. Its focus is clear - post-earthquake infrastructure; the stimulation of domestic demand; industrial restructuring and the construction or strengthening of the social safety net.

Most world leaders would recognise this, though few would admit that this stimulus package meets all of the criteria set out by Kemal Dervis (above) and would be fully resonant with the true Keynesian tradition. A number of interesting questions arise – will China be willing to lead the world? Or perhaps more importantly, would the world acquiesce to Chinese leadership? Or will the recognition that the Western model for development has failed be too much asked?

I do not wish to digress to draw attention to the failure of multilateralism. How different may this situation have been if the world's wealthiest countries had conceded to peer review or some outside influence.

For now, we should concentrate on the monumental and collective effort to get the global economy out of its current hostile environs. So where is the great destination? Might it be a caring and well-developed socialism distinct from the soviet past? Might it be towards a different capitalism, essentially freed of the excesses which the past thirty years have demonstrated? Or might it be towards a new hybrid, one that is more caring, demonstrating both the intent to support innovation whilst acting in a determined manner to close the chasm of inequality.

This is a debate we must have. For now, let us focus our collective attention on how to extricate the global economy from its present place in a way that does not aggravate the ravages of the immediate past.

Thank you.