

**TWENTY FIRST FEDERATION OF AFRO-ASIAN INSURERS  
AND RE-INSURERS (FAIR)**

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**PLENARY SESSION 1 – FINANCIAL CRISIS: STRATEGIC  
IMPACT AND RESPONSE**

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## **Crises are Common and Regular...**

- **Crises are endemic to the capitalist system.**
- **Beyond business cycle. Slowdown but not deep and prolonged.**
- **Crises are breakdowns. Collapses.**
- **Real side crises. Financial side crisis. Financial crisis affect real side. Growth contraction.**

## **Collapse of financial institutions and liquidity crunch...**

- **Crisis started in USA with the sub-prime mortgage crisis. Hundreds of billions in mortgaged-related investments turned bad.**
- **Banks and investors devised a wide range of complex financial instruments to slice up and resell mortgage-backed securities.**
- **Lehman Brothers collapse shocked confidence of bankers and investors. Liquidity crunch in interbank market and banks reluctance to lend.**
- **Bear Stearns collapse in March 2008. Treasury took over Fannie Mae and Freddie Mac in September, 2008. Mid-September Treasury decided not to salvage Lehman Brothers. AIG bailed out because of its exposure to CDSs.**

## **Crises are common and endemic...**

- **IMF study showed past 38 years – 398 episodes of banking, currency or debt crises in 161 countries or 10.4 crises/year, about once a month.**
- **Currency crises (208) most common. Twin and triple crises.**
- **1990s – banking crises  
1H 1980s – currency crises  
1980s – sovereign debt defaults.**

## **Uncertainties of depth and duration of financial crisis...**

- **Worst crisis after Great Depression of 1930s**
- **Typology of crises – currency, foreign debt, banking and systemic financial crisis.**
- **Excessive liquidity. Excessive lending. Excessive risk taking.**
- **Types of effects – first-order effects with credit linked losses, second-order effects with spillover to other financial markets, third-order effects with spillovers to real economy.**

## **Impact of financial crisis – extensive and deep...**

- **Financial impact. Real side impact.**
- **Geographical spread and severity varied.**
- **USA, Europe bore brunt of impact.**
- **Differential impact on Asian economies.**

## **Collapse of banks and financial institutions...**

- **Derivatives and crisis. Derivative products increased from US\$80 trillion in 1998 to US\$197 trillion in 2003.**
- **Enormous risks. Extent of exposure unknown.**
- **Insurance firms involved in derivative transactions especially as writers of credit default swaps (CDSs).  
AIG created CDSs. Lost faith of market.**
- **Collateral needed and more needed when firms downgraded by rating agency. AIG was caught.**

## **Real Side slide into recession...**

- **Economic activity in high-income and developing countries fell abruptly in 4Q2008 and 1Q2009. Production, trade and GDP down.**
- **Rise in unemployment and poverty.**
- **Commodity and delays in investments. Reversal in private capital flows sharpen further fall in domestic demand. Investment fell by 16.4 percent per annum in 27 of 30 high income economies in 4Q2008 and in 25 developing countries by 25 percent per annum. Capacity utilization below 70 percent. Collateral needed and more needed when firms downgraded by rating agency. AIG was caught.**
- **World economy for World Bank GDP was 1.9 percent 2008, expected – 2.9 percent 2009, 2 percent in 2010 and 3.2 percent 2011. East Asia better in 2009 (1.2 percent GDP growth) and 2010 (4.4 percent) especially China (6.5 percent in 2009 and 7.5 percent 2010) Singapore and Malaysia in recession in 2009.**
- **IMF outlook in October more optimistic than World Bank for 2009-2010.**

## **Global slowdown in FDI flows...**

- **FDI flows affected in 2008 and 1H2009. Inflows fell by 14 percent in 2008 to US\$1,697 billion from US\$1,979 billion in 2007.**
- **1H2009 FDI flows declined faster in developed economies.**
- **FDI inflows in 2008 plunged by 29 percent and outflows by 17 percent. 1H2009 inflows probably will fall by 30-50 percent.**
- **FDI inflows for developing and transition economies rose in 2008. Declined by late 2008 with economic downturn in export markets.**

**Table 1: Investment Demand Fell Sharply Worldwide**

	United States	Japan	Germany	Korea, Rep. of	Brazil	Russian Federation	Malaysia	Mexico	Lithuania
	(Growth in real investment, seasonally adjusted annual rates, percent)								
2007	-3.1	0.7	4.5	4.2	13.7	21.1	9.6	5.0	20.8
2008Q3	-5.3	-9.7	0.8	0.2	38.0	-13.9	1.7	1.9	-9.5
2008Q4	-22.0	-14.6	-10.2	-23.6	-33.9	-23.4	-34.5	-13.2	-45.2
2008Q1	-37.3	-27.5	-28.6	0.7	-	-30.4	-13.7	-	-65.8

**Source:** World Bank; national statistical agencies.

**Note:** - = Not available.

## Table 2: The Global Outlook in Summary

	2007	2008	2009e	2010f	2011f
<i>Real GDP growth<sup>e</sup></i>					
World	3.8	1.9	-2.9	2.0	3.2
Memo item: World (PPP weights) <sup>f</sup>	5.0	3.0	-1.7	2.8	4.0
High income	2.6	0.7	-4.2	1.3	2.4
OECD countries	2.5	0.6	-4.2	1.2	2.3
Euro Area	2.7	0.6	-4.5	0.5	1.9
Japan	2.3	-0.7	-6.8	1.0	2.0
United States	2.0	1.1	-3.0	1.8	2.5
Non-OECD countries	5.6	2.4	-4.8	2.2	4.6
Developing countries	8.1	5.9	1.2	4.4	5.7
East Asia and Pacific	11.4	8.0	5.0	6.6	7.8
China	13.0	9.0	6.5	7.5	8.5
Indonesia	6.3	6.1	3.5	5.0	6.0
Thailand	4.9	2.7	-3.2	2.2	3.1
Europe and Central Asia	6.9	4.0	-4.7	1.6	3.3
Russian Federation	8.1	5.6	-7.5	2.5	3.0
Turkey	4.7	1.1	-5.5	1.5	3.0
Poland	6.7	4.8	0.5	0.9	3.5
Latin America and the Caribbean	5.8	4.2	-2.2	2.0	3.3
Brazil	5.7	5.1	-1.1	2.5	4.1
Mexico	3.3	1.4	-5.8	1.7	3.0
Argentina	8.7	6.8	-1.5	1.9	2.1
Middle East and North Africa	5.4	6.0	3.1	3.8	4.6
Egypt, Arab Rep. of <sup>g</sup>	7.1	7.2	3.8	4.2	5.0
Iran, Islamic Rep. of <sup>g</sup>	6.2	6.9	2.5	3.0	4.0
Algeria	3.0	3.0	2.2	3.5	4.0
South Asia	8.4	6.1	4.6	7.0	7.8
India <sup>g</sup>	9.0	6.1	5.1	8.0	8.5
Pakistan <sup>g</sup>	6.4	5.8	1.0	2.5	4.5
Bangladesh <sup>g</sup>	6.4	6.2	5.0	4.5	5.0
Sub-Saharan Africa	6.2	4.8	1.0	3.7	5.2
South Africa	5.1	3.1	-1.5	2.6	4.1
Nigeria	6.3	5.3	2.9	3.6	5.6
Kenya	7.1	1.7	2.6	3.4	4.9

Source: World Bank

Notes:

PPP = purchasing power parity; e = estimate; f = forecast

e. GDP in 2000 constant dollars; 2000 prices and market exchange rates.

f. GDP measured at 2000 PPP weights.

g. In keeping with national practice, data for the Arab Republic of Egypt, the Islamic Republic of Iran, India, Pakistan, and Bangladesh are reported of a fiscal year basis.

### Table 3: Economic Outlook

IMF Outlook better and India, China to lead Asian Recovery...

	GDP in percent	
	2009	2010
World	-1.1	3.1
Advanced economies	-3.4	1.3
United States	-2.7	1.5
Japan	-5.4	1.7
Euro zone	-4.2	0.3
Germany	-5.3	0.3
Britain	-4.4	0.9
France	-2.4	0.9
Central and East. Europe	-5.0	1.8
Russia	-7.5	1.5
Emerging economies	1.7	5.1
China	8.5	9.0
India	5.4	6.4
Latin America	-2.5	2.9
Middle East	2.0	4.2

**Responses were extensive and widespread, especially using stimulus package...**

- **Bank bailouts. Government interventions – “nationalisation”. TARP in US. Shore-up banks to encourage lending.**
- **Deposit insurance schemes expanded. Recapitalisation of banks. Equity positions. Extended-securities as collateral. Huge funds to banks. Government Guarantees Wrote downs of US\$4.1 (IMF).**
- **Monetary conditions eased. Interest rates reduced and average of 180 basis points in high income economies since mid-September 2008. “Quantitative easing”.**
- **Developing countries have also eased interest rates.**
- **Fiscal policy for stimulus. Countercyclical spending. Fiscal deficits of many countries will rise in 2009. Largest stimulus package (SP) for Spain, US, Australia, UK ranging from 2-2.3 percent of GDP. Small SP for France, Germany and Italy.**

## **Revival of interest in new financial architecture...**

- **Multilateral institutions – World Bank, IMF.**
- **Global governance.**
- **Regional institutions – ASEAN and East Asia.**
- **Excessive risks and corporate remuneration.**