Seeing some green on tickers around the world, as opposed to the red that was flashing last week, sure feels good. Credit market conditions also appear to be easing somewhat with respect to last week. Moreover, oil prices a good indicator of markets willingness to take risk lost steam. But is this a just a blip or are we at the turning point?

Over the weekend G7 governments agreed to address this global financial crisis in a coordinated manner, laying out a set of common objectives and principles so that each country could define its own special local financial program.

Here are the main policy actions that will be undertaken:

- Preventing systemically important banks and broker dealers from going bust by taking decisive action and use all available tools to support systemically important financial institutions and prevent their failure as in the G7 statement
- Recapitalization of banks and broker dealers via public injections of capital via preferred shares i.e. partial nationalization of financial institutions. Ensure that our banks and other major financial intermediaries, as needed, can raise capital from public as well as private sources, in sufficient amounts to re-establish confidence and permit them to continue lending to households and businesses
- Temporary guarantee of bank liabilities: all deposits, possibly interbank lines (along the lines of the British approach; see here for U.S. and for Eurozone approach), likely other new debts incurred by the banking system. Ensure that our respective national deposit insurance and guarantee programs are robust and consistent so that our retail depositors will continue to have confidence in the safety of their deposits
- Unlimited provision of liquidity to the banking system and to some parts of the shadow banking system to restore interbank lending and lending to the real economy. Ensure that our banks and other major financial intermediaries, as needed, can raise capital from public as well as private sources, in sufficient amounts to re-establish confidence and permit them to continue lending to households and businesses
- Provision of credit to the corporate sector via purchases of commercial paper (certainly in the U.S., possibly in Europe)
- Purchase of toxic assets to restore liquidity in the mortgage backed securities market (U.S.). Take action, where appropriate, to restart the secondary markets for mortgages and other securitized assets. Accurate valuation and transparent disclosure of assets and consistent implementation of high quality accounting standards are necessary
- Implicit triage between distressed banks that are solvent given liquidity support and capital injection and those that are non-systemically important and insolvent that will need to be closed down/merged/resolved
- Use of the IMF and other international financial institutions to provide lending to many emerging market economies and some advanced ones such as Iceland that are now at risk of a severe financial crisis.
- Use of any other tools that are available and necessary to avoid a systemic meltdown, including implicitly more monetary policy easing as well as possibly fiscal policy stimulus. We will use macroeconomic policy tools as necessary and appropriate

More details of European financial support programs are being flashed out. As the European governments disclosed plans to invest more than $2.5 trillion into the European financial system, the U.S. authorities announced a plan to rescue frozen credit markets that includes spending **$250bn out of the $700bn already allocated for ownership stakes in nine major banks** who have already agreed to participate.

The markets are certainly greeting the policy makers response with some optimism; however we might not be out of the woods quite yet.

The process of deleveraging is still ongoing and, on the real side of the economy, the measures adopted so far might reduce the severity and the length of the U.S. (and global) downturn but will not avoid it. A recession in the U.S. likely started a long time ago. U.S. home prices are still falling and will not find a floor as long as demand for homes keeps falling faster than supply and inventories stay at record highs. U.S. personal consumption might exhibit negative growth in Q3 2008 for the first time since Q4 1991 and with personal consumption making up over 70% of U.S. aggregate demand, Q3 2008 real U.S. GDP growth could very well turn out negative. Private investment, both residential and capex, has been falling for quite some time. Unemployment is high and rising.

The old saying that when the U.S. sneezes the rest of the world catches a cold seems to still hold. Most of the other G7 economies have already experienced a quarter of negative growth and are navigating toward recession. A G7 recession coupled with a marked slowdown of large emerging economies can realistically translate into a global recession.

According to our Nouriel Roubini two essential components are still missing among the measures adopted so far. The fist one would be a large fiscal stimulus plan in the form of old fashioned traditional Keynesian spending to boost aggregate demand. If such a fiscal stimulus plan is not rapidly implemented any improvement in the financial conditions of financial institutions that the rescue plans will provide will be undermined in a matter of six months with an even sharper drop of aggregate demand that will make an already severe recession even more severe. The second one is a plan to reduce the debt overhang of distressed households via the institution of a new Home Owners Loan Corporation (HOLC) or better a Home Owners Mortgage Enterprise (HOME).